WINTHROP WEALTH

JULY 2021 CLIENT QUESTION OF THE MONTH: MARKET TIMING DOES NOT WORK

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In our July Client Question of the Month, we thought it would be helpful to assemble our favorite charts on market timing. As a wealth management firm, market timing is one of our most frequently discussed topics.

Market timing is an investment strategy that is implemented by selling a large portion of equity holdings when the market is high (keep in mind this could result in substantial capital gains for taxable investors), patiently waiting on the sideline as the market declines, reinvesting at the market low, and then riding the market back up to new highs. Rinse and repeat. Although this might sound easy, the reality is that successful market timing is nearly impossible to execute consistently. Market tops and bottoms are never obvious in real time, only in hindsight. To execute a market timing strategy an investor must get two decisions precisely correct: when to sell out of the market and when to buy back in. Most investors come up short with the second decision, buying back in. We will note that if an investor discovered the magic formula to market timing, they would essentially be able to make an unlimited amount of money. There is no magic formula.

Market timing decisions are often emotional decisions driven by fear or panic rather than fact-based analysis. Given the damaging impact that market timing decisions have on performance, the average investor should look for ways to mitigate this behavior. A trusted financial advisor can help make rational and data driven decisions rather than ones based on emotion. In our experience, the best course of action is to combine comprehensive financial planning with a globally diversified portfolio constructed by a thorough investment process.

At Winthrop Wealth, we follow a total net worth approach to wealth management that combines both comprehensive financial planning and investment management. While financial planning and investment management can function successfully on their own, the combination produces a whole greater than the sum of its parts. The financial plan defines cash flow needs, optimizes account structures, considers tax minimization strategies, and determines the appropriate asset allocation based on the client's willingness and ability to take risk. Based on the output of the financial plan, our investment management process designs a well-diversified portfolio constructed with a methodology based on prudent risk management, asset allocation, and security selection. We ensure that our client's short-term cash flow needs are met while constantly stress testing both their financial plan and investment portfolio to help them ultimately reach their longer-term goals and objectives despite challenging markets. Without a comprehensive financial plan and investment process, it is very easy to shoot yourself in the foot by making an emotionally based market timing mistake.

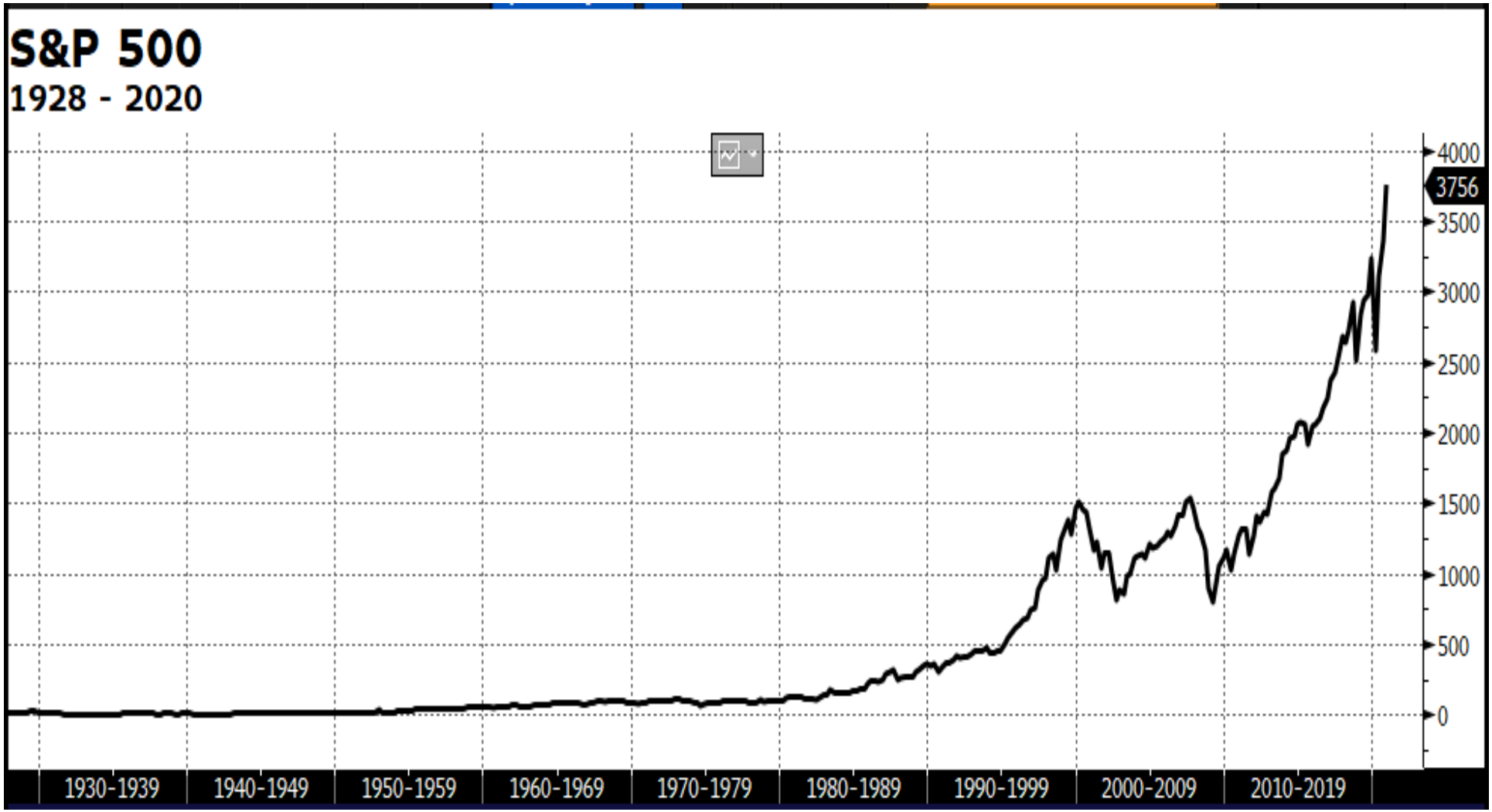
Successful investing requires skill and discipline, not reliance on gimmicks like market timing. We hope that the following slides cement that market timing is a loser's game and should not be relied upon as a serious investment strategy.

