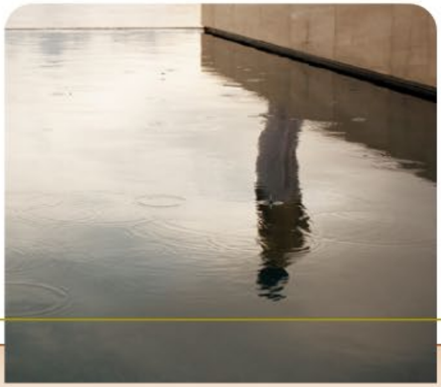
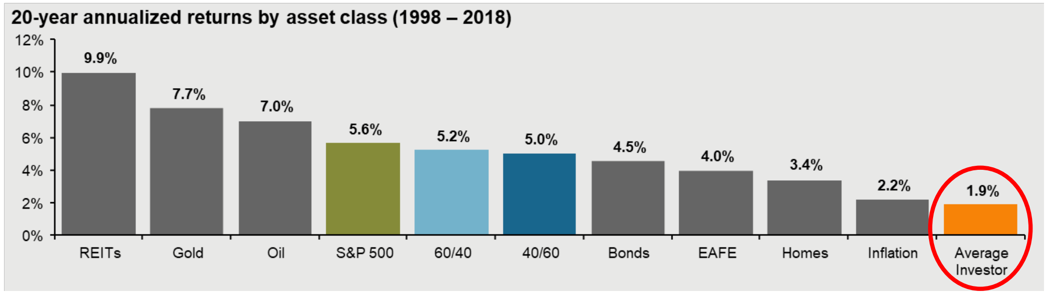
The 5 Basic Rules Equity Investors Need to Know

