How Should You Invest in a Highly Volatile Bear Market?

Description

The **S&P 500** index entered bear market territory on June 13 over concerns surrounding the Federal Reserve's potential rate hikes and the threat of an economic recession. A bear market is triggered after a benchmark index declines 20% from all-time highs. The tech-heavy **Nasdaq Composite** Index plummeted 30% year to date, as the tech sector remains the worst affected by the extended market correction and macro headwinds.

The Canadian benchmark **S&P/TSX 60 Composite** index has fared relatively better due to its heavy exposure to commodities. The surging commodity prices on the back of global shortage and supply chain disruptions amid the Russia-Ukraine war have allowed the Canadian stock market to perform relatively better compared to its western counterparts.

The TSX index has declined 10.45% year to date, entering correction territory. Falling commodity prices and a weakening loonie caused the index to plummet last week. Moreover, as the Bank of Canada gears up to hike interest rates to offset inflation hovering near 40-year highs, investors have been growing increasingly concerned regarding a potential recession, causing TSX to decline 253.25 points yesterday.

However, the current bear market has a silver lining, as quality stocks with immense upside potential are trading at a fraction of their intrinsic value. Knowing the various investment strategies and identifying value stocks can help investors build a robust equity portfolio.

Dollar-cost averaging

Dollar-cost averaging allows investors to spread out their total investment over a period of time, therefore hedging risks associated with market volatility. For example, buying 20 shares of **Shopify** (TSX:SHOP)(NYSE:SHOP), each month over six months rather than buying 120 shares in a lumpsum purchase right now can be beneficial, especially in a bear market.

Shares of Canadian tech giant Shopify are down 80% from all-time highs but have also returned 1,220% to investors since its IPO in May 2015. The downturn offers investors an opportunity to buy a quality stock at a lower multiple.

As it is tough to time the markets, investing in stocks in equal installments spaced out over a period of time can reduce the initial cost of investment, while enabling investors to limit the risks associated with market volatility.

Invest in defensive stocks

Bear markets tend to spook investors, as they typically steer clear of equities amid declining stock prices during such times. However, defensive stocks are known to hedge such risks as well as provide a steady income stream to shareholders through dividends.

Blue-chip, defensive companies generally operate in sectors that have pricing power. As a result, they typically have stable cash flows and profit margins. Also, most publicly traded defensive companies distribute dividends periodically, providing a steady income stream during a bearish market backdrop.

iShares S&P/TSX Capped Consumer Staples Index ETF and **Fidelity International High Quality ETF** are examples of two popular defensive ETFs that can generate steady returns, even during a market downturn.

Rebalance your portfolio

Diversification is the key to surviving a bear market, as the saying goes, “Don’t put all your eggs in one basket.” Looking at the broader industry trends and macroeconomic factors can help determine the crucial industries.

For example, given the current market backdrop, commodity markets and semiconductors are major market movers, while the technology industry seems to be in a rut. Thus, investing in fundamentally sound commodity stocks, such as fertilizer manufacturer **Nutrien** and oil and gas company **Enbridge** can help you generate robust returns, even during a bear market.

However, as tech stocks seem disproportionately affected by the aggressive rate hikes, investors should avoid them at the moment.

The Foolish takeaway

Tracking the portfolios of institutional investors can help investors identify value bargains right now. Following these investment strategies should allow traders to generate hefty returns, even during an extended market meltdown.

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