The stock market goes up over time

From 1928 to 2020, the stock market produced a total annualized return of +9.6%. A $10,000 investment in 1928 would have increased to over $48,000,000 at the end of 2020.

We would also like to highlight that this period includes several of the most challenging market environments in history, including, the Great Depression, World War II, 1970's Stagflation, Crash of 1987, Dot-Com Bubble, Global Financial Crisis, and the Covid Pandemic. The total period includes eleven bear markets, fifteen recessions, and dozens of corrections and pullbacks.

The stock market rewards long term investors.



SOURCE: Bloomberg

The stock market goes up over time, but returns are not linear

Since 1928, the stock market produced positive results in 68 calendar years vs. 25 years with negative returns.

The market went higher in 73% of years with an average return of +20.8% and declined in 27% of years with an average drop of-14.0%.

S&P 500 Calendar Year Returns: 1928 - 2020

Total Annualized Return: 9.6%

Positive Years: 68 (73%)

Negative Years: 25 (27%)

-50% to -40%	-40% to -30%	-30% to -20%	-20% to -10%	-10% to 0%	0% to 10%	10% to 20%	20% to 30%	30% to 40%	40% to 50%	50% to 60%
						1944 19.5%				
						1972 19.0%				
						1986 18.7%				
						1979 18.6%	2003 28.7%			
						2020 18.4%	1998 28.5%	1928 37.9%		
					1992 7.6%	1952 18.2%	1961 26.9%	1995 37.5%		
				1939 -0.1%	1978 6.6%	1988 16.6%	2009 26.4%	1975 37.2%		
				1953 -0.9%	1956 6.5%	1964 16.4%	1943 25.6%	1945 36.3%		
				1990 -3.2%	1984 6.3%	2012 16.0%	1976 23.9%	1936 33.7%		
				2018 -4.4%	1947 5.6%	2006 15.8%	1967 23.9%	1997 33.3%		
				1934 -4.7%	2007 5.6%	2010 15.1%	1951 23.8%	1950 32.6%		
				1981 -4.9%	1948 5.4%	1971 14.3%	1949 23.6%	1980 32.5%		
				1977 -7.2%	1987 5.3%	2014 13.7%	1996 22.9%	2013 32.4%		
			1957 -10.7%	1946 -8.0%	2005 4.9%	1965 12.5%	1963 22.8%	1985 31.7%		
			1941 -11.6%	1969 -8.4%	1970 3.9%	1959 12.0%	1983 22.6%	1989 31.7%		
			2001 -11.9%	1962 -8.7%	2011 2.1%	2016 12.0%	2017 21.8%	2019 31.5%		
		2002 -22.1%	1929 -11.9%	2000 -9.1%	2015 1.4%	1968 11.0%	1982 21.5%	1955 31.4%	1933 44.1%	
	1937 -34.7%	1974 -26.5%	1973 -14.7%	1940 -9.6%	1994 1.3%	2004 10.9%	1999 21.0%	1991 30.4%	1958 43.1%	
1931 -47.1%	2008 -37.0%	1930 -28.5%	1932 -14.8%	1966 -10.0%	1960 0.5%	1993 10.1%	1942 20.1%	1938 30.1%	1935 41.4%	1954 52.3%

