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Stocks strategies when markets takes a tumble

Investment pros: Don't panic after a sell-off, but examine your risks

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At one point during Tuesday's sell-off, the Dow Jones Industrial Average was down 500 plus points for the day—500 of anything is a lot and certainly when it comes to the index, it gets the attention of even the most seasoned investors, though not necessarily a reaction.

"The 500-point drop in 1987 taught me not to do anything drastic when the market declines, and certainly not to buy anything on margin," says Jim Clark, a retired financial services executive, now a private investor in Calabasas, Calif. who suspects mid-day margin calls may have fueled the worst of the sell-off. With his holdings down almost 5 percent with an hour of trading left in the day, he offered that while it was not a good day, it was far from tragic.

"There is a big difference between a technical correction and the type of fundamental correction we experienced in 2000 when the bubble in tech stocks burst," says Tim Traff, managing partner of Desert Springs Investments, a private investment firm in Minneapolis, Minn. "What we are currently experiencing is a technical correction. That is a 'good correction,'" he adds, equating it to the aggressive 10 percent correction the market experienced in the spring of 2006. He expects similar results.

"Since the stock market hit its low last summer, we have gone roughly seven months without a correction. Today's action was simply overdue, and something many professional investors were positioned for," he adds.

That may explain why the market bounced back up from its 500 plus point deficit to finish down a still eye-catching 416 points on the day.

For Traff's money and his investors', he is not expecting much more than a 5 to 10 percent correction when all is said and done. The reason: the overall good health of the economy and the U.S. Markets. "Interest rates and oil prices are steady; the price of gold looks firm; real estate prices are self-correcting; and U.S. stocks headed into this correction neither expensively nor cheaply priced. Today even China finally started correcting for the excesses in its market," says Traff.

In other words, the patient's vital signs are pretty healthy, despite a small panic attack.

Jim Ferrare, executive vice president of Pinnacle Associates in New York, similarly views the market sell-off as both expected and overdue: "Too many people were too complacent, too bullish and I suspect, exposed to too much risk."

While a day like Tuesday may cause investors to see nothing but red when they look at their portfolios' market value, it can also help them understand what having too much risk in their portfolios looks like.

"This is a great opportunity for individuals to rethink their portfolios' structure and lower the risk in their portfolios by reducing their exposure to the more volatile securities. They should be adding the types of issues that did not react to the downturn so drastically today," advises Ferrare.

At Legend Financial Advisors, based in Pittsburgh, Diane Pearson, director of financial planning for the wealth management firm reports that while clients may notice the alarming financial headlines they will not see much change in their portfolios. "Our portfolios are extremely well-diversified. It minimizes their exposure to this type of market volatility, she says. "Today's action was basically a hiccup for us."

"Though we did sell one stock today because it hit its price target and we did do some buying, the buying was planned, not a response to the market's activity. We do not let market moves make up our minds for us," says Pearson.

While it may have been the most exciting trading day in months, for investors with well-diversified portfolios and a lack of margin exposure, it was pretty much another day at the office.

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