

Great Expectations

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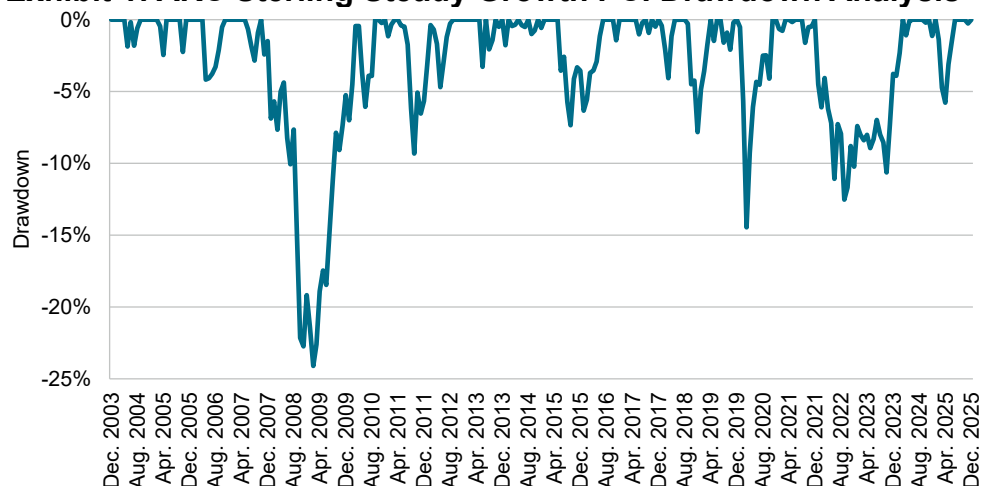
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“There’s little that’s as dangerous for investor health as insistence on extrapolating today’s events into the future” – Howard Marks¹

Despite a pivot in 2022, investors have been enjoying reasonably benign market conditions over the past 17 years. Financial markets have delivered strong performance since the 2008 Global Financial Crisis (GFC) as evidenced by the 7.1% annualized increase in the ARC Sterling Steady Growth Private Client Index (ARC Sterling Steady Growth PCI) since the March 3, 2009, low. The performance over this period compares favorably to the 5.9% annualized performance demonstrated by the index since its inception on Dec. 31, 2003.

Exhibit 1 shows the drawdown history of the ARC Sterling Steady Growth PCI since inception. The drawdown related to the GFC was a difficult experience for those invested at that time. Since then, drawdowns have been relatively shallow and short-lived.

Exhibit 1: ARC Sterling Steady Growth PCI Drawdown Analysis



Source: ARC Research, now a part of S&P Dow Jones Indices LLC. Data from Dec. 31, 2003, to Dec. 31, 2025. Past performance is no guarantee of future performance. Chart is provided for illustrative purposes.

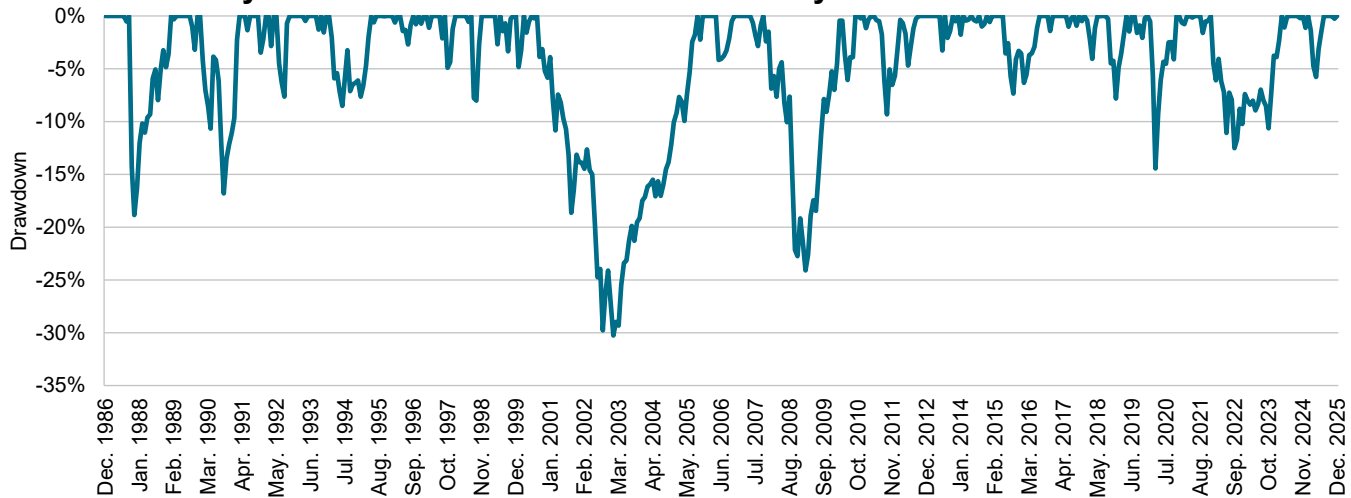
¹ “The Most Important Thing: Uncommon Sense for the Thoughtful Investor,” Columbia University Press, 2011, Chapter 8.