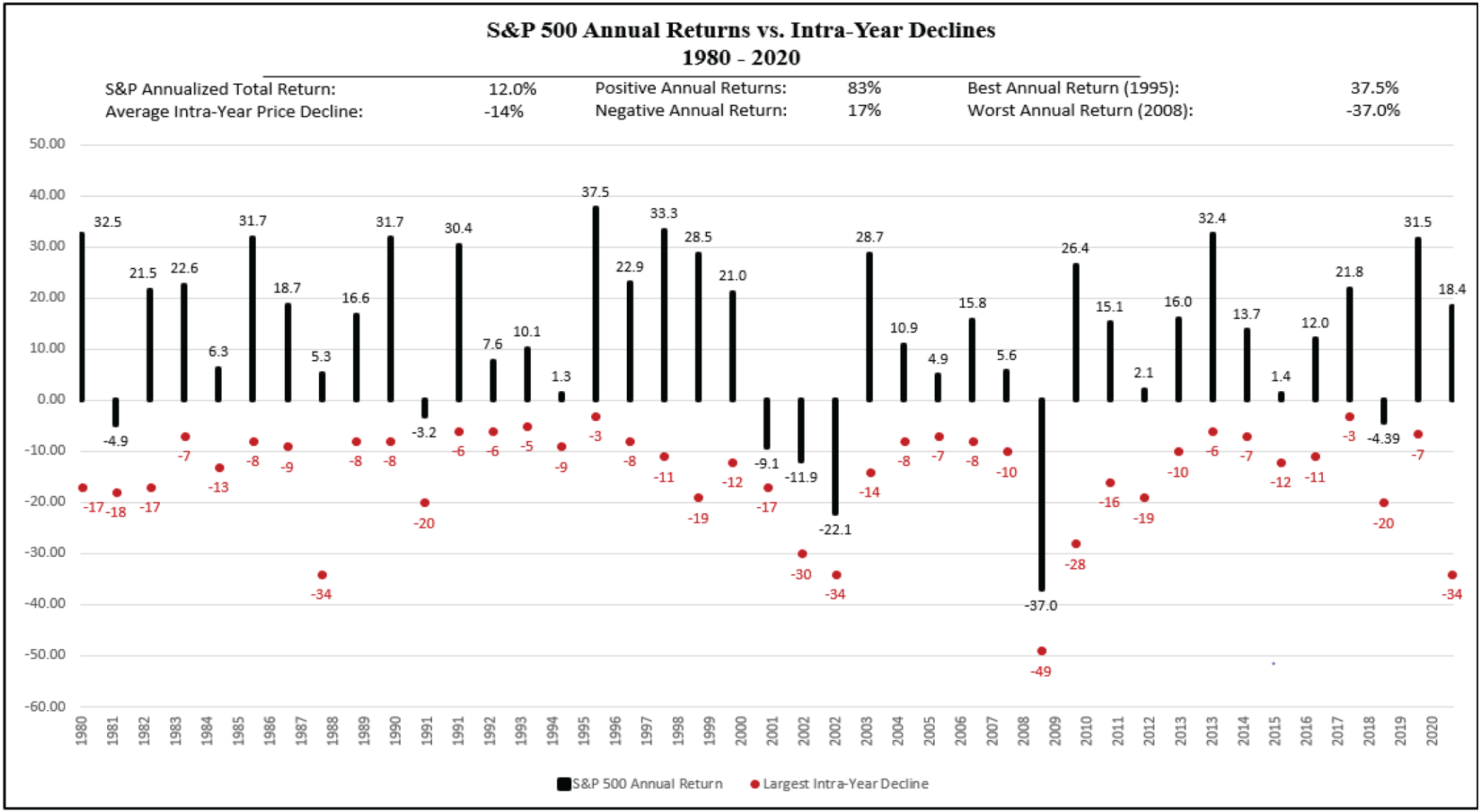
SOURCE: Bloomberg

Market declines are common

The following chart displays the S&P 500's annual return vs. the largest intra-year decline from 1980 through 2020.

Over this period, the S&P 500 has generated a total annualized return of +12.0%. Annual returns ranged from-37.0% to +35.5%.

There were plenty of market drops along the way as the average intra-year price decline was-14%. This simply means that at some point each year the S&P 500 dropped by an average of-14%.



SOURCE: Bloomberg

There are always "reasons to sell"

An old investment adage is that the stock market climbs a "wall of worry." This simply means that the market has risen over time despite a constant barrage of potential risks that could cause a correction or decline.

The market always has risks to overcome and there is never an "all-clear" signal.

The 24-hour news cycle and advent of social media might make it seem as though risks are more prevalent today, but they have always existed. Historically, you might not find out about economic data or company specific news until you read about it in the newspaper the next day. Now everything happens in real-time, with a never-ending flow of pundits and articles ready to pontificate about what happened and how it may impact the markets.

We caution our clients to not overreact to one data-point, piece of news, or what a so-called market authority might be predicting.

