Equity Investing

Know the Game You're Playing

January 2022

Phillips & Company

Wealth Strategies | Vested

DISCLAIMER

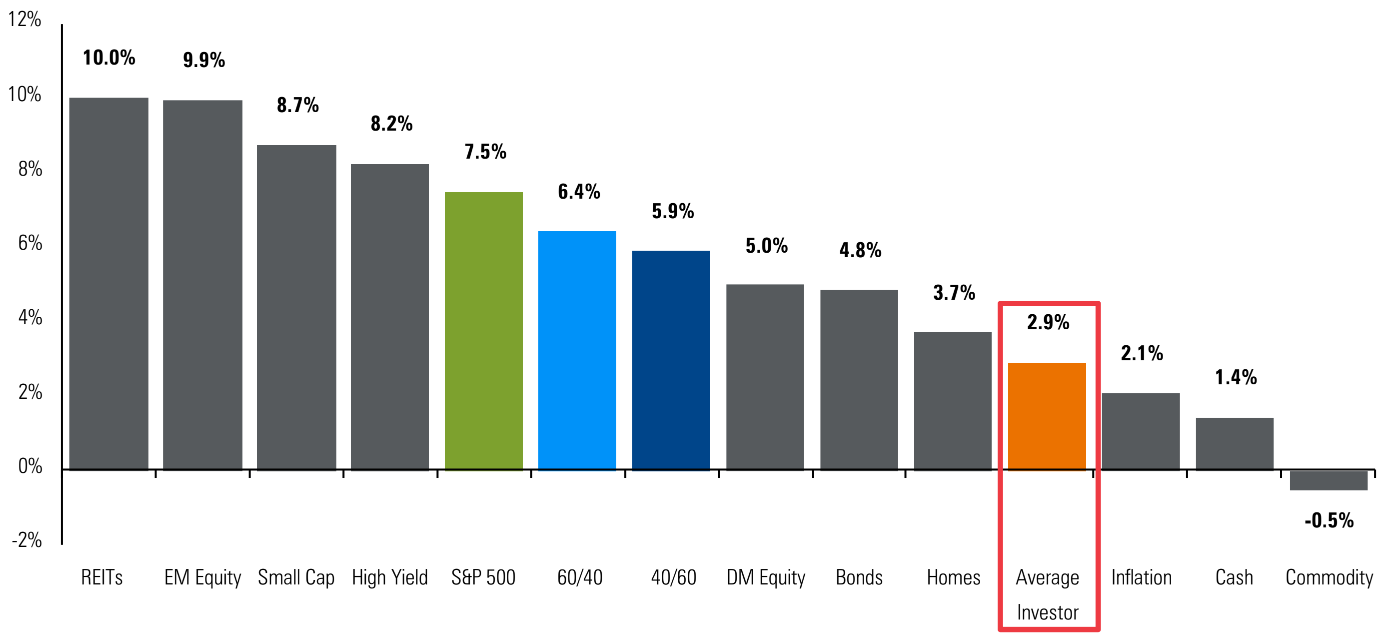
Information contained herein is derived from sources believed to be reliable.

Accuracy is not guaranteed.

This document is a general communication being provided for informational purposes only. It is educational in nature and not designed to be used as advice or a recommendation for any specific investment product, strategy, plan feature or other purpose in any jurisdiction, nor is it a commitment from Phillips and Company, LLC. to participate in any of the transactions mentioned herein. Any examples used are generic, hypothetical and for illustration purposes only.