For the past 17 years, investors have become used to higher-than-average performance and lower-than-average risk as measured by drawdown. The past three years have been even more investor-friendly, with steady growth investors enjoying an annualized return of 8.3% over this period with only the briefest of wobbles in Q2 2025. Anomalous periods such as this can lead to what behavioral scientists call “recency bias.” Recency bias is a cognitive bias in which people place too much weight on recent events (positive or negative) and underestimate long-term trends or historical probabilities.

Supporting the view that positive recency bias might be at play, it is becoming increasingly rare to find vocal opponents of the perceived wisdom that “markets always go up in the long run” or “time in the market beats timing the market.” These bold statements may be true, but to really understand the risks related to any investment it is advisable to back-test using as much historical data as is available. In this way, it is possible to put “recent” performance into context.

The ARC Private Client Indices (PCI) are constructed using the real performance (net of fees) of over 350,000 discretionary managed portfolios. This makes the PCI a critical reference point for investors wishing to make informed decisions about their investment strategies. The one limitation of using the PCI for this purpose is that the data is only available from the start of 2004. To provide a more thorough historical perspective we have chain-linked the performance of a representative proxy portfolio (15% cash, 30% U.K. equities, 35% global equities and 20% gilts) to the actual PCI data. In this way, we have extended the period under review to 39 years, thereby incorporating several economic cycles. The results are shown in Exhibit 2.

Exhibit 2: Steady Growth Risk Profile Drawdown Analysis



Source: ARC Research, now a part of S&P Dow Jones Indices LLC. Data from Dec. 31, 1986, to Dec. 31, 2025. Performance data from Dec. 31, 2003, to Dec. 31, 2025, is that of the ARC Sterling Steady Growth Private Client Index. The ARC Sterling Steady Growth Private Client Index was launched on March 31, 2007. All data prior to such date is back-tested hypothetical data of a proxy portfolio comprising 15% cash (as represented by 1-Month Libor GBP), 30% U.K. equities (as measured by FTSE All-Share TR), 35% global equities (as measured by MSCI) and 20% gilts (as measured by ICE BofA UK Gilts TR). Past performance is no guarantee of future performance. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

This extended drawdown chart highlights the concept of start-date dependency. The PCI launch date of Dec. 31, 2003, avoided the 2000–2003 drawdown while participating in a good percentage of the recovery. In Exhibit 3, we examine each drawdown of 10% or more over this 39-year period.

Exhibit 3: Summary of Drawdowns Greater than 10%

Period	Length of Drawdown (Months)	Drawdown (%)	Peak to Trough (Months)	Trough to Recovery (Months)
October 1987–December 1988	15	-18.8	2	13
January 1990–February 1991	14	-16.8	9	5
September 2000–August 2005	60	-30.3	29	31
November 2007–August 2010	34	-24.1	16	18
January 2020–October 2020	10	-14.5	3	7
January 2022–February 2024	26	-12.5	9	17

Source: ARC Research, now a part of S&P Dow Jones Indices LLC. Data from Dec. 31, 1986, to Dec. 31, 2025. Performance data from Dec. 31, 2003, to Dec. 31, 2025, is that of the ARC Sterling Steady Growth Private Client Index. The ARC Sterling Steady Growth Private Client Index was launched on March 31, 2007. All data prior to such date is back-tested hypothetical data of a proxy portfolio comprising 15% cash, 30% U.K. equities, 35% global equities and 20% gilts. Past performance is no guarantee of future performance. Table is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

The two drawdowns that stand out from this table are the 2000–2003 Dot-Com crash and the 2008 GFC. It has been 18 years since the start of the GFC, therefore there is a large subset of the investing community that has never experienced a bear market of that magnitude and duration.

