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KEY POINTS

- The 2008 financial crisis was the worst recession since the Great Depression.
- Some investors reacted to the downturn in ways that still could be holding them back today.
- Individuals who stayed focused on the fundamentals of investing have found themselves back on track.

10 Years Later

Learning from the worst market downturn in generations can help chart a better path forward.

History teaches lessons, but we only gain insights after we've worked to understand what really happened. Ten years ago, the economy was in the middle of the worst recession since the Great Depression, and equity markets were in freefall. The international banking crisis and the bankruptcy of Lehman Brothers were part of a stock market crash that would continue for several more months.

"The financial crisis offered people the opportunity to learn valuable lessons about the fundamentals of investing," says Stuart Ritter, CFP®, a senior financial planner with T. Rowe Price. "Unfortunately, some reached the wrong conclusions—which still could be holding them back from reaching their future goals."

PHOTOGRAPH BY BEE32

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>
> – **STUART RITTER, CFP®**, SENIOR FINANCIAL PLANNER WITH T. ROWE PRICE

Looking back

Investors experienced a financial one-two punch in the form of falling home prices and declining portfolio values. For some, financial lives were turned upside down, with seemingly no relief in sight. With the benefit of hindsight, we know the market hit bottom on March 9, 2009, but in late 2008, there was little to be confident about.

The S&P 500 Index recouped losses by November 23, 2012, roughly three and a half years after the market bottom. Unfortunately, not every investor chose to ride out the downturn. In addition to locking in their losses, those who acted on their emotions still may be holding on to fear-based investment mind-sets. (See “4 Post-Financial Crisis Mind-Sets” on page 3.)

Embracing the lessons

Consider the following reactions some investors may have had during the 2008 financial crisis and valuable investing lessons that have held true in the decade since the downturn:

2008 Reaction: Stocks are too risky.
Investing Lesson: Short-term volatility doesn't negate the long-term growth potential of stocks.

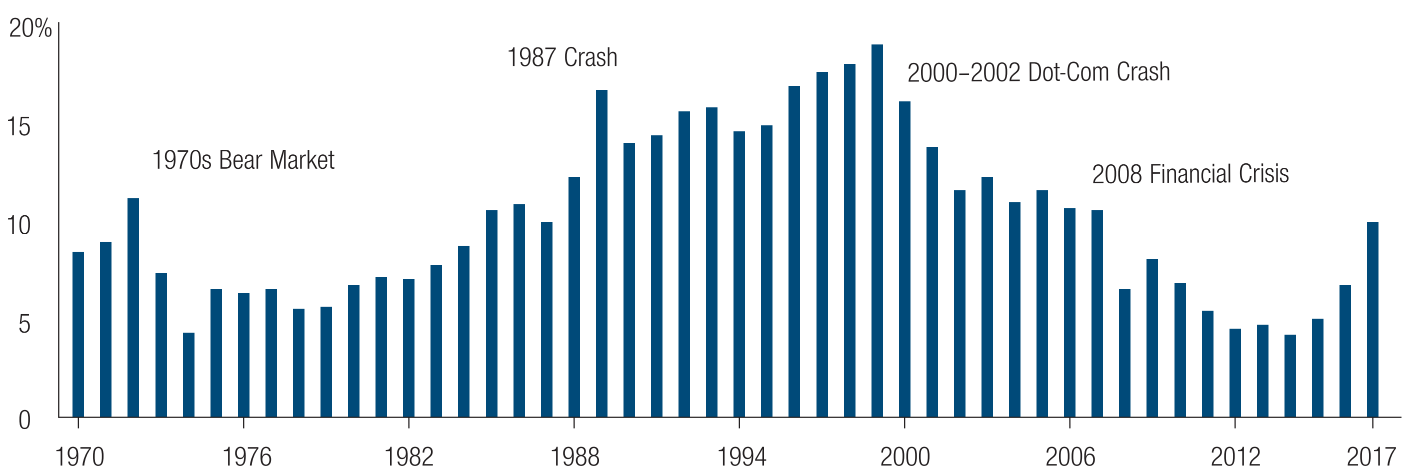
Staggering declines in the S&P 500 Index shocked inexperienced and seasoned investors alike. Individuals faced a difficult choice to either remain invested without knowing when the markets would go back up or to get out in an attempt to avoid further losses, but with the consequence of missing out on subsequent gains.

Investors who exited the market during the downturn still may not have recouped their losses despite record market highs 10 years later. Meanwhile, the S&P 500 has earned an average annual return of 7.6% since the market peak before the downturn.[1]

Steady Gains Over Time

The S&P 500 Index has never lost ground during any rolling 15-year period starting back in 1926—and, as shown in the chart, the many recent financial crises haven't changed this fact.

Annualized returns over 15-year periods ending between December 31, 1970, and December 31, 2017



Past performance cannot guarantee future results. Charts are shown for illustrative purposes only and are not indicative of any specific investment. Investors cannot invest directly in an index.

[1]S&P 500, October 9, 2007, to May 31, 2018.

7.6%

The average annual return the S&P 500 has earned since the market peak before the downturn.[1]

It's important to remember that the markets have recovered from every downturn. In fact, stocks have produced positive returns in every rolling 15 calendar year period since 1926. (See "Steady Gains Over Time" on page 2.)

