

Nordea

# Time beats timing



## Introduction

Many individuals and families are currently not enjoying the potential benefits of long term investing. Historically, risk free deposit rates have been significantly more attractive than now, where people in some cases even are experiencing negative rates. One way to potentially achieve better returns is to take an appropriate level of risk and invest in the broad equity market.

We do acknowledge that for non-professionals it can be highly complex to navigate in the financial markets, and it becomes even more difficult when trying to find answers through medias as well as social platforms, where answers can be many and often wrong. We see mainly two reasons for this;

- 1) The medias tend to focus on short term market development- and expectations. This is the nature of news, and while the entertainment value is high, it is our view that most retail investors would be better off with a more balanced information stream of short term news and long term research.
- 2) The internet is a place where anyone can share views, ideas and even recommendations. The information has an extreme degree of variation in quality, and while they are free of charge and often based on good intentions, they can be costly for the investors following them.

We have identified timing as one of the main sources to complexity, uncertainty and even myths. Our advice for most customers has always been “don’t even try to time the market”<sup>1</sup>, and we can illustrate this by breaking down historical returns with- and without the best days. Interestingly, missing out on the 10 best days since 2000 would reduce the return from 165% to 41%<sup>2</sup>! Now, one would need to be very unlucky to end up in such a scenario, but the example emphasizes the point very well. Our aim with this publication is to dig deeper and provide an information foundation enabling you to make the right decisions.

We have formulated 3 myths based on the most common questions we get, and we have either confirmed or busted the myth after crunching 50 years of historical data. No one knows what the future brings, but we strongly believe that we can learn from the past. The myths in this publication are:

- 1) Time is your friend
- 2) Never invest all at once
- 3) Wait for the dip

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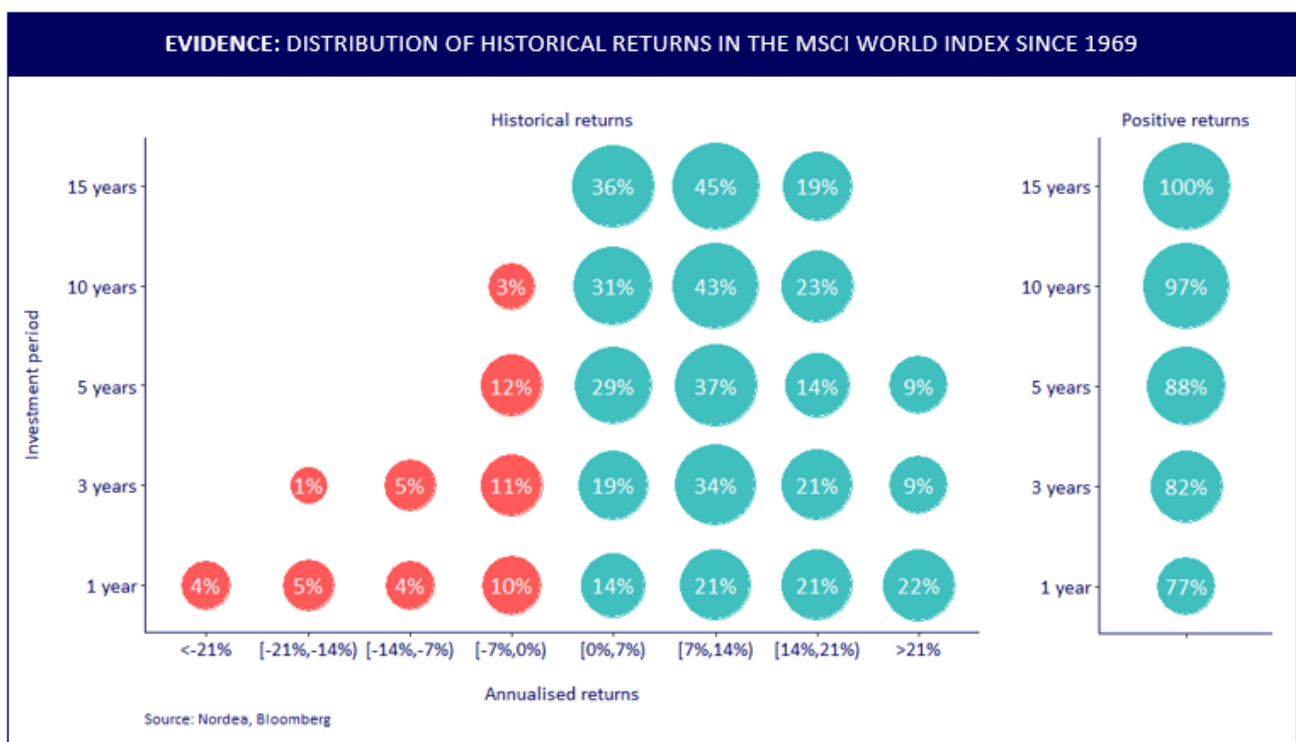
<sup>1</sup> There are several important differences between this and the tactical bets done by the Nordea House View team. Our team consists of 10 highly skilled investment professionals who follows the market constantly, and the bets are adjustments of in most cases 5% of the portfolio as an overlay to the long-term strategic asset allocation.

