Allspring

It's Time in the Market, Not Market Timing!

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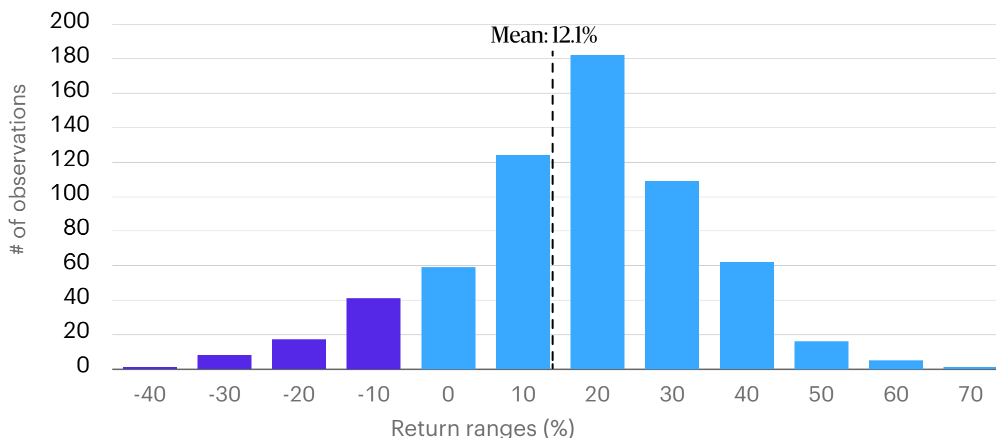
After a tumultuous 2022, investors are struggling to prepare for what's ahead. Equity losses over short periods of time can paralyze decision-making, especially when planning for the future.

Patience is a virtue.

It's important to remember that while equity market downturns are a normal occurrence, periods of extreme losses have been comparatively infrequent. Figure 1 shows a frequency distribution of S&P 500 Index 12-month returns, rolling monthly from June 1970 through May 2023. Over time, losses of 20% or more have occurred in less than 5% of all time periods. In fact, if history is a guide, investors could potentially realize an attractive return if they keep their capital invested over a full market cycle.

FIGURE 1: FREQUENCY DISTRIBUTION OF 12-MONTH S&P 500 INDEX RETURNS



Sources: Allspring and eVestment Alliance. Data from June 1970 through May 2023. **Past performance is not a reliable indicator of future results.**

+ Patient investors have been consistently rewarded:

21% of all observations had returns **greater than 25%.**

20% of all observations had a **negative 12-month** return.

Only 10.7% of all observations had returns **below -10%.**

Only 4.2% of all observations showed **-20%** returns or more.

Recoveries have rewarded patience.

Market drawdowns can be painful—particularly for corrections of -10% or more. However, investors can take solace in the pattern of rapid recoveries that markets have demonstrated following them. Figure 2 lists all calendar-quarter drawdowns of -10% or more since June 1970 and illustrates the remarkably powerful cumulative returns that have occurred in the following 1-, 3-, and 5-year periods. The average 1-year return following a correction has more than made up for the average initial loss. Moreover, the average annualized 3- and 5-year returns following corrections have far outpaced the mean 12-month return for the index, giving credence to the claim that one of the most powerful forces in markets is mean reversion. Investors who sold during corrections would have missed out on these market recoveries.

+ Outsized returns in years following market corrections have rewarded investors' patience.

