529 Savers: Stay the Course

As the COVID-19 global pandemic continues to have a deep and wide spread impact on public health and economies the world over, we believe that a rational and conscientious perspective will go a long way in helping college savers weather this intense storm and remain on track. Therefore, we believe it is critical for 529 college savers to *stay the course* and see beyond the short-term market malaise, no matter how close or far into the future their enrollment horizons may be.

Current Assessment

With the social and economic consequences of the COVID-19 outbreak still highly uncertain, abnormally high volatility has persisted. Nonetheless, we view the outbreak as a temporary, exogenous shock to both the demand and supply sides of the global economic system, culminating in what we anticipate will be a relatively shallow, technical recession, and not a breakdown of fundamentals.

> "Our view is that once the virus is contained, output and growth should resume to its previous levels in relatively short order."
> — Barbara Reinhard, CFA, Head of Asset Allocation

Why? It is important to remember the strength of the economic starting point from which the outbreak occurred. Following the global slowdown in 2018 and early 2019, the Federal Reserve provided doses of stimulus that appeared to be laying the groundwork for a pickup in growth. There was a lot of momentum heading into year-end 2019: trade concerns had subsided, manufacturing activity was accelerating, and the U.S. stock market was setting all-time highs. Additionally, consumers have been in a fortified position for several years with labor markets tight and household balance sheets strong, which was not the case during the last bear market in 2007–2008. Although spending will certainly dip, we expect that most of the job market will hold up. In short, consumers are well positioned and should remain more resilient than in other recessionary periods, both large and small.

Staying the Course

While the equity markets have been like a roller coaster over the past several weeks, we note the importance for 529 college savers to remember a few critical points when considering what to do next.

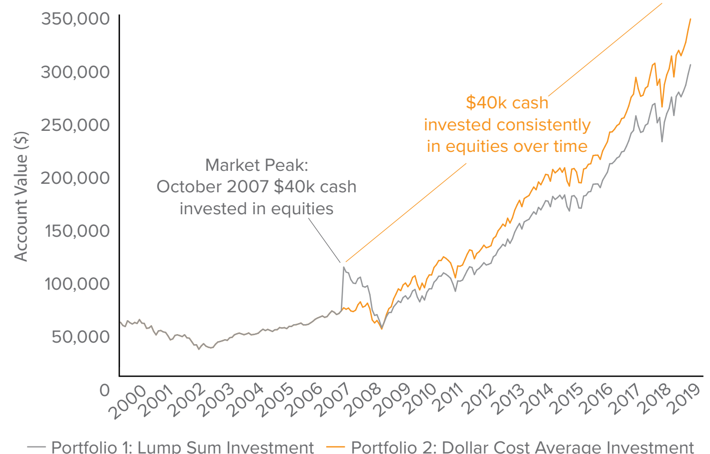
First, bull and bear market transitions, however abrupt or drawn out, are always a potential factor in any long-term investment goal, including the college saving process, no matter how unprecedented and rare the circumstances may be.

Second, as noted above, underlying economic fundamentals are strong today, and much stronger than in previous market-shock events. Indeed, current economic fundamentals strongly support a rebound once the threat from COVID-19 subsides. Optimism, in our view, is warranted.

Finally, such rapid and acute dislocations can represent great opportunities for those willing to stay the course.

As Figure 1 shows, pulling assets or holding back on contributions in downturns can cost investors down the road. In the hypothetical below, portfolios 1 and 2 start out essentially the same. Both begin with an initial investment of $60,000 with no contributions added until the market peak in 2007. But, here is where their paths diverge. Both portfolios have an additional $40,000 to invest but do so differently. Portfolio 1, caught up in the euphoria of the bull market, contributes all $40,000 at the height of the cycle and nothing more going forward, choosing to stay on the sidelines in the fallout of the Financial Crisis. Meanwhile, portfolio 2 develops a plan to consistently pay into the account no matter the market environment. By staying the course, and not getting rattled by the massive drawdown of the Financial Crisis, Portfolio 2 outperformed, by well over $40,000.

Figure 1. Lump-sum Investing vs. Dollar-Cost Averaging 20 Years Through December 2019



Source: Morningstar Direct. Data as of 12/31/19.

Past performance is no guarantee of future results.

This hypothetical example is for illustrative purposes only. It does not take into account withdrawals, fees, expenses, and taxes which would lower the results.

The Equity benchmark is represented by the S&P 500. The S&P 500 Index is an unmanaged capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The Index does not reflect fees, brokerage commissions, taxes or other expenses of investing. Investors cannot directly invest in an index.

There are no guarantees a portfolio which utilizes a dollar cost averaging method will outperform a portfolio which does not use it.

"Seeing years of savings reduced so dramatically and in such a short period is certainly a shock," commented Reinhard. "But times like these are precisely when level heads must prevail so as not to let such a sudden and drastic drawdown become a long-term detriment."

Stay safe, stay connected, and most certainly, stay the course!

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