PRIVATE WEALTH

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Asset Allocation

STOCKS VS. BONDS OVER THE PAST 153 YEARS

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In Aesop's fable *The Tortoise and the Hare*, slow and steady wins the race. But is that really how it works in life? When it comes to investing, slow and steady can be a recipe for near-certain losses.

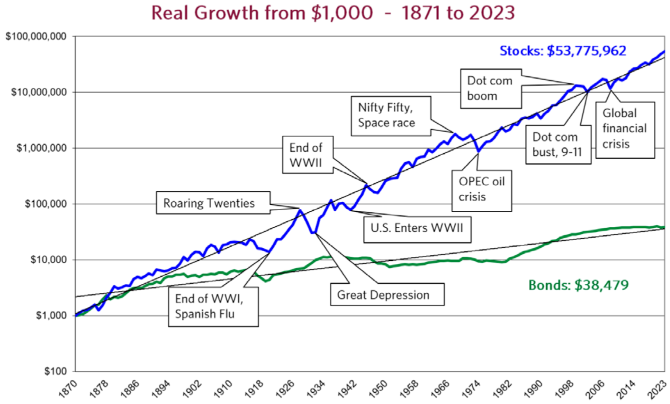
Reliable performance data first became available in 1871. So, let's look at stocks-versus-bonds returns in the 153 years since. Think of *The Tortoise and the Hare* as a story about asset allocation: of bonds, which appreciate slowly and appear reliable; and of stocks, which can appreciate strongly and quickly, but appear risky. Which is your best bet? The answer depends on what kind of race you're running.

The past 153 years have been wildly volatile: inflation, deflation, a deep depression, two global financial crises, explosive growth, two World Wars, embargoes, assassinations and worldwide pandemics. We often forget how frightening things seemed at such times. Although the world may seem scary now, it's likely that the period ahead won't be all that different from some of the periods we've experienced in the past. History repeats itself; you just don't know which part of the past you're going to get! But the past informs the future. By studying history, you can get a good idea of the range of possible outcomes going forward.

Data shows that, over the past 153 years, if you owned equal amounts of Canadian and U.S. stocks you would have enjoyed average annual growth of 9.5% (in Canadian dollars) for an inflation-adjusted (real) return of 7.4%. Over the same period, Canadian bonds averaged 4.5%, or real returns of just 2.4% per year.

Here's a graph showing 153 years of growth in stocks vs. bonds. If you started with $1,000 in each, you would now have over $53 million with stocks – but only about $38 *thousand* with bonds. Remember that these are in "real" dollars, that is, adjusted for inflation.

Real Growth from $1,000 - 1871 to 2023



Source: Siegel, Shiller, CRSP, Cdn Institute of Acutaries, TSX, Bank of Canada.

Here's a table showing the average percentage growth in stocks vs. bonds over the past 153 years. The table also compares the differences in median total dollar growth over various time horizons.

153-Year Returns

Growth in stocks vs. bonds 1871 to 2023

	Average Nominal Returns	Average Real* Returns	Average real growth from $100,000**				
			1 Year	5 Years	10 Years	15 Years	20 Years
Stocks	9.5%	7.4%	$7,416	$47,101	$112,165	$187,523	$308,811
Bonds	4.5%	2.4%	$2,400	$10,023	$19,953	$30,459	$49,129
Inflation	2.1%						
Difference in growth ($)			+$5,016	+$37,078	+$92,212	+$157,064	+$259,681
Difference in growth	2.1x	3.1x	3.1x	4.7x	5.6x	6.2x	6.3x

Source: Siegel, Shiller, CRSP, Cdn Institute of Actuaries, TSX, Bank of Canada.

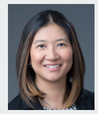
* "Real" returns are nominal returns after subracting inflation
** "Real growth from $100,000" for 5 to 20 years is the median real growth, showing the effect of compounding.

The average annual real returns from stocks were more than three times higher than those of bonds. However, because of compounding, the difference in returns grows to more than six times after 20 years: a profit of $308,811 for stocks vs. only $49,129 for bonds, on an initial $100,000 investment. So, the benefit from stocks grows as the time horizon gets longer.

Now you may be asking: But aren't stocks much riskier than bonds? Yes and no. The stock market is volatile in the short term, making stocks seem risky. But if you invest for the longer term, that is, more than five or 10 years, history shows that down markets have almost always been more than offset by up markets, giving reliable returns for stocks after inflation.

Inflation can actually make bonds riskier than stocks over the long term. Over five-year periods stocks did better than bonds 74% of the time; the chance of a negative return with bonds was nearly twice that of stocks. The average extra return for stocks was 37% higher, compared to only a 9% increase in the worst return. Over 10-year periods the worst return was about the same, and yet the median returns for stocks were 5.6 times as high. Over 20-year periods, stocks beat bonds nearly every time and never failed to beat inflation. As well, stocks' median return was 6.3 times that of bonds. By contrast, bonds lost to inflation 15% of the time, with the worst period being a loss of nearly 30% in real purchasing power. So, based on history, the longer your investment horizon, the less risky stocks are, and the riskier bonds become in comparison. At the same time, the extra returns from stocks vs. bonds grow dramatically.

The key takeaway here is that one type of asset isn't always better. How long your money is likely to be invested is critical in determining the right mix for you. If you only have a few years to invest, then most of your money should be in bonds. If you have savings earmarked for needs five to 10 years or more from now, consider investing more of those savings into stocks.



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