<sup>2</sup> Based on calculations with daily frequency for MSCI World Total Return Index in USD from 31/12/1999 to 20/01/2021. Source: Nordea, Thomson Reuters.

## Myth 1: Time is your friend – CONFIRMED!

*“Time is your friend when it comes to investing in equities, and the earlier you start, the better your odds will be despite times of uncertainty and even crises.”*

**Conclusion:** Based on historical data time has indeed been the investors’ friend in the equity market! In the short run, the market can be rough and brutal, but what we have learned by dissecting the data is, that even with a relatively short time horizon of 1 year the historical risk of having a negative return has only been 23%. This risk has been gradually reduced by adding to the time horizon, and no matter how unfortunate the timing would have been, no investor has historically realized a loss with a time horizon of more than 12 years historically, when investing in the broad global equity market<sup>3</sup>.



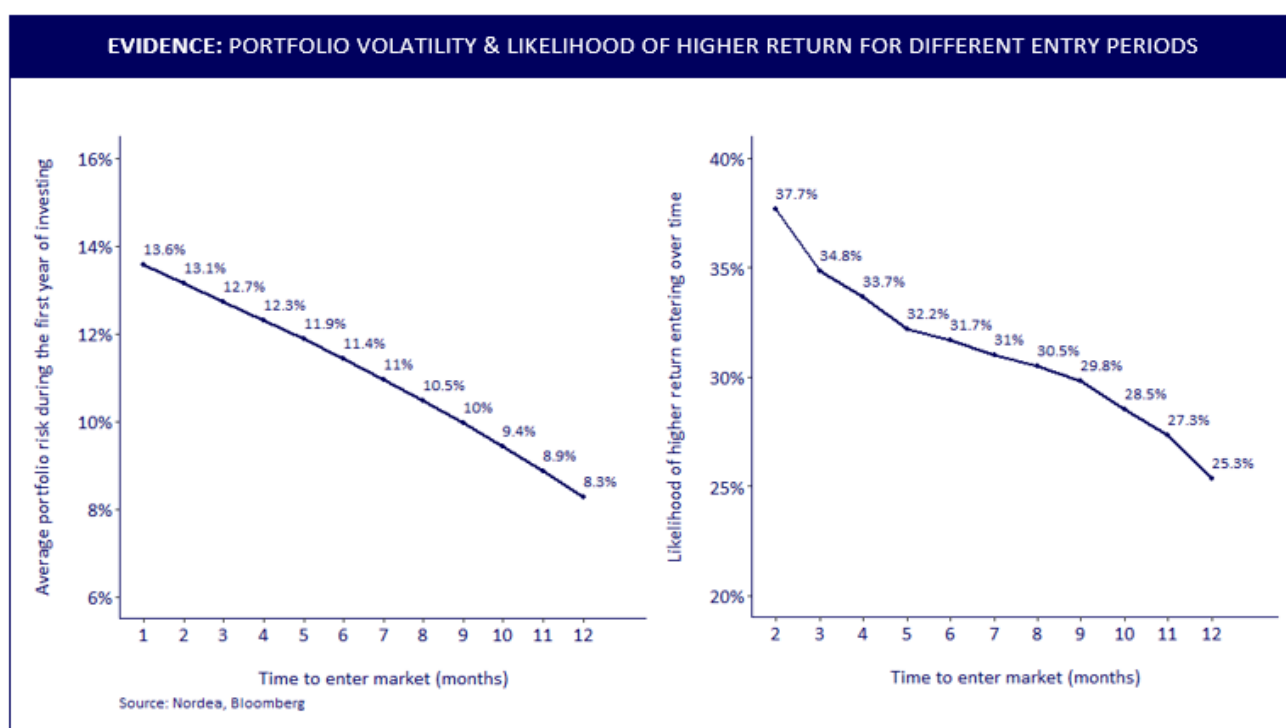
**Methodology:** We tested the myth by looking at monthly historical data for MSCI World Net Total Return USD Index from the end of 1969 to the end of 2020. MSCI World is a commonly used global index and provides us representative data on the general development in the global equity market. To see if time is your friend we tracked the returns for all the available rolling 1, 3, 5, 10, and 15-year periods. We calculated the rolling returns as follows. In December 1969 we calculated the return for each of the different time horizons. We then shifted the data one month ahead and repeated the calculations. The calculation process was repeated until the end of the dataset was reached. This means we calculated the returns for every time horizon, starting on every month, as long as enough data was available, for 50 years. Conclusions were then made based on the findings.

