Be Patient, Be Brave

Performance Dispersion and Time Horizon

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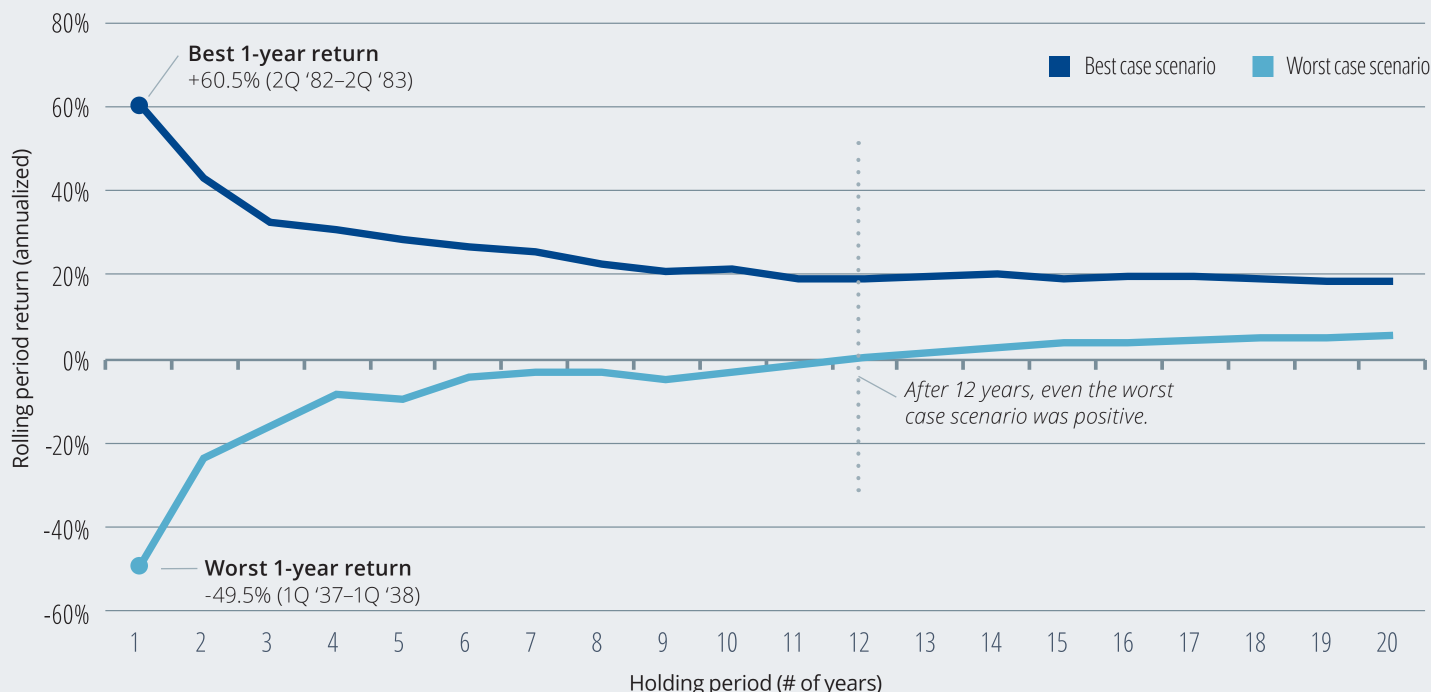
Headlines suggesting an economic downturn is right around the corner are everywhere. But making snap decisions in response to fear-mongering like this would probably be a mistake, because attempting to time the market can often lead to sub-par performance. So instead of asking yourself, "is this a good time to be invested in the market?", try asking yourself "is my investment horizon long enough to overcome any potentially bad market outcomes?"



In the short-run, returns can vary widely but investors with a longer horizon have experienced far less return dispersion.

Source for data: Morningstar®

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We analyzed quarterly returns from the S&P 500® Index from 1936[1] to today and charted the best and worst outcomes at each horizon in the chart on page 1. Notice how the lines connecting these extremes converge over time. Simply put, the longer your horizon, the more predictable the outcome has been — and the less likely you were to experience extreme results. For example:

- The worst four-quarter rolling return observed over the last 83 years was -49.49%, covering the period between April 1937 and March 1938.[2] How might an investor who had the bad luck to step into the market at exactly that point have reacted?
  - If they had kept a stiff upper lip and held on to their investment in stocks for the next 20 years, they would have earned 10.60% on an annualized basis (or 649.41% on a cumulative basis).[3]
  - On the other hand, if they were frightened by the loss and moved into the safety of government bonds for the next 19 years, they would have locked in that awful loss and lost -1.54% per year during the 20 year period.[4]
- But even those who enter the market at the right time will have their bravery tested. Someone who entered the market in June 1980 and held onto stocks for the next 20 years would have earned more than 18% per year, the best in our sample.[5]
  - But during the 80 quarterly periods during that span, 18 of them (or 22.5%) posted negative returns. Across our entire 83-year sample, stocks dropped almost one out of every three calendar quarters.

If history is any guide, a long investment horizon may give you at least some freedom to ignore the ominous headlines and invest with confidence. The chart on page 1 makes it clear that two things have occurred over time: 1) The dispersion between the worst and best outcomes narrows considerably over time, and 2) historically, investors who remained patient and stayed invested for at least 12 years always recovered from market setbacks and were ultimately rewarded with at least modest gains.

Of course, each investor has unique circumstances that they should consider when determining their own investment horizon. But if you have the luxury of a long horizon — and the courage to stare market volatility in the face without flinching — history suggests that you're unlikely to suffer significant losses, even if you're unlucky enough to have invested at what might feel like the worst possible time.

1 Selected time period reflects earliest data availability for the S&P 500 Total Return (USD) Index as available in Morningstar Direct.

2 Total return for a hypothetical investor who remained invested in stocks during the period 04/01/1937-03/31/1938, (S&P 500 TR USD).

3 Annualized return for a hypothetical investor who remained invested in stocks during the period 04/01/1937-03/31/1957 (S&P 500 TR USD).

4 Annualized return for a hypothetical investor who invested in stocks between 04/01/1937-03/31/1938 (S&P 500 TR USD) , then switched to bonds between 04/01/1938-03/31/1957(IA SBBI US IT Government TR USD).

5 Annualized return for a hypothetical investor who remained invested in stocks between 6/30/1980 and 3/31/2000 (S&P 500 TR USD).

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