It is not immediately obvious from the drawdowns presented above, but anyone unlucky enough to have invested in the average steady growth portfolio in August 2000 would have been on quite a journey: they lost almost a third of their portfolio value in the first two and a half years; were underwater for the first five years; given hope by a brief period of positive performance, only to experience another drawdown of 24%. This second significant drawdown would have taken their portfolio back into negative territory since inception, only fully recovering and starting to make positive returns 104 months after the initial investment was made. Markets have tended to go up in the “long run,” but almost nine years of investment for zero return is probably not what most investors have signed up for.

While the probability of such an experience being repeated in the near term might be low, the reality, should it occur, is serious indeed. This type of market action experienced by our unlucky investor would seriously test the resolve of all but the most committed of the “don’t worry, markets always go up in the long run” school.

Is Recency Bias Present on Wall Street?

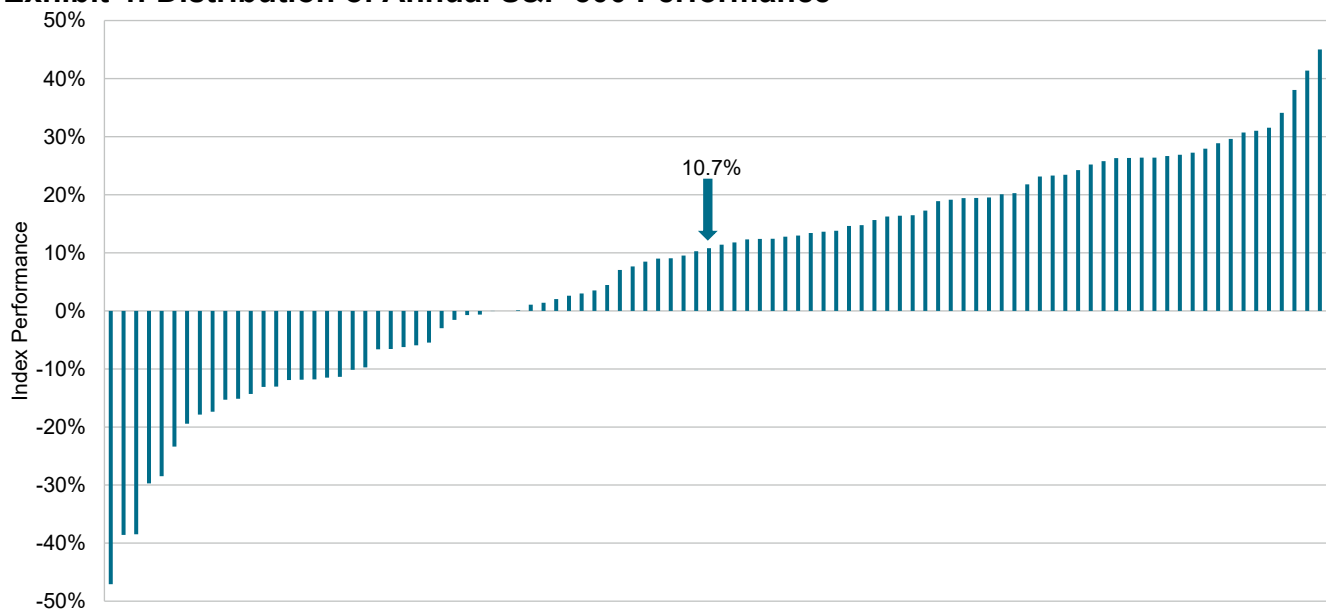
The driving force behind the exceptional returns enjoyed by steady growth investors over recent years has been the performance of equities, and more specifically, U.S. equities. The [S&P 500[®]](#) has delivered an annualized total return of 16.9% since the March 2009 low and 23.0% over the past three years.