Reasons to Sell Stocks

Year	Market Risk	Return	Year	Market Risk	Return	Year	Market Risk	Return
1970	Vietnam War Spread	3.9%	1987	Record-Setting Market Decline	5.3%	2004	Rising Interest Rates	10.9%
1971	Wage Price Freeze	14.3%	1988	Election Year	16.6%	2005	Hurricane Katrina	4.9%
1972	Largest U.S. Trade Deficit Ever	19.0%	1989	October "Mini Crash"	31.7%	2006	Real Estate Peaks	15.8%
1973	Energy Crisis	-14.7%	1990	Persian Gulf Crisis	-3.2%	2007	Subprime Lending	5.6%
1974	Steepest Market Drop in Four Decades	-26.5%	1991	Berlin Wall Falls	30.4%	2008	Great Recession Begins	-37.0%
1975	Clouded Economic Prospects	37.2%	1992	Global Recession	7.6%	2009	Double Digit Unemployment Numbers	26.4%
1976	Economic Recovery Slows	23.9%	1993	Health Care Reform	10.1%	2010	European Sovereign Debt Crisis	15.1%
1977	Market Slumps	-7.2%	1994	Fed Raises Interest Rates Six Times	1.3%	2011	U.S. Credit Downgrade	2.1%
1978	Interest Rates Rise	6.6%	1995	Dow Tops 5,000	37.5%	2012	Afghanistan War	16.0%
1979	Oil Prices Skyrocket	18.6%	1996	Dow Tops 6,400	22.9%	2013	Fed Taper Tantrum	32.4%
1980	Interest Rates at All-Time High	32.5%	1997	Hong Kong Reverts to China	33.3%	2014	Oil Prices Plunge 50%	13.7%
1981	Steep Recession Begins	-4.9%	1998	Long Term Capital Mgmt Collapse	28.5%	2015	China Economic Slowdown	1.4%
1982	Worst Recession in 40 Years	21.5%	1999	Y2K	21.0%	2016	Global Economic Slowdown	12.0%
1983	Market Hits New Highs	22.6%	2000	Tech Bubble Burst	-9.1%	2017	High Valuation	21.8%
1984	Record Federal Deficits	6.3%	2001	9/11 Terrorist Attacks	-11.9%	2018	US/China Trade War - Fed Policy Mistake	-4.4%
1985	Economic Growth Slows	31.7%	2002	Recession	-22.1%	2019	US/China Trade War	31.5%
1986	Dow Nears 2,000	18.7%	2003	War in Iraq	28.7%	2020	Covid Pandemic	18.4%

1970 - 2020:

Total Return: 18,087%. **Hypothetical Growth of $10,000: $1,820,000.** **Total Annualized Return: +10.7%**

SOURCE: Bloomberg

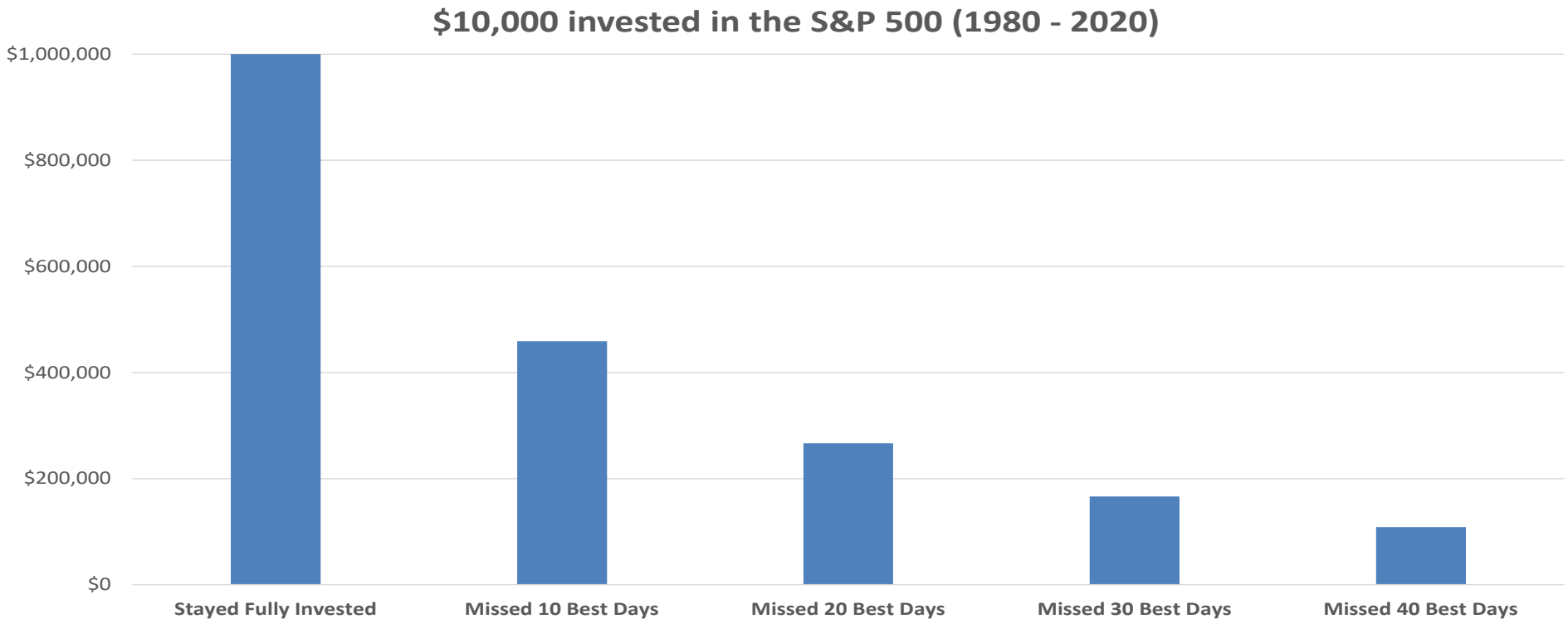
Missing the best days crushes investor returns

Investors who wait on the sidelines for the "optimal" time to buy often miss significant rallies.