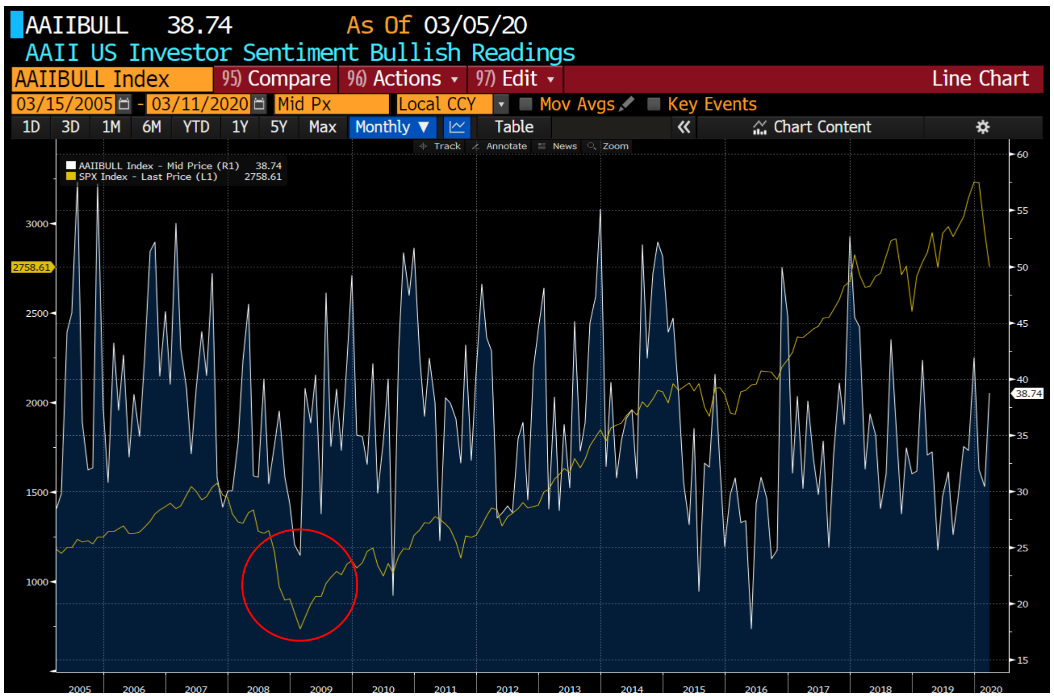


Phillips & Company

Wealth Strategies | Vested

Individual Investors Tend to Underperform





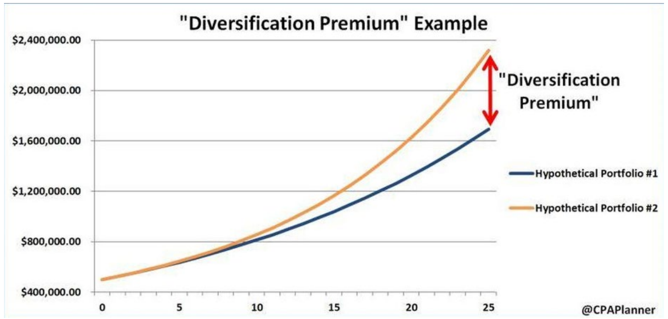
- ❑ As you can see, individual investors generally post weaker returns compared to those of both the broader market asset classes and balanced asset allocation portfolios.

- ❑ Generally speaking, those same investors tend to sell when they should buy and react when they should not. Just look at individual investor sentiment at the worst part of the financial crisis. Using the AAII Index, you can see individual investor sentiment is at its worst exactly when the market bottoms out, and then proceeds to take off on the historic bull market that we're still in today.

Sources: Bloomberg, https://am.jpmorgan.com/blob-gim/1383587507523/83456/MI-MB-Volatile%20Markets_4Q18_v2.pdf