<sup>3</sup> Based on calculations with monthly frequency on MSCI World Net Total Return USD Index. Source: Nordea, Bloomberg.

## Myth 2: Never invest all at once – BUSTED!

*"If you have an investable lumpsum, you should never invest all at once due to the risk of the equity market crashing immediately after you have entered, which will leave you with a significant loss of capital. Instead, you should split up your investments over time to mitigate this risk."*

**Conclusion:** We learned from the first myth, that with a sufficiently long time horizon, even the most unlucky investors have ended up with positive returns in the broad equity market. Further, the historical data reveals, that splitting up your investment over a time span reduces your average returns, and the longer the entry period, the more of the returns you give up compared to investing all at once. Therefore, investors have been better off investing all at once historically, and therefore this myth is busted! We do acknowledge that the risk is reduced by splitting up the investment, and that each investor of course need to invest according to their financial situation, investment objectives, including time horizon and risk tolerance. Still, our general philosophy is to find the right individual risk level through a mix of assets rather than splitting up equity investments over time.

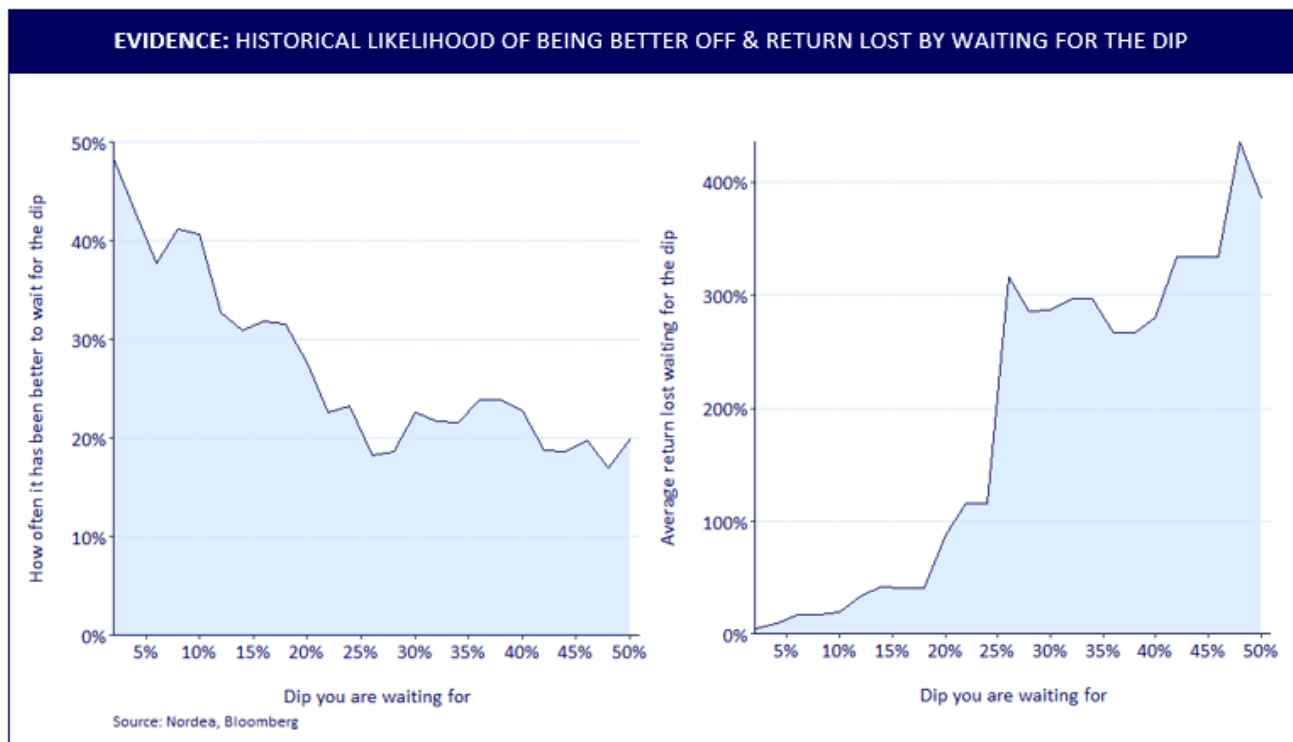


**Methodology:** We tested the myth by looking at monthly historical data for MSCI World Net Total Return USD Index from the end of 1969 to the end of 2020. We decided to look at one-year periods and how entering the market over time affected the risk and return. After the one-year periods the investor is fully invested, and the conclusions will therefore not change if we extended the holding period to more than one year afterwards. In the dataset we have 600 unique one-year periods with monthly data. For all the one-year periods we tested the risk and return an investor would have received historically by investing all at once. This is the 1-month point in the graphs. We also tested the risk and return the investor would have received by instead splitting up the investment in equal amounts from 2 to 12 months. This means we have checked the performance of each strategy, starting at any given month for 50 years. We analysed the results and made conclusions based on the findings. The risk is calculated as the annualized standard deviations of returns.

## Myth 3: Wait for the dip – BUSTED!

*"If you are looking to invest your wealth, you should stay on the side-lines and wait for the market to drop before you enter. By doing so, you will enjoy a higher return, as you will buy with a discount!"*

