How to Start Investing in a TFSA in a Down Market

Description

As of this writing, the **TSX** has fallen nearly 12% since the start of the year. Although that's not exactly in "correction" territory, we're certainly knocking on the door. With how weak the market's been, many investors have become hesitant to invest. This is especially true when it comes to TFSAs, because Canadians have a limited amount of contribution room available. In this article, I'll discuss how you should be investing in a TFSA in a down market.

Don't wait

The first thing that investors should keep in mind is that they shouldn't wait. Sitting on the sidelines could leave you missing some of the market's best days. In fact, missing just a few of those best days could significantly decrease your returns.

A recent study by Putnam Investments looked at a 15-year period. They found that by investing $10,000 into the **S&P 500** on December 31, 2006, investors would have seen that position grow to become $45,682 if they remained fully invested through that period. That represents an annualized return of 10.66%.

However, if an investor tried to time the market and ended up missing the 10 best days over that period, that position would only be worth $20,929. That represents an annualized return of 5.05%. Missing the 10 next best days over that period (20 days in total) would result in an annualized return of about 1.59% over those 15 years. Investors would start to see negative returns if they missed the 30 best market days over that 15-year period.

Studies like these are further proof that time in the market is better than timing the market. If you're anxious about investing during a down market, you can always start investing with small amounts of capital. The important thing to remember is, don't wait.

Consider index funds

Investors can also consider buying index funds. These are similar to mutual funds in that they're often structured as a basket of companies. That spreads risk across a larger number of companies, with the goal of making the position less volatile. This could be a good idea for new investors and investors that want to minimize downside in their TFSA.

One thing to keep in mind is that some of these funds could have very high fees. Generally, index funds that target certain industries or have a specific strategy will charge higher fees than funds that track the TSX or the **S&P 500**. Regardless, those high fees are generally much lower than the fees investors would be paying on a mutual fund.

In addition, index funds are much more liquid than mutual funds. This makes it easier for investors to buy and sell shares in an instant. However, at the Motley Fool, we encourage a buy-and-hold investment style. That means investors shouldn't do too much short-term trading in general, and especially in a down market.

Buy blue-chip stocks

Finally, investors should stick to buying shares of blue-chip stocks in a down market. Many popular blue-chip stocks tend to be less volatile than the broader market. The utility and industrial sectors would be an excellent place to start, since those sectors tend to feature essential companies. By that, I mean companies whose businesses don't tend to experience a significant decrease in demand during down markets.

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