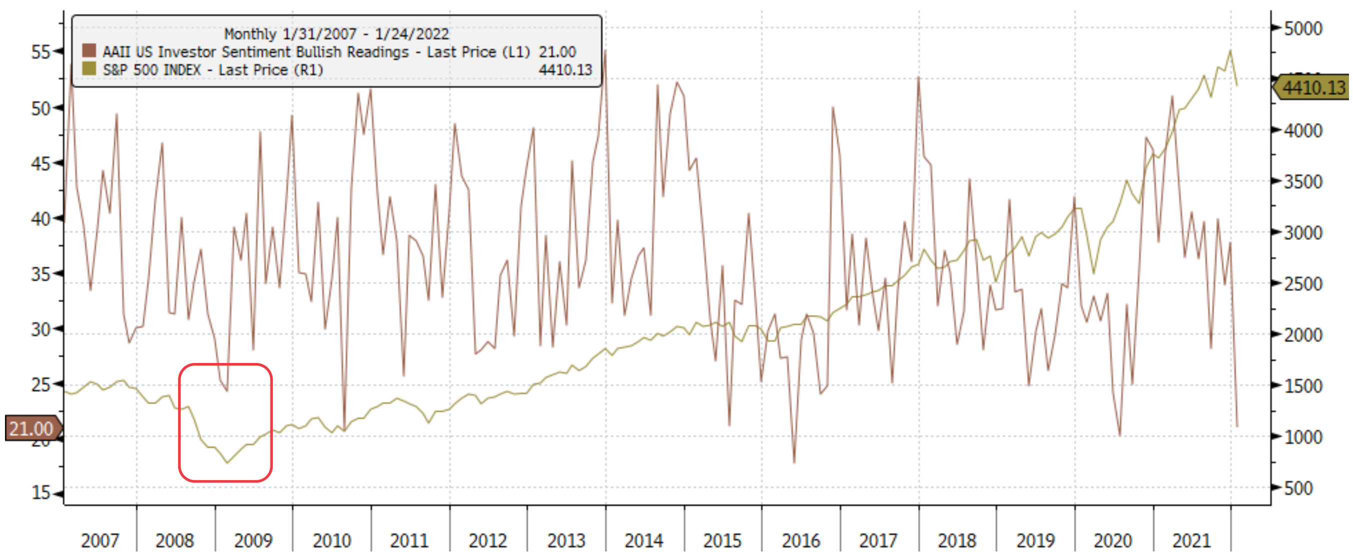
Individual Investors Tend to Underperform

20-year annualized returns by asset class (2001–2020)



- ☐ 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.

AAII Bullish Sentiment & S&P 500



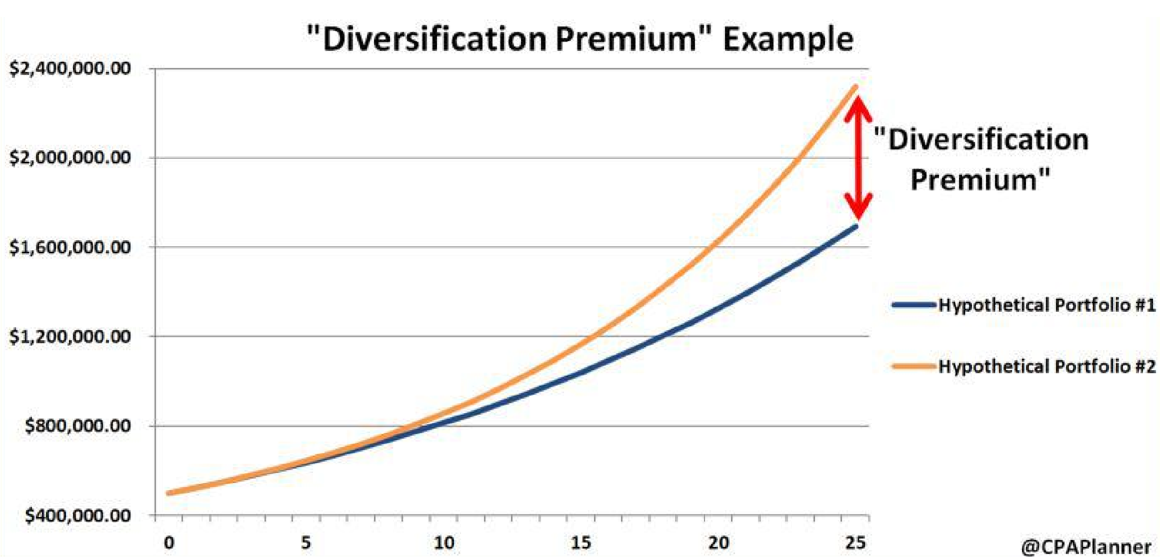
- ☐ Generally speaking, those same investors tend to sell when they should buy and react when they should not. Just look at individual investor sentiment at the worst part of the financial crisis. Using the AAII Index, you can see individual investor sentiment is at its worst exactly when the market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

