Market Perspectives

Stock market: Play the long game

Viewing equity investments through the lens of probabilities, investors can shift the potential for positive outcomes significantly in their favour by lengthening their time horizon.

Tune out the noise

The financial media tends to be obsessed with the latest news, but for long-term investors, most daily headlines and market moves are far more likely to be noise than to contain useful and/or relevant information. Because short-term market swings often reflect significant noise and randomness, moderating the focus on the day-to-day news cycle can help investors mitigate the risk of pursuing potentially unnecessary trading activity that can be detrimental to their long-term investment objectives.

Time is on the investor's side

In a world where investors are frequently enticed to play the short game, adopting a long-term mindset can provide an advantage. As illustrated in the charts below, the probability of earning a positive return on any given trading day is essentially the same as flipping a coin. However, as the time horizon is extended, investors can be increasingly confident of attaining a positive outcome.

The probability of the TSX Composite and S&P 500 generating positive returns improves substantially over longer periods, rising to about 75%–80% for one-year rolling time periods, nearly 90% for three-year rolling periods, and approaching 100% for rolling periods beyond five years. Stated differently, the likelihood of experiencing losses in equity markets diminishes markedly as the investment horizon is lengthened.

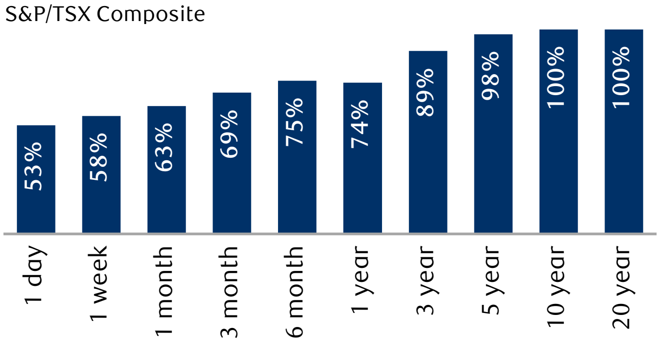
The positive compounding nature of the long game

Because uncertainty is ever present, we believe investors should always think in terms of probabilities. Time horizon is a practical tool for managing unavoidable volatility when participating in the stock market, which tends to trend upwards over the long haul. A longer time frame not only increases the likelihood of earning positive returns in stocks, but also allows the benefits of compounding to accumulate over time for investors.

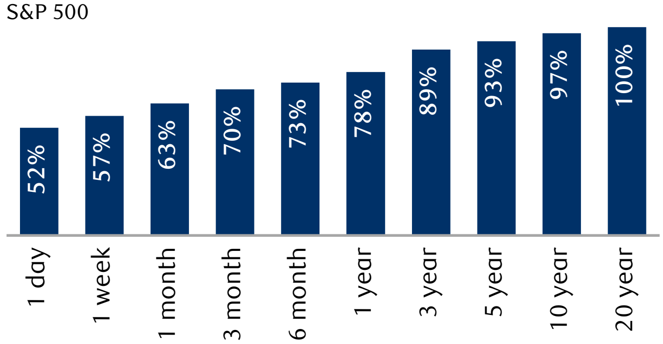
Positive returns are more likely over longer investment horizons

Percentage of positive total returns over various holding periods

S&P/TSX Composite



S&P 500



The charts above illustrate, for rolling time periods of various lengths, the percentage of those time periods that produced positive total returns on the S&P/TSX Composite Index (since 1977) and the S&P 500 Index (since 1945) through 3/31/23.

Source - RBC Wealth Management, Bloomberg

All values in U.S. dollars and priced as of Mar. 31, 2023, market close, unless otherwise noted.
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