Given this extraordinary performance, we might expect that Wall Street analysts are pricing in some sort of reversion to the mean in 2026. In fact, the opposite is true—according to research by TheStreet.com,² who collected forecasts from 21 of the leading Wall Street firms, the average target for the S&P 500 by the end of 2026 is 7,577. This equates to a year-on-year rise of 10.7% from 2025 closing levels. Maybe more surprising is that not 1 of these 21 firms expects the S&P 500 to end the year lower.

Is the expectation of a 10.7% rise in the S&P 500 evidence of recency bias among Wall Street analysts?

Examining the distribution of annual S&P 500 performance provided in Exhibit 4, we find that an (unconditional) gain of 10.7% or more for the S&P 500 is far from uncommon. Just over half (51.5%) of S&P 500 calendar year returns have been in excess of this level.

Exhibit 4: Distribution of Annual S&P 500 Performance



Source: S&P Dow Jones Indices LLC. Data from 1928 through 2025. The S&P 500 was launched on March 4, 1957. All data prior to such date is back-tested hypothetical data. Index performance in USD. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

² Blaine, C, "[Every major analyst's S&P 500 price target for 2026](#)," Dec. 29, 2025, TheStreet.

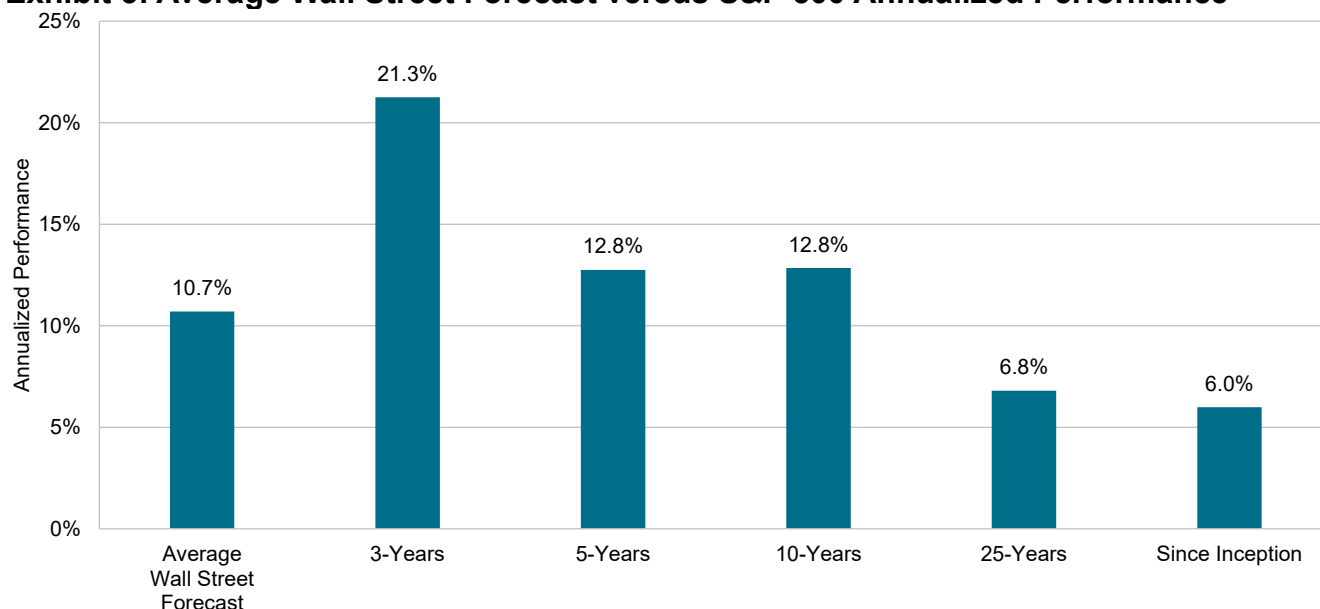
It is important to note that probabilities derived from this distribution are unconditional, meaning that there is no consideration of what has occurred before. Unlike the tossing of a fair coin, where previous outcomes have no influence on the probability of the next toss, prior rises in the value of an equity index such as the S&P 500 are economically relevant. Higher past prices imply higher current valuations of the underlying constituents and, all else equal, create a more “expensive” starting point for future returns.