A $10,000 investment in 1980 would have increased to about $1,030,000 at the end of 2020. Note, this period includes over 10,000 trading days and assumes the individual stayed fully invested. If an investor missed only the 10 best days in the market, their total return would have been less than half. If an investor missed the 40 best days, their return would have been about one tenth.

To make things more difficult for market timers, the best days often occur during periods of severe market stress. Nine of the ten best days in the market over the last forty-one years occurred during either the Global Financial Crisis (2008-2009) or the Covid Pandemic (2020). Nervous or frustrated investors who threw in the towel would have missed the subsequent market rebound and devasted their portfolios.

During periods of market stress, it is impossible to know when the market bounce will occur, but we do know that missing the bounce can have a severe negative impact on total return.



	Stayed Fully Invested	Missed 10 Best Days	Missed 20 Best Days	Missed 30 Best Days	Missed 40 Best Days
Total Return	$1,030,000	$460,000	$270,000	$170,000	$110,000
Annualized Return	12.00%	9.80%	8.30%	7.10%	6.00%

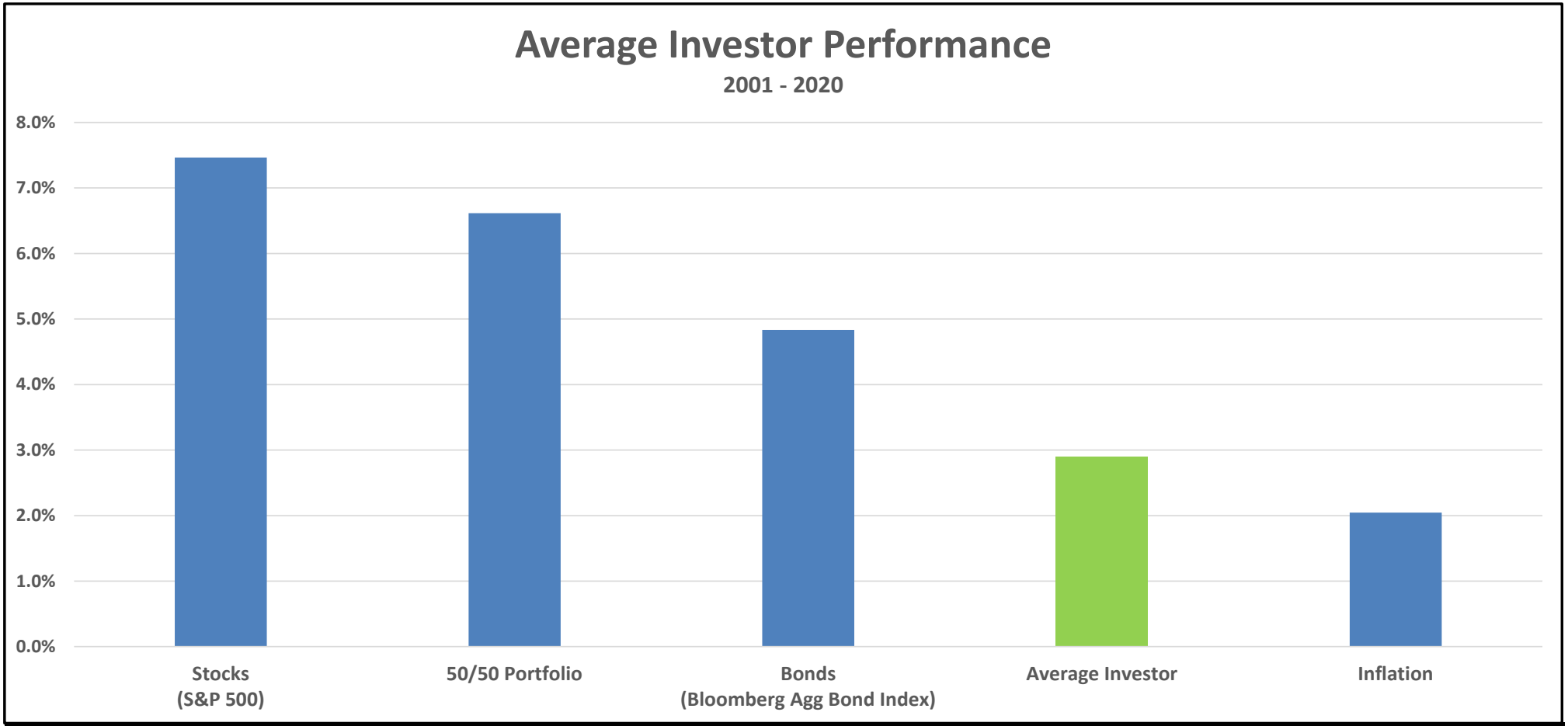
SOURCE: Bloomberg

The average investor underperforms due to market timing

The following chart is from a Dalbar study titled "Quantitative Analysis of Investor Behavior" that displays the annualized returns of various asset classes and the average investor for the twenty-year period of 2001 through 2020.

