How to Avoid Losing Money in a Bear Market

**Description**

Last year, I proudly took profits in a number of growth stocks. I would sound smart if that were the end of the story. It's not. I ended up re-allocating the proceeds into other growth stocks that were less expensive. Fast forward to today, and many of my growth stock holdings are in the red.



It doesn't take a bear market for investors to lose money. All it takes is selling your holdings under the water when there's a major correction in certain stocks you hold. Recent examples include growth stocks such as tech stocks and Chinese stocks, including a bunch of them that are listed as ADRs on U.S. exchanges.

I already had some rules in place to prevent myself from losing money. In hindsight, there's much more I could do to make my investing journey to retirement less bumpy. I reflect upon and combine my past and recent experiences to come up with the following tips.

## Have a long investment horizon

When you have a long-term investment horizon, you can sit through market volatility, including terrifying market crashes. You should never put cash in the stock market if you need to use the money over the next few months or even year. A long-term investment horizon is at least three to five years.

Market recoveries are usually much slower than market corrections. For example, the pandemic market crash on the Canadian stock market took roughly a month to fall 32% from peak to trough. It took approximately nine months to return to the high. After breaking the high, the Canadian stock market continued to grind higher with little dips. That said, selective areas of the market have fallen and other parts rallied. The tech stock bubble burst is one painful experience investors are still experiencing.

## Only buy profitable businesses

I could have avoided most of the tech stock bubble if I focused on buying profitable businesses only.

Having revenue doesn't imply a profitable business, although having revenue is the first step. Ultimately, a business is considered profitable if it reported net income (versus a net loss).

I remember pundits talking about high-flying tech stocks that just kept going higher. And they were talking about the stocks in terms of price to sales. For example, **Shopify** stock traded as high as 50 times *next 12-month* sales at one point in 2020. I didn't really pay close attention at the time as I had a small position. But I probably should have because the bubble finally burst this year. I'm sorry to pick on Shopify, but it is the most prominent growth name I can think of. But really, the bubble burst for many other growth stocks as well.

In any case, traditionally, investors should look at the price-to-earnings (P/E) ratio of a company when they initially value the company. If a stock isn't profitable yet, it's generally safer to avoid it altogether. Needless to say, other performance metrics should also be studied carefully for the same company over time as well as compared to peers to determine which may be a better investment.

## Watch the valuation

I kind of touched upon this in the previous section. When you study a potential stock investment with a trading history, you can compare their P/E over time as well as how stable their earnings are. By trying to pay a reasonable valuation on the stock versus overpaying, you have a better chance of making a profit over the next year to five years.



You can also check with the analysts' 12-month consensus price target, which is likely available at the bank that you trade at or at a financial media site like Yahoo Finance. Depending on the stock in question, I would aim for a discount of at least 20-40% before I consider making a purchase. The higher the risk of a stock, the greater the discount I demand.

## Dividends help

Holding stocks that pay out safe dividends significantly helps investors pull through bear markets. This is why I hold a bunch of dividend stocks as core holdings. Often, these dividend stocks also have the capability to increase their dividends over time.

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