2008 Reaction: Saving in stocks for retirement isn't worth it if the market will just crash again.
Investing Lesson: By steering clear of the stock market, people potentially miss more in gains than they avoid in losses.

The market decline resulting from the 2008 financial crisis effectively erased a decade's worth of gains. The markets recovered, but this only benefited those who remained invested. Individuals who sold their stock holdings, despite potentially many years until retirement, locked in their losses and missed out on the subsequent gains. "The downturn decreased people's account balances; but it was the choice to sell out of stocks that made that decrease permanent and kept retirement account balances low," explains Ritter.

The fact is, despite back-to-back crises in 2001 and 2008, the stock markets have recovered to record highs. (See "A Decade Found" on page 4.) Since just before the 2008 crisis, the inflation rate has averaged 1.8% per year, which means that stocks have delivered the annual growth necessary to keep retirement assets growing more than inflation.[2]

2008 Reaction: Day-to-day volatility matters.
Investing Lesson: Long-term results from a well-diversified and properly allocated portfolio are what really matter.

4 Post-Financial Crisis Mind-Sets

All investors feel emotions, but some let those emotions influence their actions, leading them to draw the wrong conclusions from the 2008 downturn:

Too Cautious
Those who exited the markets in 2008 and are still too fearful to get back in.

Market Watching
Those who focus on what the markets are doing in the short term (and not the long-term performance of their own portfolios) and react to headlines by constantly adjusting their investments.

Enticed and Chasing
Those who think they know better now yet still keep chasing the next big thing, whether it be tech stocks, real estate, gold, or cryptocurrencies.

Complacent
Those who assume stocks are supposed to keep rising steadily and have allowed themselves to remain too heavily exposed to stocks despite a shorter time horizon and the risks of short-term volatility.

Many investors experience these mind-sets from time to time. What sets some apart is that they also know how to stick to their plan despite these emotions.

[2] U.S. inflation, October 2007 through April 2018.

"Throughout the crisis, media headlines called out various one-day market declines as if they represented important news for all investors, as well as a trend that would continue indefinitely," recalls Ritter. "Such was the level of alarm being raised at the time."

The headlines stoked fear based on an assumption that individuals were invested entirely in, or had a high allocation to, U.S. equities and that the day-to-day volatility was something they should react to. What these headlines omitted, however, was that properly allocated investors with significant stock portfolios would have decades to recover from any market decline. "For many people, however, what they were reading in the headlines wasn't what was happening in their portfolios," says Ritter. "Investors with shorter time horizons likely had exposure to bonds and even cash to help buffer the declines they experienced in their equity portfolios."

Markets regularly cycle through periods of less and more volatility. This pattern is why maintaining an asset allocation that is appropriate for your time horizon is so important—not to mention sticking to your plan regardless of what part of the volatility cycle you find yourself in.

The fundamentals of investing

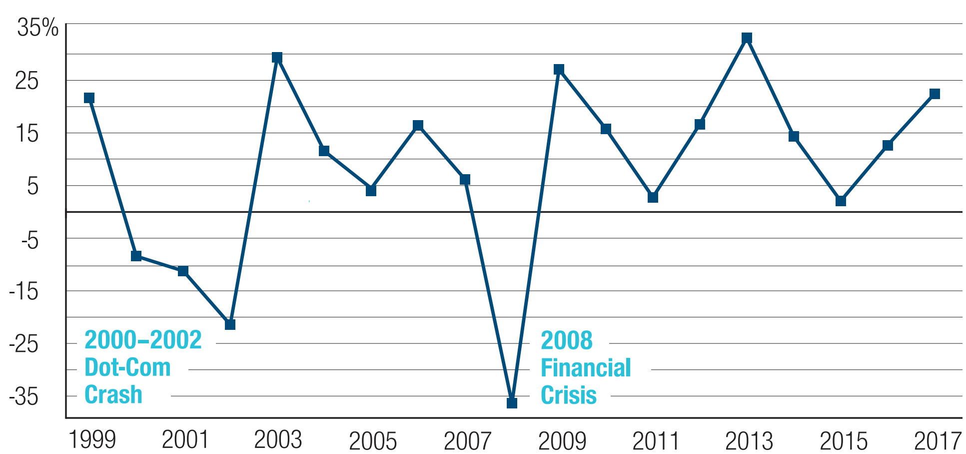
There is no doubt that the 2008 financial crisis was unsettling for many individuals. At the same time, past fears should not change a sound approach to investing. As markets do what they do, the best strategy is still the one that has helped investors weather every market crisis to date: Stick to the fundamentals.

Investors who stayed focused on the principles of sound investing—namely, an appropriate asset allocation based on time horizon and risk tolerance, along with a well-diversified portfolio—have found themselves back on track with their savings despite the worst market downturn in generations. "The real lesson to take away from the 2008 financial crisis is not that the fundamentals of investing need to change," says Ritter. "It's that those fundamentals really do work."

A Decade Found

The media touted the Lost Decade in the wake of back-to-back market downturns in the early and late 2000s, but few have bothered to note that in the 10 years since the 2008 financial crisis, markets have rebounded strongly.

Annual total return for the S&P 500 Index



Past performance cannot guarantee future results.

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