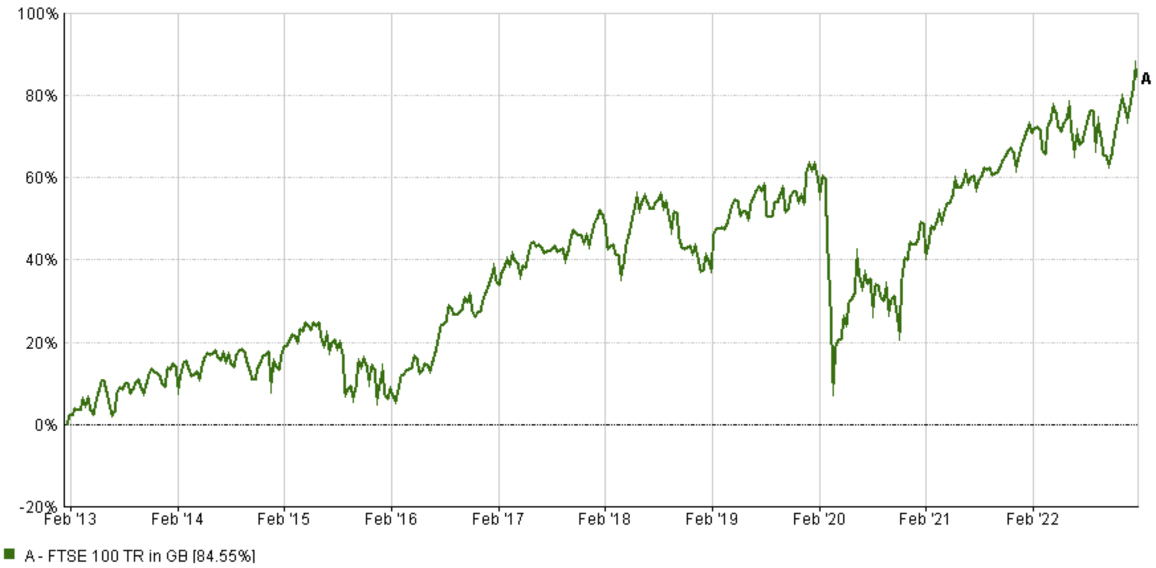
FTSE 100 research article

February 2023

The FTSE 100 is a major UK stock market index comprising the largest 100 companies by market capitalisation listed on the London Stock Exchange (LSE) and represents approximately 81% of UK public listed companies. The index began in January 1984 at a base level of 1000 and has closed above 8000 for the first time this week.



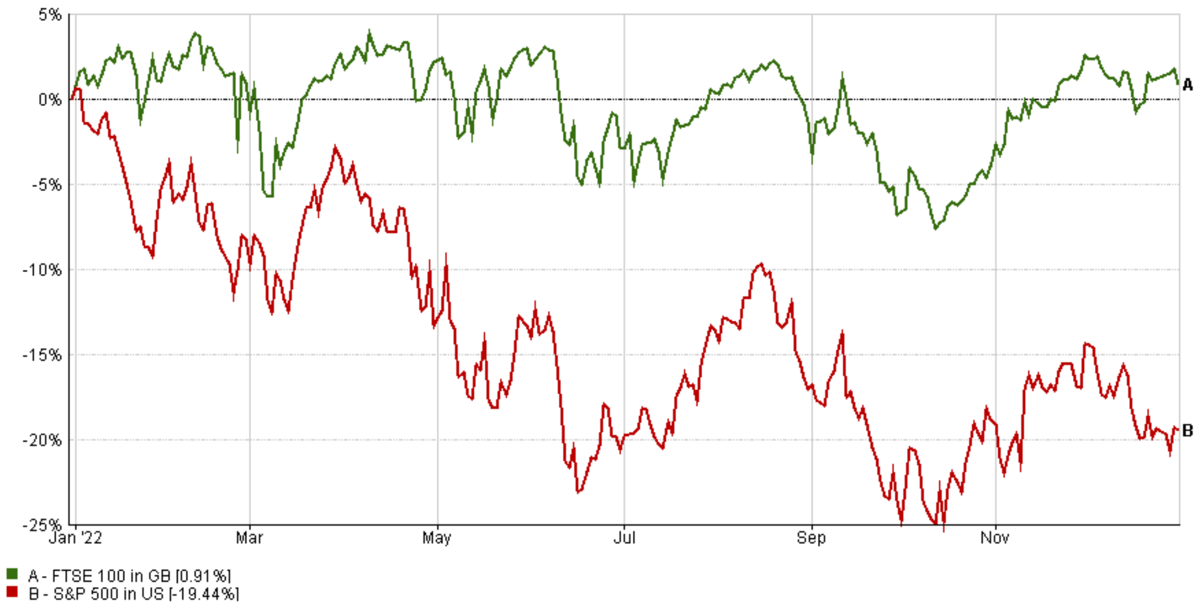
FTSE 100 performance

The FTSE 100 has returned a respectable compound growth rate of 84.55% over the past 10 years. In practice, this means that if you invested £100,000 into a FTSE 100 tracker fund in 2013, your investment would now be worth £184,550 (minus investment costs).

Despite the challenging macroeconomic environment of 2022, the FTSE 100 held up relatively well when compared with other global indices over the year.

The S&P 500 is another major index, which many people consider to be the best indicator of US stock market performance and the overall US economy.