The average asset allocation investor's return is based on an analysis of the net aggregate mutual fund sales, redemptions, and exchanges each month. The study shows that the average investor's return over this period was less than half of stocks and far worse than a bond portfolio.

Dalbar cites market timing as a main factor for poor investor performance.



	Stocks (S&P 500)	50/50 Portfolio	Bonds (Bloomberg Agg Bond Index)	Average Investor	Inflation
Annualized Return	7.5%	6.6%	4.8%	2.9%	2.0%

SOURCE: Bloomberg and Dalbar Inc.

Remember the benefit of diversification

Diversification and time are an investor's two best friends. Diversified portfolios can lead to more consistent and less volatile results than a single asset class. We know that markets can be extremely volatile in the short-term but difficult periods do not last forever.

To highlight the benefits of diversification, we examined the total return performance of nine separate asset classes and a diversified asset allocation portfolio from 2006 to 2020. From year-to-year many asset classes rotate from top to bottom performers, while the asset allocation portfolio consistently stays the middle.

Asset Class Returns

2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2006 - 2020 Annualized Return	2006 - 2020 Annualized Volatility	2006 - 2020 Sharpe
Emerging Markets 32.1%	Emerging Markets 39.4%	Fixed Income 5.2%	Emerging Markets 78.5%	Small Cap 26.8%	Fixed Income 7.8%	Emerging Markets 18.2%	Small Cap 38.8%	Large Cap 13.7%	Large Cap 1.4%	Small Cap 21.3%	Emerging Markets 37.3%	Cash 1.8%	Large Cap 31.5%	Small Cap 19.9%	Large Cap 9.9%	Emerging Markets 21.8%	Fixed Income 1.04
Developed International 26.3%	Commodities 16.2%	Cash 1.8%	High Yield 58.2%	Mid Cap 26.6%	High Yield 5.0%	Mid Cap 17.8%	Mid Cap 33.5%	Mid Cap 9.7%	Fixed Income 0.5%	Mid Cap 20.7%	Developed International 25.0%	Fixed Income 0%	Mid Cap 26.2%	Large Cap 18.4%	Mid Cap 9.5%	Small Cap 20.3%	High Yield 0.65
Small Cap 18.3%	Developed International 11.2%	Asset Allocation 23.5%	Mid Cap 37.3%	Emerging Markets 18.9%	Large Cap 2.1%	Developed International 17.3%	Large Cap 32.4%	Asset Allocation 7.1%	Cash 0%	High Yield 17.1%	Large Cap 21.8%	High Yield -2.1%	Small Cap 25.5%	Emerging Markets 18.3%	Small Cap 8.9%	Mid Cap 18.3%	Asset Allocation 0.62
Large Cap 15.8%	Mid Cap 8.0%	High Yield -26.2%	Developed International 31.8%	Commodities 16.8%	Asset Allocation 1.3%	Small Cap 16.4%	Developed International 22.8%	Fixed Income 6.0%	Asset Allocation -0.8%	Large Cap 12.0%	Mid Cap 16.2%	Large Cap -4.4%	Developed International 22.0%	Mid Cap 13.6%	High Yield 7.5%	Developed International 17.5%	Large Cap 0.58
Asset Allocation 12.9%	Asset Allocation 7.3%	Small Cap -33.8%	Small Cap 27.1%	High Yield 15.1%	Cash 0.1%	Large Cap 16.0%	Asset Allocation 17.4%	Small Cap 4.9%	Developed International -0.8%	Commodities 11.8%	Asset Allocation 14.8%	Asset Allocation -4.6%	Asset Allocation 20.7%	Asset Allocation 12.5%	Asset Allocation 7.5%	Commodities 16.5%	Mid Cap 0.46
High Yield 11.8%	Fixed Income 7.0%	Commodities -35.6%	Large Cap 26.4%	Large Cap 15.1%	Mid Cap -1.7%	High Yield 15.8%	High Yield 7.4%	High Yield 2.5%	Mid Cap -2.2%	Emerging Markets 11.2%	Small Cap 14.6%	Small Cap -11.0%	Emerging Markets 18.4%	Developed International 7.8%	Emerging Markets 6.6%	Large Cap 15.1%	Small Cap 0.38
Mid Cap 10.3%	Large Cap 5.6%	Mid Cap -36.2%	Asset Allocation 23.4%	Asset Allocation 12.5%	Small Cap -4.2%	Asset Allocation 11.9%	Cash 0%	Cash 0%	Small Cap -4.4%	Asset Allocation 8.8%	High Yield 7.5%	Mid Cap -11.1%	High Yield 14.3%	Fixed Income 7.5%	Fixed Income 4.5%	Asset Allocation 10.1%	Emerging Markets 0.25
Cash 4.8%	Cash 4.8%	Large Cap -37.0%	Commodities 18.9%	Developed International 7.8%	Developed International -12.1%	Fixed Income 4.2%	Fixed Income -2.0%	Emerging Markets -2.2%	High Yield -4.5%	Fixed Income 2.6%	Fixed Income 3.5%	Commodities -11.2%	Fixed Income 8.7%	High Yield 7.1%	Developed International 4.5%	High Yield 9.7%	Developed International 0.19
Fixed Income 4.3%	High Yield 1.9%	Developed International -43.4%	Fixed Income 5.9%	Fixed Income 6.5%	Commodities -13.3%	Cash 0.1%	Emerging Markets -2.6%	Developed International -4.9%	Emerging Markets -14.9%	Developed International 1.0%	Commodities 1.7%	Developed International -13.8%	Commodities 7.7%	Cash 0.5%	Cash 1.2%	Fixed Income 3.2%	Cash 0
Commodities 2.1%	Small Cap -1.6%	Emerging Markets -53.3%	Cash 0.1%	Cash 0.1%	Emerging Markets -18.4%	Commodities -1.1%	Commodities -9.5%	Commodities -17%	Commodities -24.7%	Cash 0.3%	Cash 0.8%	Emerging Markets -14.6%	Cash 2.2%	Commodities -3.1%	Commodities -4.0%	Cash 0.5%	Commodities -0.31