Diversification: The Only Free Lunch in Finance

																2005 - 2019	
2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	YTD	Ann.	Vol.
EM Equity 34.5%	REITs 35.1%	EM Equity 39.8%	Fixed Income 5.2%	EM Equity 79.0%	REITs 27.9%	REITs 8.3%	REITs 19.7%	Small Cap 38.8%	REITs 28.0%	REITs 2.8%	Small Cap 21.3%	EM Equity 37.8%	Cash 1.8%	Large Cap 31.5%	Fixed Income 3.8%	Large Cap 9.0%	REITs 22.2%
Comdty. 21.4%	EM Equity 32.6%	Comdty. 16.2%	Cash 1.8%	High Yield 59.4%	Small Cap 26.9%	Fixed Income 7.8%	High Yield 19.6%	Large Cap 32.4%	Large Cap 13.7%	Large Cap 1.4%	High Yield 14.3%	DM Equity 25.6%	Fixed Income 0.0%	REITs 28.7%	Cash 0.3%	REITs 8.3%	EM Equity 22.1%
DM Equity 14.0%	DM Equity 26.9%	DM Equity 11.6%	Asset Alloc. -25.4%	DM Equity 32.5%	EM Equity 19.2%	High Yield 3.1%	EM Equity 18.6%	DM Equity 23.3%	Fixed Income 6.0%	Fixed Income 0.5%	Large Cap 12.0%	Large Cap 21.8%	REITs -4.0%	Small Cap 25.5%	High Yield -1.7%	Small Cap 7.9%	Comdty. 18.6%
REITs 12.2%	Small Cap 18.4%	Asset Alloc. 7.1%	High Yield -26.9%	REITs 28.0%	Comdty. 16.8%	Large Cap 2.1%	DM Equity 17.9%	Asset Alloc. 14.9%	Asset Alloc. 5.2%	Cash 0.0%	Comdty. 11.8%	Small Cap 14.6%	High Yield -4.1%	DM Equity 22.7%	Asset Alloc. -5.4%	EM Equity 7.8%	Small Cap 17.7%
Asset Alloc. 8.1%	Large Cap 15.8%	Fixed Income 7.0%	Small Cap -33.8%	Small Cap 27.2%	Large Cap 15.1%	Cash 0.1%	Small Cap 16.3%	High Yield 7.3%	Small Cap 4.9%	DM Equity -0.4%	EM Equity 11.6%	Asset Alloc. 14.6%	Large Cap -4.4%	Asset Alloc. 19.5%	REITs -5.8%	High Yield 7.2%	DM Equity 17.3%
Large Cap 4.9%	Asset Alloc. 15.3%	Large Cap 5.5%	Comdty. -35.6%	Large Cap 26.5%	High Yield 14.8%	Asset Alloc. -0.7%	Large Cap 16.0%	REITs 2.9%	Cash 0.0%	Asset Alloc. -2.0%	REITs 8.6%	High Yield 10.4%	Asset Alloc. -5.8%	EM Equity 18.9%	Large Cap -8.3%	Asset Alloc. 6.6%	Large Cap 14.0%
Small Cap 4.6%	High Yield 13.7%	Cash 4.8%	Large Cap -37.0%	Asset Alloc. 25.0%	Asset Alloc. 13.3%	Small Cap -4.2%	Asset Alloc. 12.2%	Cash 0.0%	High Yield 0.0%	High Yield -2.7%	Asset Alloc. 8.3%	REITs 8.7%	Small Cap -11.0%	High Yield 12.6%	EM Equity -9.7%	DM Equity 5.3%	High Yield 10.9%
High Yield 3.6%	Cash 4.8%	High Yield 3.2%	REITs -37.7%	Comdty. 18.9%	DM Equity 8.2%	DM Equity -11.7%	Fixed Income 4.2%	Fixed Income -2.0%	EM Equity -1.8%	Small Cap -4.4%	Fixed Income 2.6%	Fixed Income 3.5%	Comdty. -11.2%	Fixed Income 8.7%	DM Equity -10.9%	Fixed Income 4.1%	Asset Alloc. 10.0%
Cash 3.0%	Fixed Income 4.3%	Small Cap -1.6%	DM Equity -43.1%	Fixed Income 5.9%	Fixed Income 6.5%	Comdty. -13.3%	Cash 0.1%	EM Equity -2.3%	DM Equity -4.5%	EM Equity -14.6%	DM Equity 1.5%	Comdty. 1.7%	DM Equity -13.4%	Comdty. 7.7%	Small Cap -11.4%	Cash 1.3%	Fixed Income 3.4%
Fixed Income 2.4%	Comdty. 2.1%	REITs -15.7%	EM Equity -53.2%	Cash 0.1%	Cash 0.1%	EM Equity -18.2%	Comdty. -1.1%	Comdty. -9.5%	Comdty. -17.0%	Comdty. -24.7%	Cash 0.3%	Cash 0.8%	EM Equity -14.2%	Cash 2.2%	Comdty. -12.0%	Comdty. -2.6%	Cash 1.0%