With conditional probabilities in mind, a 10.7% rise in the value of the S&P 500 in 2026 would be the fourth double-digit calendar year gain in a row, something that has only happened three times in the 97 years since the inception of the index. The last occurrence was during the Dot-Com bubble (five years of double-digit returns between 1995 and 1999).

If the S&P 500 were to rise by 10.7% in 2026, this would take the four-year increase in the level of the index to 97.3%. This would be the fourth-highest rise since the end of World War II, with the three highest four-year rises (108%, 168% and 139%) all occurring during the Dot-Com bubble.

Exhibit 5 shows the annualized performance of the S&P 500 over various time periods compared with Wall Street forecasts.

Exhibit 5: Average Wall Street Forecast versus S&P 500 Annualized Performance



Source: TheStreet.com, S&P Dow Jones Indices LLC. Data from 1928 through 2025. The S&P 500 was launched on March 4, 1957. All data prior to such date is back-tested hypothetical data. Index performance in USD. Past performance is no guarantee of future results. Chart is provided for illustrative purposes and reflects hypothetical historical performance. Please see the Performance Disclosure at the end of this document for more information regarding the inherent limitations associated with back-tested performance.

The current Wall Street forecast of a 10.7% gain in the index looks somewhat conservative compared to the realized returns over the past 3, 5 or 10 years, but starts to look optimistic over longer time periods.

Anyone who has studied financial market history understands that short-term market moves are difficult to predict and anything is possible. It is entirely plausible that the S&P 500 ends 2026 higher than even the most optimistic of the Wall Street forecasts. But all things considered, it is hard not to conclude that recency bias is a factor at play when considering these S&P 500 targets.

Might Discretionary Fund Managers also Be Susceptible to Recency Bias?

Based on the 40–60 meetings with discretionary fund managers (DFMs) that ARC Research holds each quarter, we do not see any empirical evidence of the PCI Peer Group succumbing to recency bias, or at least we don't see empirical evidence of any recency bias being reflected in the form of aggressive asset allocation or excessive risk taking.

This is borne out by the results of our Q4 2025 ARC Research Market Sentiment Survey shown in Exhibit 6. Current net sentiment toward equities at 49% is only slightly above the long-term average of 40% and well below the all-time high of 79%.

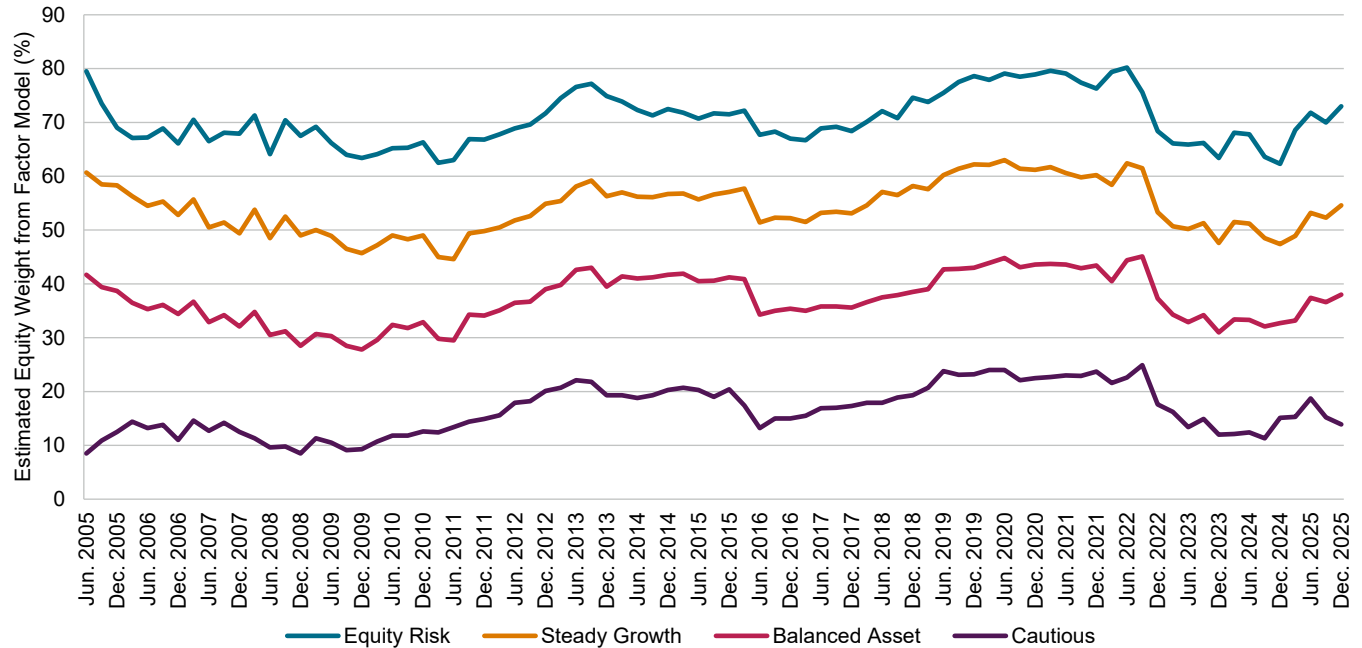
Exhibit 6: ARC Research Market Sentiment Survey: Equities – Net Sentiment



