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Resources Management Corp

# MARKET COMMENTARY

## ON THE RISKS OF MARKET TIMING (PART 2)

It has been 112 months since we officially exited the Great Recession and entered our current bull market. According to J.P. Morgan Asset Management, the total return on the S&P 500 over this period has been 316% [1], making it one of the longest running and highest return (on a cumulative basis) bull markets since before the Great Depression. While today's broader backdrop remains supportive of continued strong performance, it is inevitable that both the economy and stock market will at some point reverse for a period of time. To be clear, this is not a prediction that a correction is imminent, but simply a commentary on the cyclical nature of economies and markets in general. Investors and market pundits, alike, have been calling for the demise of this bull market for years, and for years they have been proven wrong. Either by selling the stock market short or simply sitting on the sidelines, significant money has been lost (or not earned) through failed attempts to time the market cycle. In our view, intelligent and well-informed investors exert too much energy attempting to predict when the cycle will turn. Instead, we find it far more prudent to focus our time on identifying businesses that are poised to perform well over the long term across a variety of economic environments.

When it comes to predicting the timing of a shift in the economic cycle, it is our preference to recall the sage advice of Socrates: "All I know is that I know nothing." While we are constantly evaluating the current state of the economy, especially as it relates to the fundamentals of the businesses we have invested in, we do not center our investment strategy around correctly timing when to make large moves in and out of the market. Strategies like this, despite having the potential to be highly profitable when executed correctly, often result in an unnecessary degree of variability in investment results. Studies have shown that missing a very small number of trading days can have a dramatic impact on performance. As can be seen below, missing just the 5 best trading days over 20 years, for example, would result in a gain of only $16,625 over the period compared with a gain of $30,135 when fully invested for the entire period.

**The Problem With Market Timing: Missing The Best Days**

**20 Years (1/1/1998 - 12/31/2017)**

| $10,000 Invested in the S&P 500 Index | S&P 500 Annualized Return | Value of $10,000 at the End of the Period | Gain/ Loss | Impact of Missing Days |
|---|---|---|---|---|
| All 5,036 trading days | 7.20% | $40,135 | $30,135 | -- |
| Less the 5 days with the biggest gains | 5.02% | $26,625 | $16,625 | -45% |
| Less the 10 days with the biggest gains | 3.53% | $20,030 | $10,030 | -67% |
| Less the 20 days with the biggest gains | 1.15% | $12,570 | $2,570 | -91% |
| Less the 40 days with the biggest gains | -2.80% | $5,670 | -$4,330 | -114% |

Source: Yahoo! Finance

The idea that only 5 days over a 20-year period can cause such a dramatic difference in financial outcomes is rather striking. While perfectly missing all of the top 5 days of an extended trading period is unlikely even for a very active market timer, it highlights the dramatic impact that even seemingly minor mistakes can have on long term investment results. Given how unpredictable the timing of market shifts can be (even to an investor who has correctly deemed something as over or under valued), we view it to be far more sensible to focus on remaining invested at our predetermined asset allocation targets and selecting securities that offer a compelling value proposition over the long term. In doing so, we increase the probability of achieving the financial goals and outcomes that have been determined at the outset of a client relationship.

[1] As of July 31, 2018

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