What Do Stock Market Jolts Mean for My 401(k)?

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You may remember a few weeks back that the stock market had a record setting run, with the Dow setting an all-time closing high of 15,676 on Sept. 18. But what does that mean for average investors like you?

There's no shame in not having a perfect understanding of what the stock market's record means -- if you didn't major in finance or work on Wall Street, financial markets can seem confusing and opaque. One of your first questions on hearing the news of the record-breaking market highs may have been: "What does this mean for my 401(k)?" As you know, your retirement savings aren't sitting in a static account, but are invested in a low-risk way, probably across several different asset classes including stocks. However, you may be surprised how little of an effect the high stock prices will have on your retirement nest egg. We got a few experts to weigh in on the topic:

You can't time the market, so don't try! Seeing a soaring stock price and reacting to it by changing an investment strategy is not what sophisticated investors are in the business of doing. While financial media may show an image of panicked stockbrokers scurrying around the trading floor whenever there's a big market move, seasoned professionals will tell you that emotional, reactive investing is a bad idea. Set up a low-risk, long-term retirement strategy -- and don't change it based on what you see on TV. Financial advisor Mike Kwon, principal of Steward Advisors, based in Glen Ellyn, Ill., said making calls about the short-term future is just too unpredictable. "Too many people see stock prices go up and jump in wanting those gains. When the market falls, too many panic and react doing the wrong thing by selling," he said. "Investors should have an individual written investment policy that provides a framework to guide personal investment decisions with a disciplined plan."

Tune out the media and stay the course. "Today, more investors are being overloaded with information about market performance," said Chris Alman, financial planner and investment manager at Charles D. Jones Capital in Fairhope, Ala. "There is so much chatter and noise coming from the media, that it's hard not to hear it. What I tell clients, whether they are in the accumulation phase or preparing to enter retirement, is that it is critical to filter out the noise and take a disciplined approach to investing." That means not selling your low-risk bonds and piling into equities just because CNBC is making it sound like you would be a fool not to. "I remind my clients that these trends in market performance are exactly that -- trends," Alman added. "Trends always come and go. That's why they're called trends."

It's never a bad time to review your allocation. The same amount of risky investments is not appropriate for a person who is just setting out to save, and for someone who is looking to retire soon. When you're young, your allocation should be tilted towards risky and high-yielding investments, and when you get older, your portfolio should be slow and steady. You don't have to review this manually, however: many 401(k)s offer automatic rebalancing. Financial advisor Patricia Jennerjohn, managing partner of Focused Finances in Oakland, Calif., said she advises clients to research if their 401(k) offers the automatic feature. "When markets hit highs and lows, or when the portfolio naturally drifts over time, the rebalancing feature will be sure to sell and purchase the appropriate assets to keep their allocation on target -- this automates the process of buying low and selling high -- a process that works beautifully," Jennerjohn explained. "Buying low and selling high is certainly common sense, but during market turmoil, our emotions can get in the way of executing this strategy; we tend to freeze up, or actually sell what has gone down and chase what is going up -- wrong! Automatic rebalancing keeps emotions out of the process."

It's not about highs and lows. Think about costs to invest, portfolio diversification and exposure to risks. Financial advisor Robert Riedl, director of wealth management at Endowment Wealth Management in Appleton, Wis., said that he informs his 401(k) clients that they can't control the short-term market returns and volatility, but they can control their costs of investing, portfolio diversification, exposure to interest rate risks, exposure to inflation risks and the execution of their long-term retirement plan. "We educate them to look at their 401-k account as two separate investments," Riedl explained. "The first being their accumulated account balance and the second being their future twelve months of monthly contributions. The accumulated balance we set an appropriate risk profile of say 70 percent stocks and 30 percent bonds, but on their future contributions we invest 100 percent in stocks to take advantage of dollar cost averaging in to the market and benefiting from the short-term market moves."

So next time the TV has you digging out your last 401(k) plan statement, think twice. Your retirement savings are in the market for the long-haul, and short-term gains are not a good basis for changing course.

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