Sources: J.P. Morgan, Bloomberg

Diversification: The Only Free Lunch in Finance

2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2007-2021 Annualized	2007-2021 Volatility
REITs 28.0%	REITs 8.3%	High Yield 19.6%	Small Cap 38.8%	REITs 30.1%	REITs 3.2%	Small Cap 21.3%	EM Equity 37.3%	Cash 1.8%	Large Cap 31.5%	Small Cap 20.0%	REITs 43.2%	Large Cap 10.7%	REITs 23.2%
Small Cap 26.9%	Fixed Income 7.8%	EM Equity 18.2%	Large Cap 32.4%	Large Cap 13.7%	Large Cap 1.4%	High Yield 14.3%	DM Equity 25.0%	Fixed Income 0.0%	REITs 26.0%	Large Cap 18.4%	Large Cap 28.7%	Small Cap 8.7%	EM Equity 22.9%
EM Equity 18.9%	High Yield 3.1%	REITs 18.1%	DM Equity 22.8%	Fixed Income 6.0%	Fixed Income 0.5%	Large Cap 12.0%	Large Cap 21.8%	High Yield -4.1%	Small Cap 25.5%	EM Equity 18.3%	Commodities 27.1%	REITs 6.9%	Small Cap 22.5%
Commodities 16.8%	Large Cap 2.1%	DM Equity 17.3%	Asset Allocation 14.8%	Asset Allocation 5.2%	Cash 0.0%	Commodities 11.8%	Small Cap 14.6%	Large Cap -4.4%	DM Equity 22.0%	Asset Allocation 10.4%	Small Cap 14.8%	High Yield 6.6%	Commodities 19.1%
Large Cap 15.1%	Cash 0.1%	Small Cap 16.3%	High Yield 7.3%	Small Cap 4.9%	DM Equity -0.8%	EM Equity 11.2%	Asset Allocation 14.3%	REITs -4.6%	Asset Allocation 19.3%	DM Equity 7.8%	Asset Allocation 13.4%	Asset Allocation 6.5%	DM Equity 18.9%
High Yield 14.8%	Asset Allocation -0.8%	Large Cap 16.0%	REITs 2.5%	Cash 0.0%	Asset Allocation -2.0%	REITs 8.5%	High Yield 10.4%	Asset Allocation -5.9%	EM Equity 18.4%	Fixed Income 7.5%	DM Equity 11.3%	EM Equity 4.5%	Large Cap 16.9%
Asset Allocation 13.2%	Small Cap -4.2%	Asset Allocation 12.0%	Cash 0.1%	High Yield 0.0%	High Yield -2.7%	Asset Allocation 8.2%	REITs 5.2%	Small Cap -11.0%	High Yield 12.6%	High Yield 7.0%	High Yield 1.0%	Fixed Income 4.1%	High Yield 12.2%
DM Equity 7.8%	DM Equity -12.1%	Fixed Income 4.2%	Fixed Income -2.0%	EM Equity -2.2%	Small Cap -4.4%	Fixed Income 2.6%	Fixed Income 3.5%	Commodities -11.2%	Fixed Income 8.7%	Cash 0.6%	Cash 0.0%	DM Equity 3.6%	Asset Allocation 11.7%
Fixed Income 6.5%	Commodities -13.3%	Cash 0.1%	EM Equity -2.6%	DM Equity -4.9%	EM Equity -14.9%	DM Equity 1.0%	Commodities 1.7%	DM Equity -13.8%	Commodities 7.7%	Commodities -3.1%	Fixed Income -1.5%	Cash 0.9%	Fixed Income 3.3%
Cash 0.1%	EM Equity -18.4%	Commodities -1.1%	Commodities -9.5%	Commodities -17.0%	Commodities -24.7%	Cash 0.3%	Cash 0.8%	EM Equity -14.6%	Cash 2.2%	REITs -8.0%	EM Equity -2.5%	Commodities -2.6%	Cash 0.7%