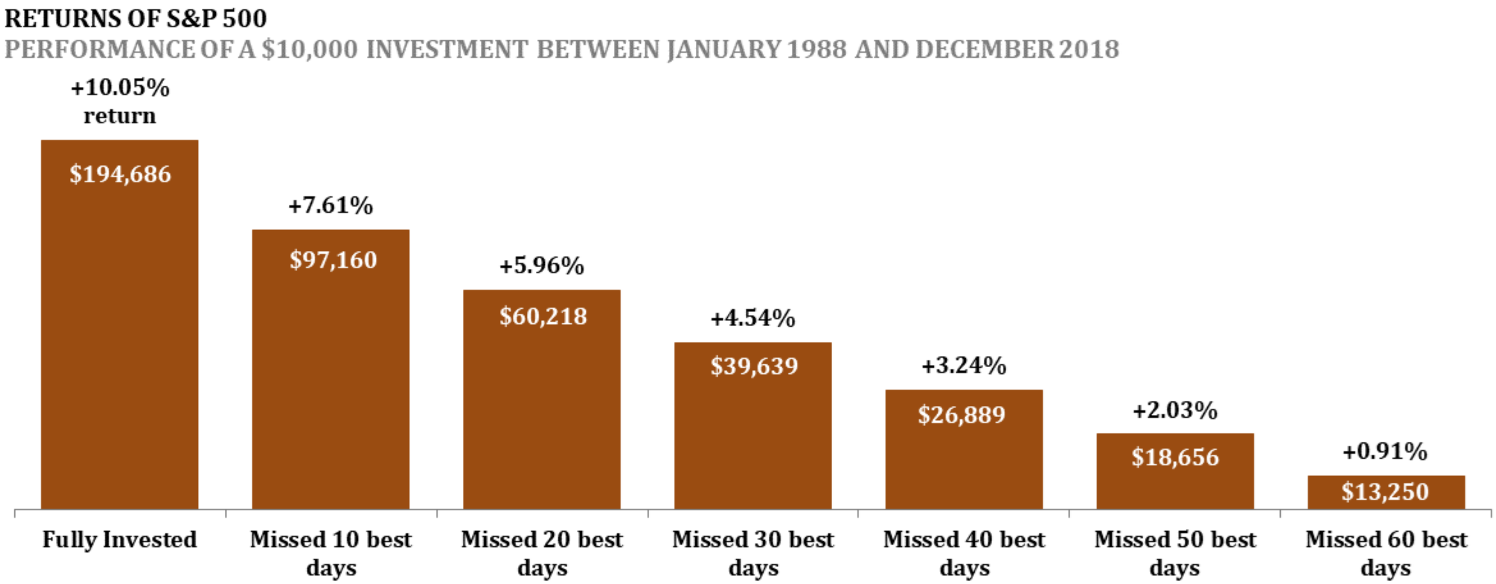


- ❑ In addition, there is almost no cost attached to smart diversification; if done properly, investors can even reduce risk while maintaining their return targets, and in some cases, expand the growth potential of their portfolios.

- ❑ You can see from the table above, no asset class on a year-over-year basis has consistently dominated the markets. Some years small company stocks lead; other years, it's the large company stocks, and at other points, it might be emerging markets or real estate.

Sources: https://am.jpmorgan.com/blob-gim/1383587507523/83456/MI-MB-Volatile%20Markets_4Q18_v2.pdf, https://www.forbes.com/sites/jeffreylevine/2018/07/31/the-big-benefit-of-diversification-no-one-talks-about/#4c94de9743cf