Source: Q4 2025 ARC Research Market Sentiment Survey, ARC Research, now a part of S&P Dow Jones Indices LLC. Data as of Dec. 31, 2025. Chart is provided for illustrative purposes.

The same is true when we consider the average estimated equity weight for each of the ARC Sterling Private Client Indices (see Exhibit 7). These estimates are derived from the factor model used to calculate PCI daily, monthly and quarterly performance estimates.

Estimated equity weight has tended to move in a reasonably tight range for all four of the PCI risk profiles. The most recent estimates would suggest that equity weight is currently toward the middle of the historical ranges, providing no evidence that DFMs have increased risk within client portfolios due to recency bias.

Exhibit 7: Estimated Equity Weight

Source: ARC Research, now a part of S&P Dow Jones Indices LLC. Data June 30, 2005, through Dec. 31, 2025. Past performance is no guarantee of future performance. Chart is provided for illustrative purposes.

While the majority of the peer group are positive on equities, most are also acutely aware of the risks that could unsettle financial markets in the medium term, citing factors such as equity market concentration, sovereign debt levels and private market liquidity as their major concerns (see our recent [2025 ARC Research Year in Review](#) for full details).

Conclusion

As Howard Marks observes, “there’s little that’s as dangerous for investor health as insistence on extrapolating today’s events into the future.”

Recent stock market performance has been strong, resulting in above-average performance for private client investors with discretionary managed portfolios. This could be seen by less experienced private clients as confirmation of the belief that “markets always go up in the long run” and that it’s all about “time in the market not timing the market.”

The conditions are well set for recency bias to creep into the minds of the unsophisticated investing public, leading to expectations of unrealistically high returns for the foreseeable future combined with the belief that there is little or no risk to their capital (in the long run). These elevated expectations are arguably being reinforced by the press and by Wall Street.

This presents a challenge for DFMs. The primary responsibility of the DFM is to manage portfolios in line with each individual client’s investment objective and risk tolerance. Recency bias may embolden their clients to seek a risk profile that could result in short-term drawdowns

that exceed their tolerance for loss and test their resolve. In the worst-case scenario, should markets enter a prolonged bear market, these clients might capitulate at exactly the wrong time, leaving the strategy in tatters and the investment objective unachievable.

The suitability assessment is a crucial part of the process and the opportunity for the DFM to ensure that the client fully understands the potential risk related to the proposed investment strategy. The importance of setting realistic expectations at the outset, based on a thorough understanding of how markets have performed over multiple cycles, cannot be underestimated and remains central to protecting clients from the behavioral errors that undermine long-term investment outcomes.

About ARC Research

ARC Research—now part of S&P Dow Jones Indices—specializes in converting investment performance and fee data into actionable intelligence, while also assessing how investment firms deliver value to clients. With over 145 contributing firms and more than 375,000 portfolios, the ARC Wealth Indices offer a real-world reflection of professionally managed wealth. ARC Research complements S&P DJI's commitment to objective, transparent and rules-based benchmarking by expanding its capabilities into the private wealth space. Together, the firms promote greater clarity and data-driven decision-making across both the institutional and individual investment landscapes.

