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Noel Swain: The Stock Market: When to Get Out

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Mike, a financial adviser friend, told me recently that the stock market was climbing way too quickly, and if the market lost ground three days in a row, he was going to take all of his clients out of it.

I asked him, and he confirmed, that was his only criteria for getting his clients out.

The Dow had pierced both the 25,000 and 26,000 levels just before we had this conversation. At the end of the month, the Dow had two bad days, a good day, then two more bad days, losing about 8½ percent over that six-day trading time.

Mike has since moved most of his clients' investments to cash. I guess because of the severity of the market swing he decided to forgo the "three down days in a row" rule and start getting his clients out of equities.

A few days ago, I asked him what his plan was to get his clients back into the market. His reply was, "I dunno, maybe 22,000."

I like Mike. He's a good friend. But I don't want him managing my retirement account.

Using emotion and arbitrary numbers to get in or out of the stock market is, in my opinion, a sure recipe for poverty. But when people get frightened of the market, their emotions normally overrule their good sense.

It's sad, but many financial advisers manage that same way. As much as we may like to pontificate, we advisers (just like everyone else) don't really know what the markets will do tomorrow. So if our clients get frightened, we too may panic if we have no strict discipline for deciding what we'll do when the stock market turns volatile.

When it's going straight up, one needs very little discipline to do well. Just keep investing. Since 2009, it has for the most part done just that.

On March 9, 2009, the Dow Jones Industrial Average reached its lowest point after a seventeen-month drop from 14,165 to 6,547.

Since then, the Dow – with few interruptions – has climbed more than 20,000 points to reach 26,617 on Jan. 26, just a few days ago.

Will the market crash from here, or will it resume its pace of the last nine years and climb on to 30,000 or 40,000 before we have another recession?

Again, nobody knows. What we do know, however, is that having a plan in place for what you will do in either case is the only way to protect yourself from emotionally charged investing.

If you do your own investing, I recommend that you make a plan for when you will sell out or buy into the market. Resolve that you will stick it out no matter what the market does.

And if you have a financial adviser, I recommend that you ask him or her to explain their buy-and-sell discipline to you, or if they plan to keep you invested even through a withering, gut-wrenching market sell-off.

Having a plan based on reliable research and your own risk tolerance may be the best way to preserve and grow your retirement assets.