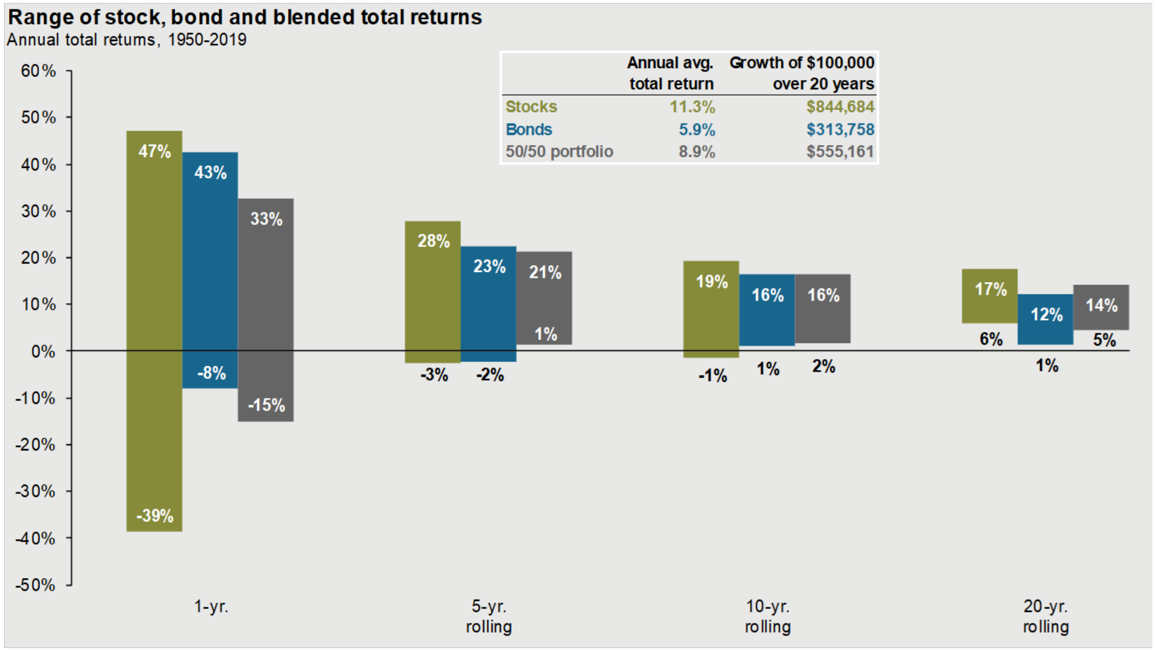
Markets Move in Brief Bursts



- Over a thirty-year period of market returns, a portfolio fully invested in the S&P 500 generates, on average, a return of just over 10.05% annually. But if you missed the ten best days during that thirty-year period, your returns would be cut by almost one-third.
- So what percentage of trading days do those ten best days amount to over a thirty-year period? Let me explain. There are approximately 252 trading days in a given year, so multiply that number by thirty years and you have 7,560 days. And that means those ten days amount to less than a quarter of one percent (0.13 percent) of that time total. That's an incredibly small number. In other words, missing out on only 0.13 percent of trading days costs you more than eighteen times that in return potential.
- Extend that same scenario to missing twenty of the best trading days over the same thirty-year period, and you lose almost half of your potential investor returns. Based on the same math above, by missing out on only 0.26 percent of trading days, investors may be sacrificing almost sixteen times that in their return potential.
- And if you miss thirty of the best trading days, your annualized return is cut by almost 60 percent. That's clearly not a great retirement strategy.

Source: https://www.zacksim.com/perils-moving-investments-cash/

Time Shapes Risk



- Exposing your portfolio to equity markets requires tremendous patience. In the short run, markets can be extremely volatile. I probably don't need to tell you that because you experienced the first few weeks of 2020. But long-term equity investing can produce some reliable and helpful return averages for investors.

- If you examine the one-year range of returns for the S&P 500 since 1950, you will see a wide range of return outcomes, from a negative 39 percent to a positive 47 percent. As an investor, if you're tempted to time the market, I refer you back to the first two charts to see what your likely outcome could be.

- With that said, if your time horizon is long, you can see how the risk of negative equity returns is shaped out, providing investors with long-range risk and returns that they can depend on for retirement.

Source: https://am.jpmorgan.com/us/en/asset-management/gim/protected/adv/insights/guide-to-the-markets

Don’t Do Something; Just Stand There

Market downturns happen frequently but don’t last forever

Standard & Poor’s 500 Composite Index (1950–2019)

Size of decline	-5% or more	-10% or more	-15% or more	-20% or more
Average frequency*	About three times per year	About once per year	About once every four years	About once every six years
Average length†	43 days	112 days	262 days	401 days
Last occurrence	August 2019	December 2018	December 2018	December 2018

* Assumes 50% recovery of lost value.
† Measures market high to market low.

Sources: Capital Group, Standard & Poor’s.

- ❑ While you wait for your returns, you are likely to experience some difficult times. That is apparent when you consider the frequency and longevity of corrections and bear markets.
- ❑ In my experience, investors often can become downright desperate while they wait. But most of the time, your best bet, beyond rebalancing and dollar-cost averaging, is to remain patient.

Source: https://www.capitalgroup.com/advisor/insights/articles/how-stay-calm-when-markets-stumble.html

Thank You