**Conclusion:** Historically, waiting for the market to drop, has not been the winning strategy in the equity market! The data reveals that investors waiting on the side-lines, have had the odds against them, and the odds as well as the average returns have become increasingly unattractive as the required market drop magnitude increases. The reason for this comes back to the first myth, where we learned that time has been the investors' friend in the equity market, and the discount by waiting for the dip has simply been more than offset by the fact that the equity market has gone more up than down over time. As an example, waiting for a 10% drop is rather unattractive, if the market increases by 20% before this opportunity arises.



**Methodology:** We tested the myth by looking at monthly historical data for MSCI World Net Total Return USD Index from the end of 1969 to the end of 2020. For each month since December 1969, we have tested what the index value was, compared to the index values after the next drawdowns of different sizes. If the value was lower after the drawdown you would have been better off waiting. If the value was higher after the drawdown you would have been better off by investing straight away. We performed the above test for 51 years and tested the results over 600 different starting points. The results were analysed and we concluded based on the findings.

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## IMPORTANT INFORMATION

Past performance is no guarantee of future return. Investments imply risk.

Nordea gives advice to private customers and small and medium-sized companies in Nordea regarding investment strategy and concrete generic investment proposals. The advice includes allocation of the customers' assets as well as concrete investments in national, Nordic and international equities and bonds and in similar securities. To provide the best possible advice we have gathered all our competences within analysis and strategy in one unit - Nordea Investment Center (hereafter "IC").

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