Asset Class Key

Large Cap:	S&P 500	Developed International:	MSCI EAFE	Fixed Income:	Bloomberg Barclays US Agg
Mid Cap:	S&P 400	Emerging Markets:	MSCI Emerging Markets	Treasury Bills:	Bloomberg Barclays 1-3M Treasury Bills
Small Cap:	Russell 2000	High Yield	Bloomberg Barclays US Corporate High Yield	Commodities:	Bloomberg Commodity Total Return Index

Hypothetical Asset Allocation Portfolio Weights

Large Cap:	40%	Developed International:	9%	Fixed Income:	30%
Mid Cap:	4%	Emerging Markets:	3%	Treasury Bills:	3%
Small Cap:	4%	High Yield	5%	Commodities:	2%

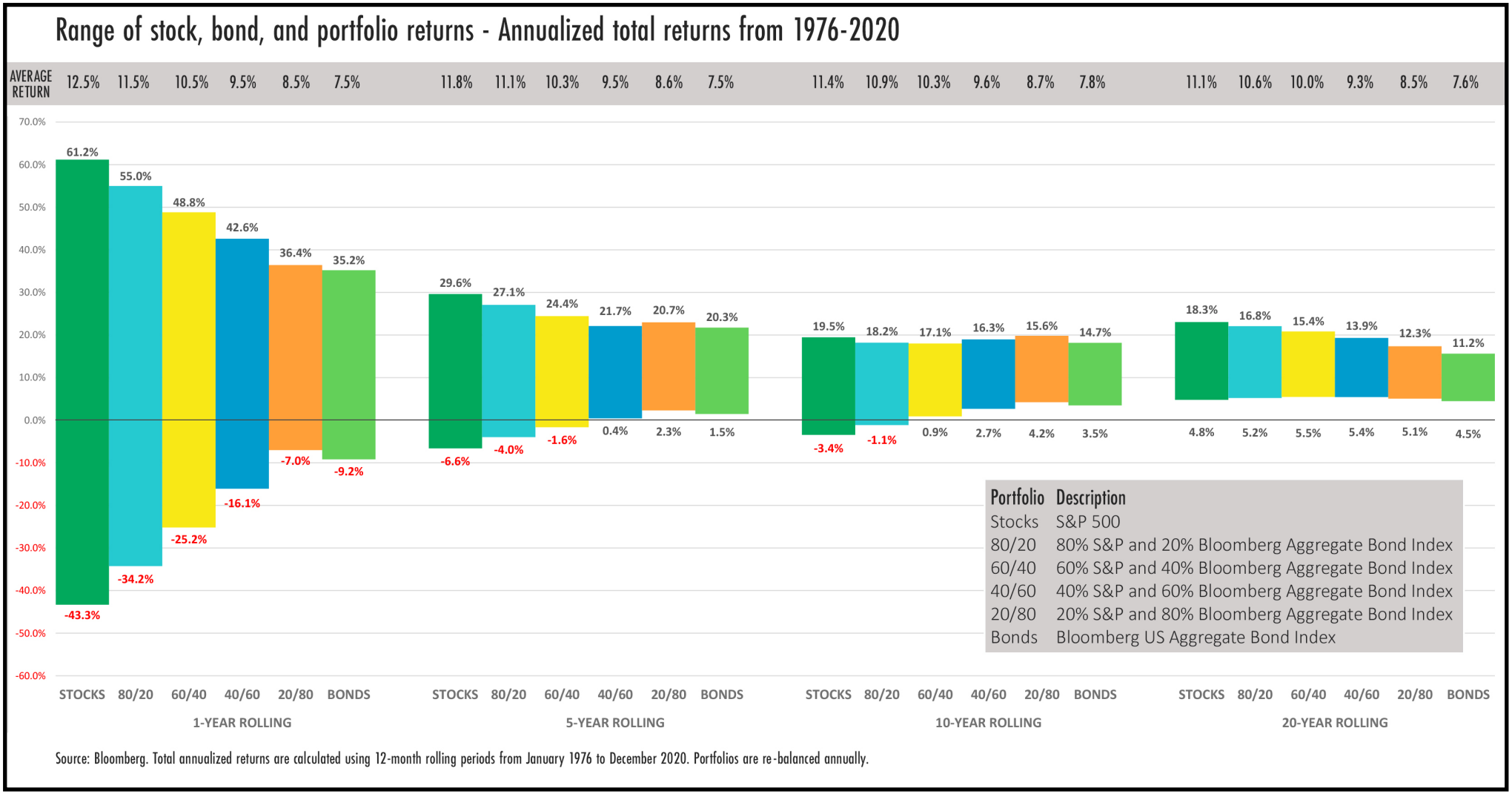
SOURCE: Bloomberg

Remember the value of time

The following chart displays the performance of various stock and bond portfolios over rolling periods. Our time-period runs from January 1976 through December 2020 – this is the longest possible data period we have for both the S&P 500 (stocks) and Bloomberg Barclays Aggregate Bond index (bonds).

As the rolling time-period increases, the value of the lowest return increases and the range of outcomes (high – low) decreases. Markets can be extremely volatile in the short-term and equity drawdowns can be severe and occur suddenly.

The longer the investment time horizon the greater the odds of positive returns. Time invested in the market matters more than market timing.



SOURCE: Bloomberg

DISCLOSURES:

Content in this material is for general information only and not intended to provide specific advice or recommendations for any individual.

The economic forecasts set forth in this material may not develop as predicted and there can be no guarantee that strategies promoted will be successful.

Financial planning is a tool intended to review your current financial situation, investment objectives and goals, and suggest potential planning ideas and concepts that may be of benefit. There is no guarantee that financial planning will help you reach your goals.

Likewise, it is important to remember that no investment strategy assures success or protects against loss. Past performance is no guarantee of future results. Asset allocation does not ensure a profit or protect against loss. There is no guarantee that a diversified portfolio will enhance overall returns or outperform a non-diversified portfolio. Diversification does not protect against market risk. All investing involves risk which you should be prepared to bear.

Rebalancing a portfolio may cause you to incur tax liabilities and/or transaction costs and does not assure a profit or protect against a loss.