FIGURE 2: CUMULATIVE RETURNS IN PERIODS FOLLOWING A -10% OR GREATER DRAWDOWN

>=10% DRAWDOWN	DRAWDOWN (%)	1 YR (%)	3 YR (%)	5 YR (%)
Q2 2022	-16.10	12.18	N/A	N/A
Q1 2020	-19.60	56.35	66.84	N/A
Q4 2018	-13.52	31.49	100.37	N/A
Q3 2011	-13.87	30.20	86.05	113.44
Q2 2010	-11.43	30.69	66.20	122.47
Q1 2009	-11.01	49.77	87.99	161.06
Q4 2008	-21.94	26.46	48.59	128.19
Q3 2002	-17.28	24.40	59.01	105.13
Q2 2002	-13.40	0.25	26.96	66.31
Q3 2001	-14.68	-20.49	12.63	40.08
Q1 2001	-11.86	0.24	1.91	21.48
Q3 1990	-13.74	31.16	64.60	121.43
Q4 1987	-22.53	16.61	48.79	108.91
Q3 1981	-10.23	9.91	66.16	150.64
Q3 1975	-10.95	30.44	40.13	91.23
Q3 1974	-25.16	38.14	72.88	117.97
Averages	**-15.46**	**22.99**	**56.61**	**103.72**

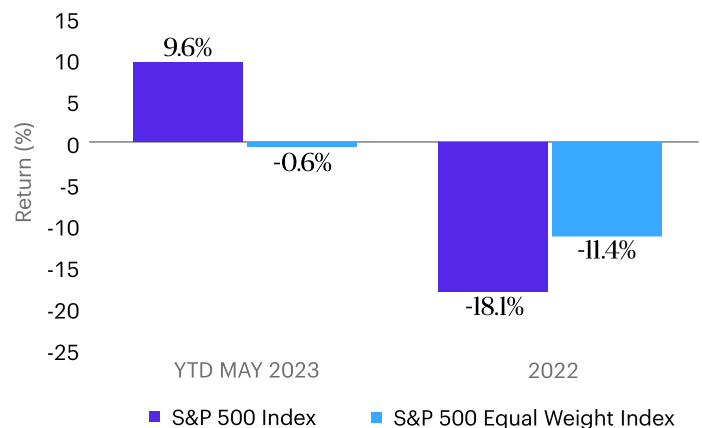
Sources: Allspring and eVestment Alliance. Figure 2 presents all calendar-quarter drawdowns of -10% or more and subsequent cumulative returns from June 1970 through May 2023.
Past performance is not a reliable indicator of future results.

Active management can help reduce the impact of mega caps on portfolio performance.

More recently, we've seen significant return dispersion from the outsized contributions of a handful of mega-cap companies in the post-COVID era. In Figure 3, we contrast the performance of the standard, value-weighted S&P 500 Index with the equal-weighted S&P 500 Index since 2022[1]—the equal-weighted index mutes the influence of the megacap companies on index performance. As shown, the value-weighted index significantly underperformed the equal-weighted index in 2022 and then drastically reversed its fortunes to date in 2023. Much of the dispersion is driven by just a few tech-oriented names—including Apple, Microsoft, Amazon, NVIDIA, Alphabet, Tesla, and Meta—which together make up nearly 28% of the S&P 500 Index by value.[2]

+ Active management can help reduce the volatility resulting from high index concentration.

FIGURE 3: S&P 500 INDEX AND S&P 500 EQUAL WEIGHT INDEX PERFORMANCE FOR 2022 AND YEAR-TO-DATE 2023



Sources: Allspring and eVestment Alliance. Year-to-date performance is through May 2023. **Past performance is not a reliable indicator of future results.**

1. A value-weighted index assigns a market value weight to each index constituent. An equal-weighted index assigns the same weight to each index constituent.
2. Source: FactSet, as of June 23, 2023

We believe active approaches can limit the impact that stretched mega-cap names can have on portfolio risk. Moreover, from an intermarket perspective, U.S. equities are not the only game in town. Cheap relative valuations of international stocks also present an attractive opportunity to overweight allocations to markets that have historically generated very attractive returns but are currently on sale relative to U.S. equity markets.

Let's recap.

In the long term, investors' strategic allocations among the various asset classes that make up their broader portfolios account for the lion's share of their expected returns and risks. We leave readers with two takeaways:

01 Staying invested with patience and discipline through difficult periods will provide the best opportunity to realize longer-term strategic goals.

02 Active management and tactical allocation can help investors add value to their strategic allocations in markets with narrow leadership.

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