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



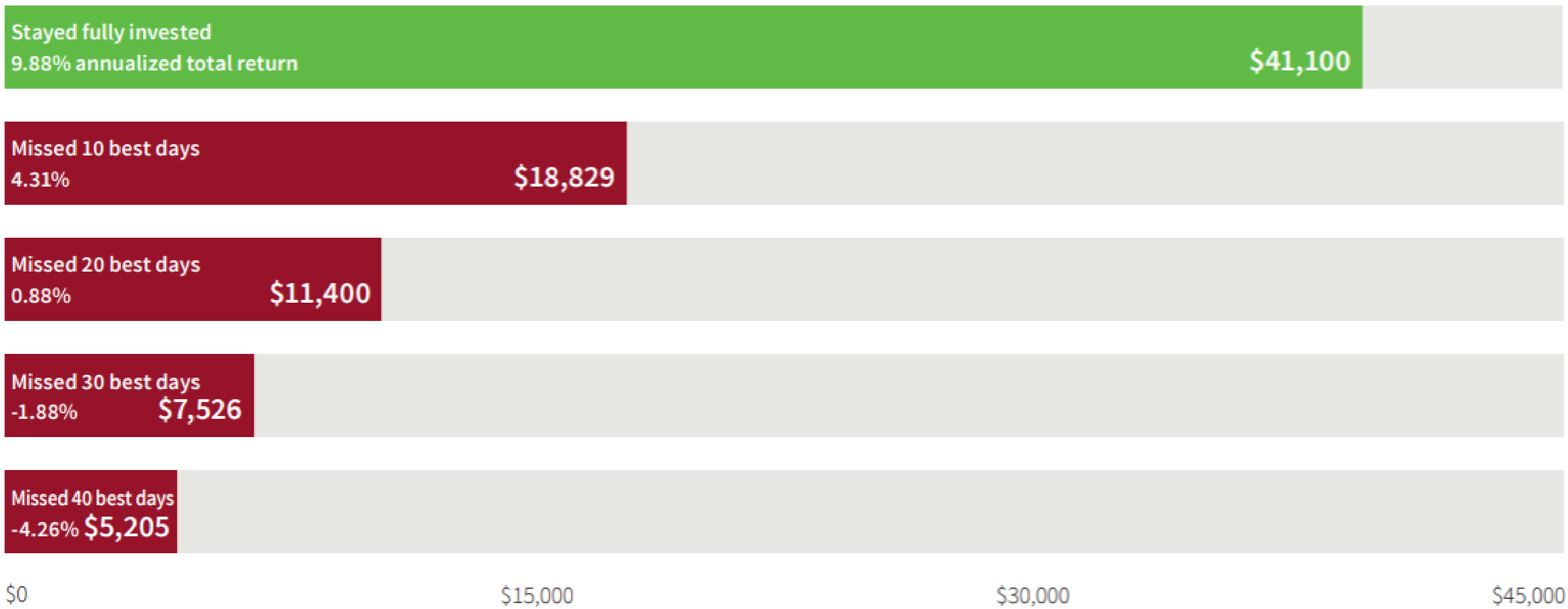
- In addition, there is almost no cost attached to smart diversification. If done properly, investors can even reduce risk while maintaining their return targets, and in some cases, expand the growth potential of their portfolios.

Source: J.P. Morgan

Markets Move In Brief Bursts

Miss Just a Few Days & You Lose All the Advantage

$10,000 invested in the S&P 500 (12/31/05–12/31/20)



Data is historical. Past performance is not a guarantee of future results. The best time to invest assumes shares are bought when market prices are low.