All indexes mentioned are unmanaged indexes which cannot be invested into directly. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. Past performance is no guarantee of future results.

The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The S&P Midcap 400 Stock Index is an unmanaged index generally representative of the market for the stocks of mid-sized US companies.

The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.

The prices of small cap stocks and mid cap stocks are generally more volatile than large cap stocks.

The Bloomberg Barclays U.S. Aggregate Bond Index is an index of the U.S. investment-grade fixed-rate bond market, including both government and corporate bonds.

The Bloomberg Barclays US Treasury Bills 1-3 Month Index is designed to measure the performance of public obligations of the U.S. Treasury that have a remaining maturity of greater than or equal to 1 month and less than 3 months. The Index includes all publicly issued zero coupon U.S. Treasury Bills that have a remaining maturity of less than 3 months and at least 1 month, are rated investment grade, and have $300 million or more of outstanding face value.

Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.

The Bloomberg Barclays Capital US Corporate High Yield Bond index is an index representative of the universe of fixed-rate, non-investment grade debt.

The Bloomberg Commodity Total Return index is composed of futures contracts and reflects the returns on a fully collateralized investment in the BCOM. This combines the returns of the BCOM with the returns on cash collateral invested in 13 week (3 Month) U.S. Treasury Bills.

The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings.

"https://www.bloomberg.com/quote/BCOMTR:IND#skip-taboola-ads"The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. The MSCI EAFE Index consists of the following developed country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland and the UK.

The MSCI EM (Emerging Markets) Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the emerging market countries of the Americas, Europe, the Middle East, Africa and Asia. The MSCI EM Index consists of the following emerging market country indices: Brazil, Chile, Colombia, Mexico, Peru, Czech Republic, Egypt, Greece, Hungary, Poland, Qatar, Russia, South Africa. Turkey, United Arab Emirates, China, India, Indonesia, Korea, Malaysia, Philippines, Taiwan, and Thailand.

International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.