The Risks of Market Timing

APRIL 2020

Nobody ever got on a roller coaster expecting a level ride.

It's the same with investing. Over long periods of time, the financial markets can be remarkably steady—since 1926, stocks have never lost money in any 15-year period[1]—but in the short run, sharp spikes in security prices can be the norm.

As uncertainty surrounding the eventual economic impact of the coronavirus has recently escalated, the S&P 500 Index has displayed significant volatility—rising or falling at least 3% uncommonly often.[2]

This volatility suggests that the market can't seem to make up its mind, triggering a bumpy ride for investors—some of whom may be tempted to pull out of stocks and wait for the market to regain its footing.

But is moving assets from your current portfolio to what you think are more stable, "safer" investments really a good idea?

Amid such uncertainty, what can you do to keep your cool and avoid making potentially costly, emotionally-driven decisions?

[1] Based on rolling, 15-year periods from December 31, 1925, through March 17, 2020, with dividends reinvested. Stocks measured by the S&P 500 Index, an unmanaged index that measures the performance of 500 large-capitalization domestic stocks representing major industries. It is not possible to invest in an index. Past performance is no guarantee of future results.

[2] Through the first 52 trading days of 2020, the S&P 500 Index rose or fell 3% or more on 13 trading days; it rose or fell by 3% or more just 7 times in all of 2018 and 2019 combined. Source: Bloomberg, SEI.

First, Remember Why You Invest

If you're like most investors, you began your investment program with the intent of achieving any number of goals, some long-term, others shorter-term—such as enjoying a comfortable retirement, sending your children to college, buying a second home or supporting your current lifestyle.

You have invested in stocks and bonds to steadily build and preserve wealth over decades. Your long-term strategy did not include trying to jump in and out of the market based on its short-term performance.

Besides, brief, explosive spurts of volatility, both positive and negative, are typically the norm. In the short run, severe moves in security prices should be expected.

But an impulsive investor who abandoned the market during one or more of its sharp downturns may have missed the strong, ensuing rebounds.

Exhibit 1: Market-Timing Approaches Fall Short

*Strategy: 1926-2019	Annualized Return	Growth of $100,000
Exit when market declines; stay out until market has a decent year	9.6%	$562.9M
Exit when market is "too high"; stay out until after correction (a down year)	9.7%	$605.4M
Remain Invested Through Ups And Downs	**10.2%**	**$920.4M**

This is a hypothetical example. Past performance does not guarantee future results.

*The first approach involved switching from stocks to T-bills following any year in which the stock market declined and returning to stocks after the market earned at least 10% for a year. The second approach involved switching from stocks to T-bills following a combined two-year stock market rise of 40% or more and returning to stocks after the market declined for a year-or after two years, in any event.

The launch date of the S&P 500 Index was March 4, 1957. Information for an index prior to its launch date is back-tested, based on the methodology that was in effect on the launch date. Back-tested performance, which is hypothetical and not actual performance, is subject to inherent limitations because it reflects application of an index methodology and selection of index constituents in hindsight. No theoretical approach can take into account all the factors in the markets in general and the Impact of decisions that might have been made during the actual operation of an index. Actual returns may differ from, and be lower than, back-tested returns.

Source: Compustat: Roger G. Ibboston and Rex A. Sinquefiled, "Stocks, Bonds Bills, and Inflation: Year-by-Year Historical Returns," University of Chicago Pres Journal of Business (January 1976); Lehman Brothers and Standard & Poor's

Second, Understand the Risk of Market Timing

When it comes to investing, what's the biggest risk of all? Market risk? Company risk? Interest-rate risk? Credit risk? Inflation risk?

No, for many investors, the biggest risk is, quite fundamentally, the risk of losing money.

And because losing money can provoke a powerful, visceral reaction, some investors turn to market timing: buying or selling a security based on future price predictions (Exhibit 2).

Exhibit 2: Dangers of Market Timing

Investment Period 1988-2019	S&P 500: Average Annual Total Return
Fully Invested (all days)	**10.7%**
Minus 20 Best Days	6.7%
Minus 30 Best Days	5.3%
Minus 40 Best Days	4.0%
Minus 50 Best Days	2.8%
Avg. Annual Return T-Bills	3.0%

Past performance does not guarantee future results. An investor cannot invest directly in an index or average and they do not include sales charges or operating expenses associated with an investment in a mutual fund, which would reduce total returns. Source: Federal Reserve and Standard & Poor's

But choosing when to invest, or "time" the market, is difficult. Investors who attempt to time the market may run the risk of missing periods of exceptional returns.

Clearly, market timing can seriously diminish long-term performance if market volatility isn't managed properly. On the other hand, volatility provides investors with the opportunity to buy stocks and stock mutual funds at attractive prices (Exhibit 3).

Exhibit 3: Strategic Market Timing Is Harmful to Your Wealth

S&P 500: 1988-2019	Average Monthly Return
Full 384 Months	0.8%
Best 36 Months (~10% of the time)	**7.6%**
All other Months (~90% of the time)	0.2%

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As a financial advisor, I am committed to:

- Making a point of knowing you and knowing your individual financial goals.
- Helping you avoid making emotion-driven mistakes in turbulent times.
- Always being available to consult with you, in good markets and rough markets.

Together we will create your personalized goals-based investment plan—with an emphasis on managing risk, and designed to produce relatively consistent and predictable results in various market environments.

Index returns are for illustrative purposes only and do not represent actual portfolio performance. Index returns do not reflect any management fees, transaction costs or expenses. One cannot invest directly in an index. Bonds will decrease in value as interest rates rise. Past performance does not guarantee future results.

The S&P 500 Index, or the Standard & Poor's 500 Index, is a market-capitalization-weighted index of the 500 largest U.S. publicly traded companies. The S&P is a float-weighted index, meaning company market capitalizations are adjusted by the number of shares available for public trading.

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200368.02 IAS (04/20)