How Have Premiums Performed Following Past Market Declines? Maintaining Discipline & Sticking to the Plan are Vital.

May 22, 2020 - As you may know, Dopkins Wealth Management has published numerous pieces that illustrate the importance of staying invested through difficult times. As hard as it may be, investors who have stayed in their seats have usually been rewarded.

Many advisors structure their clients' portfolios to emphasize smaller market capitalization stocks, deeper value stocks, and higher profitability stocks, and have asked how these premiums have fared following previous market downturns.

The below table reports average cumulative returns of the premiums over 1-, 3-, and 5-year periods following market downturns of 10%, 20%, and 30% for US stocks. For example, following a 20% market downturn, value outperformed growth by 7.49% on average over the subsequent 1-year. The data suggest that, overall, **premiums have tended to be positive even during difficult environments.**

Despite disappointing recent results, we continue to expect these premiums to show up every day. Investors may be tempted to extrapolate the recent past into the distant future, which can lead them to abandon their investment philosophy at potentially inopportune times. Maintaining discipline and sticking to the plan are vital. So, if your goals haven't changed, then your asset allocation likely doesn't need to change.

Furthermore, premiums can materialize quickly, and you want to be properly positioned to capture the returns when they show up. The period leading up to and shortly after the start of the 21st century provides a great example, when many wondered if value was still a relevant strategy in the so-called "new economy." Through March of 2000, the Russell 1000 Growth Index outperformed the Russell 1000 Value Index over the previous 1, 3, 5, 10, 15, and 20 year periods. One year and one market turn later, the script flipped. Through March of 2001, value stocks had regained the advantage over every one of those periods.[1] This a great example of the importance of staying disciplined.

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US Stocks, July 1963–December 2019

	Small Minus Large			Value Minus Growth			High Profitability Minus Low Profitability		
	1YR	3YR	5YR	1YR	3YR	5YR	1YR	3YR	5YR
10% Decline (N = 13)	6.31%	29.11%	49.11%	2.27%	20.82%	48.64%	4.46%	10.65%	21.88%
20% Decline (N = 5)	4.16%	4.83%	40.55%	7.49%	8.47%	29.82%	2.75%	13.21%	14.44%
30% Decline (N = 4)	13.79%	26.80%	77.60%	-2.47%	9.78%	46.00%	0.50%	8.16%	-5.23%

Past performance is no guarantee of future results.

Returns are calculated for the 1-, 3-, and 5-year periods beginning the month after a downturn of 10%, 20%, and 30%, respectively, from a new all-time high for the market. There are thirteen, five, and four observations of downturns that compose each average return for the 10%, 20%, and 30% thresholds, respectively. Market represented by the Fama/French Total US Market Research Index. Small cap and large cap stocks represented by the Dimensional US Small Cap Index and the S&P 500 Index, respectively. Value and growth stocks represented by the Fama/French US Value Research Index and the Fama/French US Growth Research Index, respectively. High profitability and low profitability stocks represented by the Fama/French US High Profitability Index and the Fama/French US Low Profitability Index, respectively. Eugene Fama and Ken French are members of the Board of Directors of the general partner of, and provide consulting services to, Dimensional Fund Advisors LP. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio. Descriptions of Dimensional and Fama/French index data available upon request.