The S&P 500 comprises the largest 500 companies measured by market capitalisation on both the Nasdaq and the New York Stock Exchange (NYSE). The FTSE 100 outperformed the S&P 500 last year. As shown below, the FTSE 100 increased by 0.91% during 2022, while the S&P 500 fell by 19.44% over the same period.



FTSE 100 vs. S&P 500 2022 performance

To explain this divergence in performance, one must look at the composition of the two indices.

The top three largest sectors in the FTSE 100 are healthcare, energy and natural resources, which make up more than one-third of the index. These sectors performed relatively well in 2022 as healthcare became a post-pandemic priority and because the Russia-Ukraine conflict drove commodity and energy prices to all-time highs.

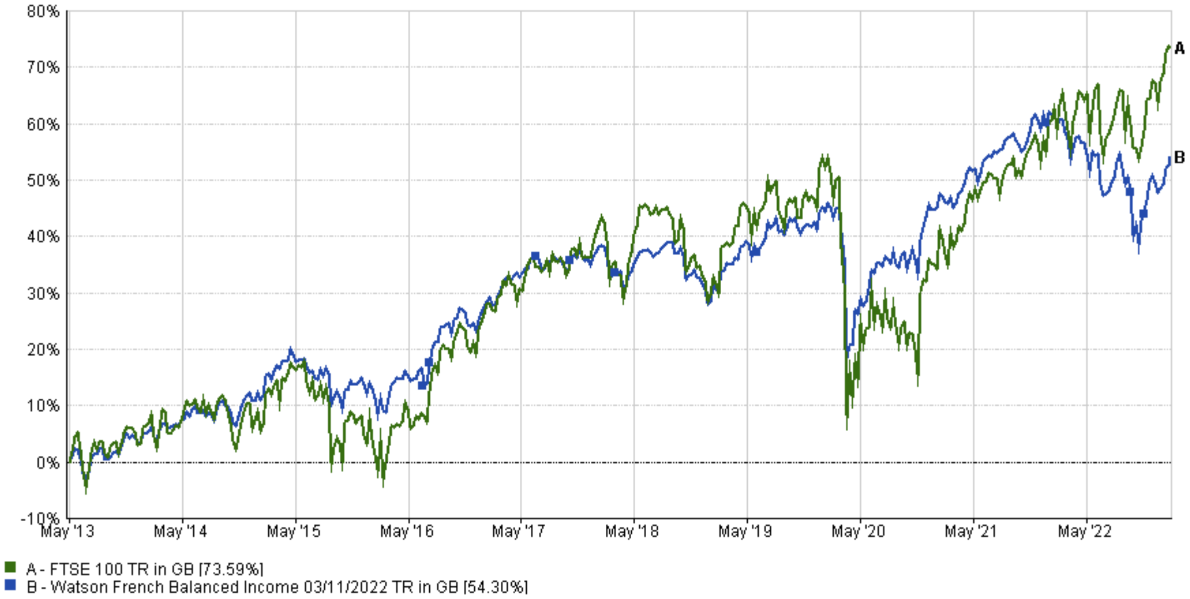
Conversely, the S&P 500 is heavily weighted towards technology companies, with 28.1% of its market value made up of companies in the IT sector. Technology companies trading at high valuations generally underperformed in 2022 due to global interest rates hikes and weak consumer confidence.

A recent article from investment manager 7iM[1] investigated this price divergence in more detail and uncovered some interesting results. Although the 2022 performance of the two indices differs by over 20%, the narrative shifts if the top 10 companies from both indices are excluded from the comparison.

The 2022 return of the S&P 500 excluding the top 10 companies was -8.8% and the return of the FTSE 100 excluding the top 10 was -9.8% over the same period. This result highlights the dependence of the FTSE on defensive sectors and the dependence of the S&P on tech stocks.

Over the past 10 years, the FTSE 100 has experienced short term volatility in the presence of changing economic conditions and black swan events such as the COVID-19 pandemic. From 2013 until now, the FTSE 100 holds a volatility figure (measured by standard deviation) of 15.45 with a maximum drawdown of -31.62. Maximum drawdown is the maximum observed loss from a peak to a trough of an investment, before a new peak is attained. Maximum drawdown is an effective indicator of downside risk over a specified time period.

[1] It's the economic cycle, stupid! | Financial advisers | 7IM



FTSE 100 vs. Watson French Balanced Income performance

A FTSE 100 tracker fund and the Watson French Balanced Income portfolio are completely different investment and cannot be directly compared. However, the chart above shows the performance of the two investments over the last 10 years. It is worth noting that our income portfolio has much lower volatility and maximum drawdown figures of 8.06 and -19.33, when compared to the FTSE 100. This shows that taking a widely diversified approach is generally effective at reducing risk.

With the FTSE 100 hitting all-time highs and closing above 8000 for the first time this week, how the index is expected to perform in 2023 is still up for debate. Many agree that an economic downturn in 2023 is already priced into the market, with most leading economic indicators suggesting that a recession is just around the corner. How painful a recession and for how long the pain lasts will likely determine the outcome of the index's performance this year. Despite the index hitting all-time highs, many investors believe that the FTSE 100, trading at 10.7 times forecasted earnings, is still relatively cheap. This indicates that there is still potential for further investment gains. Not all investors are bullish for 2023, however. A prolonged cost of living crisis, further interest rate hikes and the consequences of Brexit could all impact the performance of the major UK index in 2023.

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This article is not a recommendation to invest and should not be construed as advice. The value of an investment can go down as well as up, and you may get less back than you invested. Naturally, future investment performance cannot be guaranteed.