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Performance Disclosure/Back-Tested Data

The ARC Sterling Steady Growth Private Client Index was launched on March 31, 2007. The S&P 500 was launched on March 4, 1957. All information presented prior to an index's Launch Date is hypothetical (back-tested), not actual performance. The back-test calculations are based on the same methodology that was in effect on the index Launch Date. However, when creating back-tested history for periods of market anomalies or other periods that do not reflect the general current market environment, index methodology rules may be relaxed to capture a large enough universe of securities to simulate the target market the index is designed to measure or strategy the index is designed to capture. For example, market capitalization and liquidity thresholds may be reduced. Complete index methodology details are available at www.spglobal.com/spdji. Past performance of the Index is not an indication of future results. Back-tested performance reflects application of an index methodology and selection of index constituents with the benefit of hindsight and knowledge of factors that may have positively affected its performance, cannot account for all financial risk that may affect results and may be considered to reflect survivor/look ahead bias. Actual returns may differ significantly from, and be lower than, back-tested returns. Past performance is not an indication or guarantee of future results. Please refer to the methodology for the Index for more details about the index, including the manner in which it is rebalanced, the timing of such rebalancing, criteria for additions and deletions, as well as all index calculations. Back-tested performance is for use with institutions only; not for use with retail investors.

S&P Dow Jones Indices defines various dates to assist our clients in providing transparency. The First Value Date is the first day for which there is a calculated value (either live or back-tested) for a given index. The Base Date is the date at which the index is set to a fixed value for calculation purposes. The Launch Date designates the date when the values of an index are first considered live: index values provided for any date or time period prior to the index's Launch Date are considered back-tested. S&P Dow Jones Indices defines the Launch Date as the date by which the values of an index are known to have been released to the public, for example via the company's public website or its data feed to external parties. For Dow Jones-branded indices introduced prior to May 31, 2013, the Launch Date (which prior to May 31, 2013, was termed "Date of introduction") is set at a date upon which no further changes were permitted to be made to the index methodology, but that may have been prior to the Index's public release date.

Typically, when S&P DJI creates back-tested index data, S&P DJI uses actual historical constituent-level data (e.g., historical price, market capitalization, and corporate action data) in its calculations. As ESG investing is still in early stages of development, certain datapoints used to calculate S&P DJI's ESG indices may not be available for the entire desired period of back-tested history. The same data availability issue could be true for other indices as well. In cases when actual data is not available for all relevant historical periods, S&P DJI may employ a process of using "Backward Data Assumption" (or pulling back) of ESG data for the calculation of back-tested historical performance. "Backward Data Assumption" is a process that applies the earliest actual live data point available for an index constituent company to all prior historical instances in the index performance. For example, Backward Data Assumption inherently assumes that companies currently not involved in a specific business activity (also known as "product involvement") were never involved historically and similarly also assumes that companies currently involved in a specific business activity were involved historically too. The Backward Data Assumption allows the hypothetical back-test to be extended over more historical years than would be feasible using only actual data. For more information on "Backward Data Assumption" please refer to the [FAQ](#). The methodology and factsheets of any index that employs backward assumption in the back-tested history will explicitly state so. The methodology will include an Appendix with a table setting forth the specific data points and relevant time period for which backward projected data was used.

Index returns shown do not represent the results of actual trading of investable assets/securities. S&P Dow Jones Indices maintains the index and calculates the index levels and performance shown or discussed but does not manage actual assets. Index returns do not reflect payment of any sales charges or fees an investor may pay to purchase the securities underlying the Index or investment funds that are intended to track the performance of the Index. The imposition of these fees and charges would cause actual and back-tested performance of the securities/fund to be lower than the Index performance shown. As a simple example, if an index returned 10% on a US \$100,000 investment for a 12-month period (or US \$10,000) and an actual asset-based fee of 1.5% was imposed at the end of the period on the investment plus accrued interest (or US \$1,650), the net return would be 8.35% (or US \$8,350) for the year. Over a three-year period, an annual 1.5% fee taken at year end with an assumed 10% return per year would result in a cumulative gross return of 33.10%, a total fee of US \$5,375, and a cumulative net return of 27.2% (or US \$27,200).

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