

The high cost of cashing out



When the stock market declines, moving to cash can be a tempting option for investors seeking a respite from volatility. However, cashing out of a down market could come at a cost.

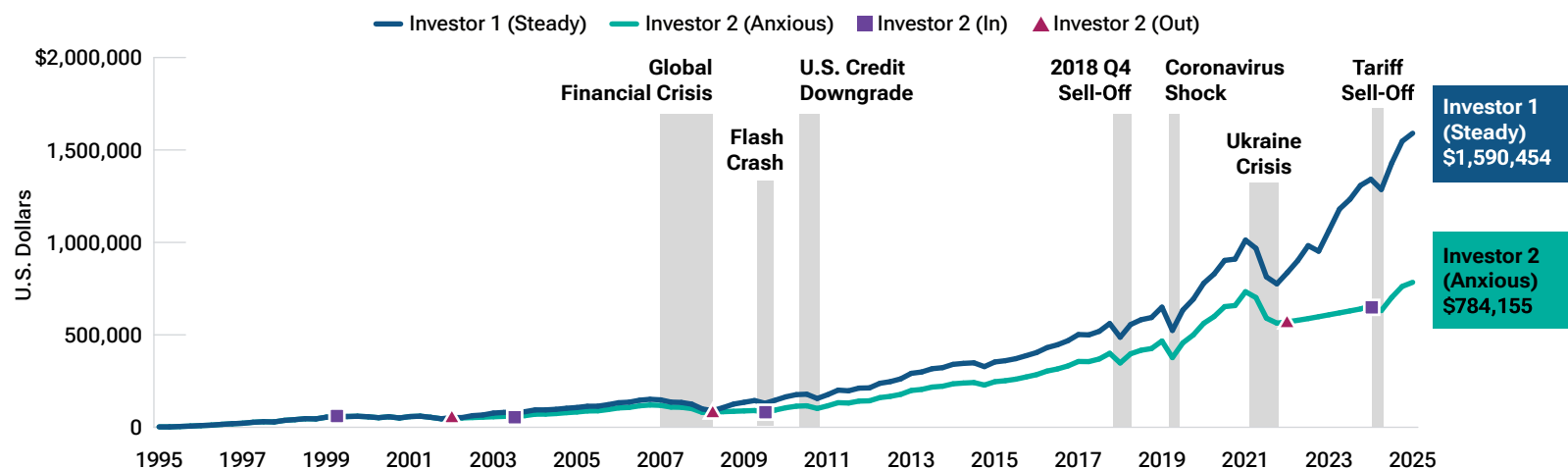
A tale of two investors

To see the benefit of staying invested through varying market conditions, let's consider two hypothetical investors. Both investors contributed U.S.\$2,000 each quarter to their investment accounts.

Investor 1 kept their money and ongoing contributions invested, riding out the stock market's ups and downs. **Investor 2** moved their account balance and contributions to cash when stocks dropped 20% or more in a quarter OR a cumulative drop of 20% over two quarters. They felt comfortable putting money back into equities only after four consecutive quarters of positive returns. This behavior was repeated throughout three market cycles.

The 30-year market performance of Investor 1 and Investor 2 from 1995 to 2025

(Fig. 1) In this example, two investors with identical portfolios achieve vastly different returns based on their decisions to either stay invested during periods of volatility or repeatedly exit and reenter the market. Both investors started investing in 1990 in the same portfolio. By September 30, 2002, both investors have U.S.\$46,144. Starting in the fourth quarter of 2002, Investor 1 continued to invest the same way and Investor 2 decided to avoid steep losses and exited the market. There were three in-out cycles starting with 2002.



Past performance is not a guarantee or a reliable indicator of future results. It is not possible to invest directly in an index. Chart is shown for illustrative purposes only. Investor 2, the anxious style of investor, is assumed to be invested in three-month Treasury bills as a cash equivalent. The U.S.\$2,000 contributed each quarter in this example assumes minimal interest earned. The anxious style of investor also assumes that cash is invested in Treasury bills during those periods when it is not invested in the stock market. The performance of stocks shown is that of the S&P 500 Stock Index, which measures the performance of large-capitalization companies that represent a broad spectrum of the U.S. economy. Sources: T. Rowe Price and S&P. See Additional Disclosure.

Investor 1 sticks to their investment strategy despite market fluctuations and chooses to remain invested at all times.

Investor 2 becomes anxious during volatile market conditions, causing them to periodically exit (▲) and reenter (■) based on short-term performance.

How investor behavior impacts long-term returns

While both investors saw their portfolio balances decline during downturns, they continued to contribute to their accounts. Investor 1 took advantage of lower stock prices through their ongoing contributions and was rewarded as the market recovered. Investor 2 earned less than half of what the steady, long-term investor earned by the end of the period. Investor 2 exited before the market had the opportunity to correct, essentially locking in their investment losses. Doing so eliminated the opportunity to benefit from a recovery.



Investor 1 took advantage of lower stock prices through their ongoing contributions and was rewarded as the market recovered.

U.S.\$1,590,454



Investor 2 earned less than half of what the steady, long-term investor earned by the end of the period.

U.S.\$784,155

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In times of stress, we feel the need to do something—even when the best course of action may be to stick with the plan we already have.

– Stuart Ritter, CFP®
Insights Director

Additional Disclosure

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