Where You Finish Could Depend on Where You Start

November 15, 2014

by Robert Isbitts

of Sungarden Investment Research

Sungarden
Investment
Research 2014

Consider the table above. It contains 11 different investments and their 5-year returns. This is about as comprehensive a view as many 401k participants get from their providers – a list of past returns from which to either make a decision about where to invest their nest egg, or do more research. But while that is a sad fact for many, the goal is this article is for you to view those returns and ask yourself which one you would choose to invest in if you only had the ability to choose one.

Would you go with K, the one with the best return over the past five years? I imagine many would. Would you avoid A and B because they did poorly? I suspect they would not win too many investment beauty contests. Or, would you ask if there was an option to just invest in a money market fund and earn little or no return, given that seven of the 11 choices have produced negative 5-year returns? What would you do?

OK, now it is time to tell you what you are looking at…it is an optical illusion. The investment returns shown are all annualized returns for the S&P 500 Index as of October 31. The difference between them is that each "investment" of five years in the S&P 500 has a different ending year. For instance, investment A is the S&P's return for the five years ending 10/31/2004. B is the 5 years ending 10/31/2005, and so on until investment K, which is the S&P's very strong 5-year compounded return through 10/31/2014.

What's the point?

The fact that the S&P 500's five-year return is now higher than its been at any October-end period in the past 11 years should give you pause. This does not mean we think people should abandon the stock market. Rather, they should be figuring out ways to extract some of its potential upside, but have a plan to win the war against the downside.

In reality, we don't get to choose what market environment we start to invest into. But not recognizing at what point you are in history and market cycles, and simply hoping for the best is not a strategy.

So, it helps to be aware of the many possible outcomes and adjust your strategy to sync with the current record price highs in this popular market benchmark. Doing so can help you be more successful, regardless of what the next five years may bring. In this sense, it is not where you finish, its where you start.

www.sungardenresearch.com