March 2020

QS Investors
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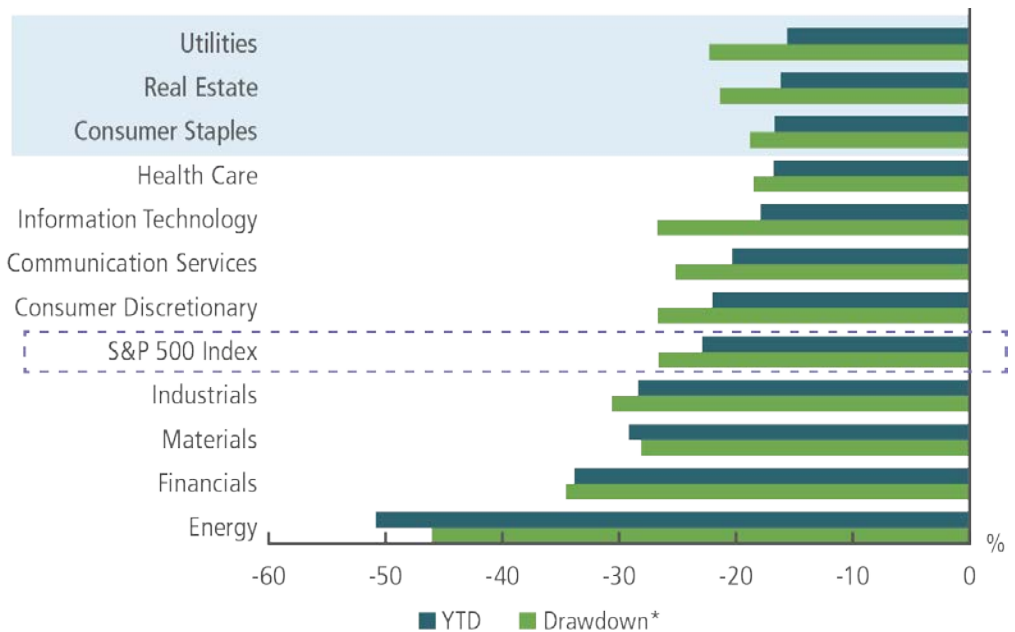
Bad News BEAR Market — No Pain, No Gain

> Year to date, we have seen low volatility, dividend-oriented sectors hold up the best, while traditional cyclical, value-oriented sectors have sold off significantly.

The S&P 500 Index was down over 9% on March 12th, 2020. This marks the single worst down day since Black Monday (October 1987) as the market grapples to price in the uncertainty surrounding COVID-19 (Coronavirus) as well as the oil supply/demand shock due to Russia resisting OPEC's proposed supply cut. As of March 12th, 2020, the US market cap-weighted index was down over 26%, officially in bear market territory, and the VIX (Volatility Index) spiked at over 75, elevated significantly from the sub-15 levels realized at the beginning of last year and throughout much of 2019.

Year to date we have seen low volatility, dividend-oriented sectors such as Utilities, Real Estate and Consumer Staples hold up the best (highlighted in blue below), while sectors traditionally considered as cyclical and value-oriented, such as Energy and Financials, have sold off significantly, down over 51% and 34% respectively year to date.

PERFORMANCE YEAR TO DATE AND DURING PEAK TO TROUGH DRAWDOWN
AS OF MARCH 12, 2020



*Peak to trough drawdown period from 2/19/20 through 3/12/20.
Source: Bloomberg, S&P 500 GICS Sector Returns.

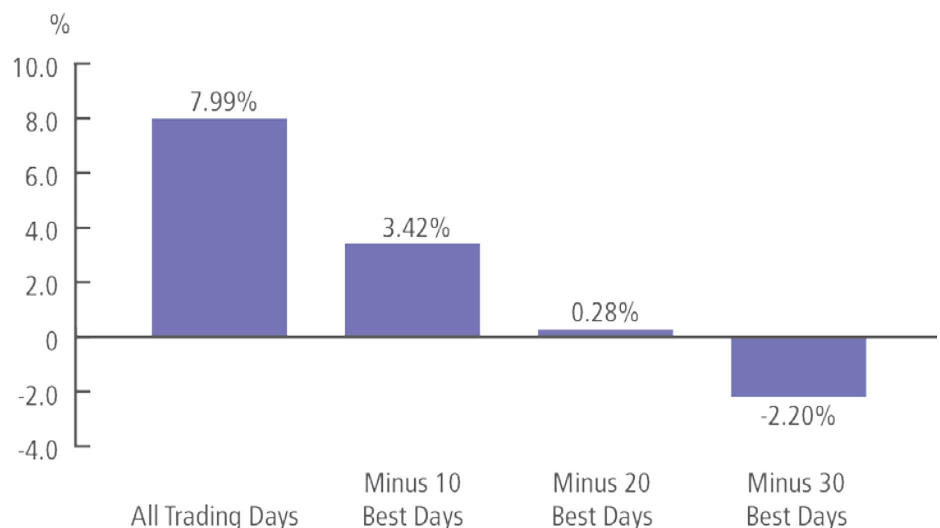
While a 9% drop on a given day is difficult for any investor to stomach, it is important to remember that corrections and bear markets happen relatively often. From 1980 – 2019 there were **13 S&P 500 market corrections,** defined as a peak to trough move of 10% or greater and **seven bear markets,** defined as a peak to trough move of 20% or greater. Despite being in an 11-year bull market, that means on average there has been one attention-grabbing downturn every two years.

It is important for investors to maintain a long-term view and an equity portfolio with a risk/return profile they can tolerate, especially in the worst of times. Historically, equity markets have delivered strong returns right after a market bottom.

Market timing has its cost. Historically, some of the best trading days have followed the worst.

Loss aversion may push investors to stay on the sidelines which may lead to missing out on gains. Timing markets is a difficult task even for the most seasoned investors, and investors lucky enough to avoid drawdowns may fail to benefit from rebounds. For example, following the aforementioned March 12th decline, the S&P 500 Index spiked over 9% on Friday March 13th, representing the largest one-day rally since 2008 (during the financial crisis). Missing just ten of the best trading days over the last ten years would have reduced returns over this period by over two-fold. Missing 20 of the best trading days over this ten-year holding period would have resulted in a near-flat return. We view a long-term, diversified and strategic mindset as the bedrock of investment strategy.

THE RISK OF MISSING OUT
10-YEAR ANNUALIZED RATE OF RETURN AS OF MARCH 13, 2020



Source: Bloomberg, S&P 500 Index.

Equities continue to be an integral component of investment portfolios, particularly as rates move lower and income from bonds is likely to be squeezed. However, the true benefit of the asset class is only realized when investors are able to stay the course. As such, it is important for investors to look at reducing their overall beta to the market through diversifying into under-exposed market

cap-weighted sectors such as Utilities, Consumer Staples and Real Estate which not only diversify total return streams through the income they provide but also allow for exposure to the low volatility factor which has shown historical strength amidst periods of heightened market volatility as well as collapsing rates. When considering a lower volatility strategy in this environment, investors should look for exposure to the dividend factor as well as a consideration for underlying fundamentals, favoring those high-conviction non-cyclicals that have the earnings power to support their dividend payouts.

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