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October 2023 Crescent Commentary

"The 60-40 Investment Strategy Is Back After Tanking Last Year" (April 2023)

"The Trusted 60-40 Investing Strategy Just Had Its Worst Year in Generations…Wall Street's boilerplate mix of stocks and bonds isn't cutting it anymore" (October 2023)
Source: The Wall Street Journal

The two headlines above were published six months apart this year. The first headline seems optimistic, declaring that an allocation of 60% stocks and 40% bonds "is back". The second headline, published six months later, seems to suggest the exact opposite: the author tells us the 60 /40 allocation "isn't cutting it anymore".

With two headlines in a reputable news source appearing to contradict each other just six months apart, it's no wonder a lot of investors are confused about what to do right now. Part of the issue stems from the nature of the media. Obviously, publications want to publish what's top of mind with readers right now. And after several years of losses in both bond and stock markets, readers have an interest in this topic.

The problem with the above headlines is that they teach investors the wrong lessons about investing. The headlines imply that investors should change their opinion about an investment strategy based on how it has performed over six months. Yet the most successful investors in history preach the need to look at investing as a long-term process. For example, Warren Buffett says "we recommend not less than a five-year test as a rough yardstick of economic performance."(1)

Instant gratification seems to have intensified in our society with the rise of technology and smart phones. You can order things online and expect to have them delivered the same day. You can get instant response to an electronic message where you used to have to wait for the mail. You can watch TV shows anytime, anywhere, rather than waiting for the scheduled time on your living room TV. There are many more examples. Allowing instant gratification to seep into investment strategy is dangerous.

Owning a diversified mix of stocks and bonds has worked as an investment strategy over the past decade, over the past several decades, and over the past century. And as with any investment strategy, such a strategy will go through periods of stagnation. These periods can last for years. We are in the middle of one of those periods right now, with U.S. stocks down for going on three years now, and the U.S. bond market down for going on four years.(2)(3)

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U.S. financial markets have actually experienced several episodes where they were stagnant for ten years or more. We call them “lost decades”. Over the past 60 years, there were two such time periods: the 1964 to 1981 time period when U.S. stocks were flat for 17 years; and most recently, the 1999 to 2013 time period when U.S. stocks were flat for over 13 years. Despite more than a decade of stagnation in those two time periods, abandoning a sound allocation to stocks or bonds would have been a major mistake. Instead of running for the exits, investors should have been buying more or at least stayed the course with their investments. And the same is true today during the current financial market stagnation.[4][5]

The October headline at the top of this commentary states that a sound investment allocation that has worked for decades “isn’t cutting it anymore”. While it certainly has had its challenges with flat bond and stock markets over the past several years, it would be very dangerous to think that it means you should abandon the strategy. Let’s consider the most recent “lost decade” we referenced, the 1999 to 2013 time period where U.S. stocks were flat. This happened as a result of the bursting of a technology stock bubble, followed by a home price bubble. It certainly would test your patience to see financial markets do nothing for more than thirteen years. And we can definitely understand the mindset that would cause an investor to give up on investing after seeing it fail to work for so long. Many investors did sell and move to cash during this time period. Unfortunately, that was the wrong thing to do. While U.S. stocks did nothing from 1999 to 2013, appreciation since then has more than made up for the lost decade. From 1999 through October 2023, U.S. stocks have appreciated about 6.7% a year. If that return seems low, keep in mind that the starting point is 12/31/99, which was the peak of the technology stock bubble. So even if you invested everything you had at the peak of the bubble, you earned nearly 7% a year through October 2023. This is an adequate return for most people to achieve their retirement goals, and it’s well in excess of the inflation rate over the past 24 years. Another data point to keep in mind is that the long-term annual return on U.S. stocks since 1900 is roughly 7% a year, so 6.7% isn’t far off the very long-term average. But the main point I’m making is that if you had become discouraged and sold your investments because they didn’t work over the 1999 to 2013 time period, you would have missed out on the huge economic boom that would have rewarded your patience.[6]

With investing, it’s always important to block out short-term noise and focus on the long term. It’s even more important during long market corrections like the one we currently find ourselves in, when emotions of fear or frustration increase the risk that an investor makes a bad decision in the heat of the moment. Unfortunately, as investors, we are constantly bombarded by information that often doesn’t help us. More often than not, short-term data – or even opinion presented as fact – end up in the news headlines. We will continue to work with you to cut through the noise and help guide you to good decision making with your investments and financial planning.

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Sources:

(1) Berkshire Hathaway
(2) Jeremy Siegel
(3) Yahoo Finance
(4) Fortune
(5) Factset
(6) S&P Dow Jones Indices

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