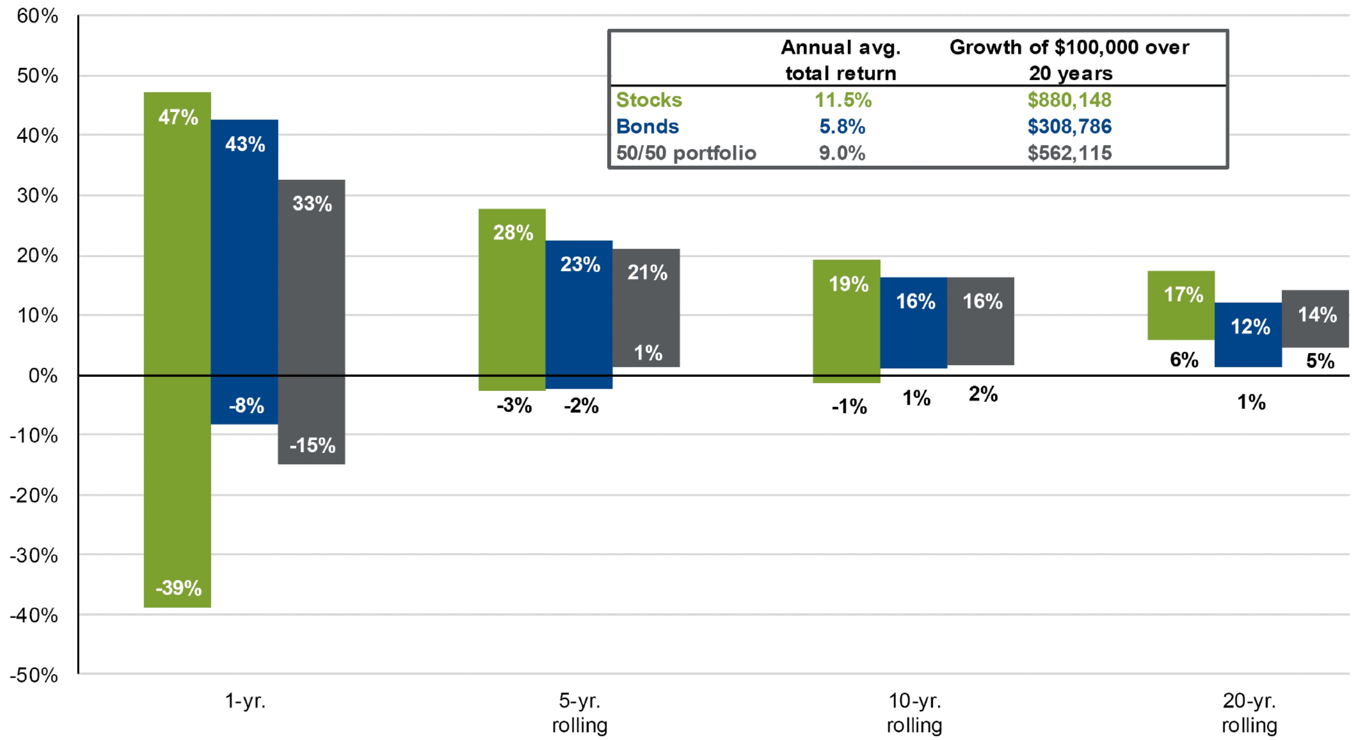
- ☐ Over a 15-year period of market returns, a portfolio fully invested in the S&P 500 generates, on average, a return of just approximately 9.88% annually. But if you missed the ten best days during that 15-year period, your returns would be cut by almost one-half.

- ☐ 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 fifteen years and you have 3,780 days. And that means those ten days amount to about a quarter of one percent (0.26 percent) of that time total. That's an incredibly small number. In other words, missing out on only 0.26 percent of trading days costs you more than 20 times that in return potential.

Source: Putnam

Time Shapes Risk

Range of stock, bond and blended total returns
Annual total returns, 1950 - 2021



- ☐ 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 reliable 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: J.P. Morgan

Pain is Part of the Process

The Key is Not Minding

Standard & Poor's 500 Composite Index (1951-2020)

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 three years	About once every six years
Average length†	43 days	110 days	251 days	370 days
Last occurrence	October 2020	September 2020	March 2020	March 2020

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

- ☐ 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.
- ☐ Investors often can become downright desperate while they wait. Most of the time, your best bet – beyond rebalancing and dollar-cost averaging – is to remain patient.

Source: Putnam