Flight to Safety: Is History Repeating Itself?

- The stock market tumbled more than 50% since its peak in 2007, causing many investors to flee to cash.
- At the end of 2008, the percentage of all mutual fund assets invested in money-market funds (37%) stood at its highest level on record, surpassing the previous peak during the bear market of 2002 (34%).
- Fleeing to cash during a bear market reduces one's exposure to stocks when they are at historically lower prices.
- Back in October 2002, although a new bull market had begun, investors kept an above-average level of cash until February '04—meaning in the aggregate, investors over-allocated to cash during a 15-month period when stocks rose more than 30%.
- As a result, some investors who kept long-term capital tied up in cash likely missed out on big gains in the early stages of a rebound.

The Bottom Line: Ineffective Market Timing Can Be Costly

- Historically, many investors overcome with fear have increased cash positions during bear markets but have been slow to reallocate to stocks in the early stages of a new bull market.
- This sell-low, buy-high behavior is a sub-optimal strategy, and can cause investors to end up with returns that are worse than the market's average performance.

Investing involves risk. Decisions should be based on an individual's own goals, time horizon, and risk tolerance.