

Importance of Diversification in Your Sector Allocation

The below table shows the S&P 500 Index GICS (global industry classification standard) sector returns ranked from highest to lowest for the last 15 calendar years, along with the S&P 500 Index for comparison purposes. Upon inspection, it quickly becomes evident that not only does market leadership change frequently from year to year, but absolute returns vary widely as well. AAM believes a portfolio diversified across several sectors can smooth volatility and potentially increase risk-adjusted returns.

2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Information Technology 61.72	Consumer Discretionary 27.66	Utilities 19.91	Financials 28.82	Consumer Discretionary 43.08	Utilities 28.98	Consumer Discretionary 10.11	Energy 27.36	Information Technology 38.83	Health Care 6.47	Information Technology 50.29	Information Technology 43.89	Energy 54.64	Energy 65.72	Information Technology 57.84
Materials 48.59	Industrials 26.73	Consumer Staples 13.99	Consumer Discretionary 23.92	Health Care 41.46	Health Care 25.34	Health Care 6.89	Communication Services 23.49	Materials 23.84	Utilities 4.11	Communication Services 32.69	Consumer Discretionary 33.30	Real Estate 46.19	Utilities 1.57	Communication Services 55.80
Consumer Discretionary 41.30	Materials 22.20	Health Care 12.73	Telecom Services 18.31	Industrials 40.68	Information Technology 20.12	Consumer Staples 6.60	Financials 22.80	Consumer Discretionary 22.98	Consumer Discretionary 0.83	Financials 32.13	Communication Services 23.61	Financials 35.04	Consumer Staples -0.62	Consumer Discretionary 42.41
S&P 500 26.46	Energy 20.46	Telecom Services 6.27	Health Care 17.89	Financials 35.63	Consumer Staples 15.98	Information Technology 5.92	Industrials 18.86	Financials 22.18	Information Technology -0.29	S&P 500 31.49	Materials 20.73	Information Technology 34.53	Health Care -1.95	S&P 500 26.29
Industrials 20.93	Telecom Services 18.97	Consumer Discretionary 6.13	S&P 500 16.00	S&P 500 32.39	Financials 15.20	Telecom Services 3.40	Materials 16.69	Health Care 22.08	Real Estate -2.22	Industrials 29.37	S&P 500 18.40	S&P 500 28.71	Industrials -5.48	Industrials 18.13
Health Care 19.70	S&P 500 15.06	Energy 4.72	Industrials 15.35	Information Technology 28.43	S&P 500 13.69	S&P 500 1.38	Utilities 16.29	S&P 500 21.83	S&P 500 -4.38	Real Estate 29.01	Health Care 13.45	Materials 27.28	Financials -10.53	Materials 12.55
Financials 17.22	Consumer Staples 14.11	Information Technology 2.41	Materials 14.97	Consumer Staples 26.14	Industrials 9.83	Financials -1.53	Information Technology 13.85	Industrials 21.03	Consumer Staples -8.38	Consumer Discretionary 27.94	Industrials 11.06	Health Care 26.13	Materials -12.27	Real Estate 12.36
Consumer Staples 14.89	Financials 12.13	S&P 500 2.11	Information Technology 14.82	Materials 25.60	Consumer Discretionary 9.68	Industrials -2.53	S&P 500 11.96	Consumer Staples 13.49	Communication Services -12.53	Consumer Staples 27.61	Consumer Staples 10.75	Consumer Discretionary 24.43	S&P 500 -18.11	Financials 12.15
Energy 13.82	Information Technology 10.19	Industrials -0.59	Consumer Staples 10.76	Energy 25.07	Materials 6.91	Utilities -4.85	Consumer Discretionary 6.03	Utilities 12.11	Financials -13.03	Utilities 26.35	Utilities 0.48	Communication Services 21.57	Real Estate -26.13	Health Care 2.06
Utilities 11.91	Utilities 5.46	Materials -9.75	Energy 4.61	Utilities 13.21	Telecom Services 2.99	Materials -8.38	Consumer Staples 5.38	Real Estate 10.85	Industrials -13.29	Materials 24.58	Financials -1.69	Industrials 21.12	Information Technology -28.19	Consumer Staples 0.52
Telecom Services 8.93	Health Care 2.90	Financials -17.06	Utilities 1.29	Telecom Services 11.47	Energy -7.78	Energy -21.12	Real Estate 3.39	Energy -1.01	Materials -14.70	Health Care 20.82	Real Estate -2.17	Consumer Staples 18.63	Consumer Discretionary -37.03	Energy -1.33
							Health Care -2.69	Communication Services -1.25	Energy -18.10	Energy 11.81	Energy -33.68	Utilities 17.67	Communication Services -39.89	Utilities -7.08

Source: Morningstar. Past performance does not guarantee future results. It is not possible to invest directly in an index. Diversification does not assure a profit or protect against loss. This table is not indicative of the performance of any AAM product. See reverse for additional important information.

Sectors represented by the relevant S&P 500 sector index, which is a subset of the S&P 500 Index and includes all companies classified in the respective GICS sector. In 2016, the Real Estate industry group (with the exception of mortgage REITs) was moved out of the Financials sector to a newly created Real Estate sector. In 2018, the Telecom Services sector was renamed Communication Services. The sector was expanded to include media and entertainment companies previously in the Consumer Discretionary sector, as well as interactive media and services companies from the information technology sector.

As illustrated in the table, both absolute and relative returns vary widely between sectors each year. It can therefore be very difficult to correctly forecast top performing areas on a consistent basis and we believe a portfolio diversified across several sectors may have the potential to smooth volatility and increase risk-adjusted returns.

In fact, we see several potential benefits of approximately equal-weighting sectors within a portfolio:

- Increase sector diversification by reducing concentration in individual sectors
- Avoid large weightings in potentially overvalued sectors
- Increase exposure to possibly undervalued sectors that may have greater upside potential
- Potential to generate higher returns compared to a less diversified portfolio, given participation by all sectors, including the highest performers

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All investments involve risk; principal loss is possible. Diversification does not assure a profit or protect against loss. **S&P 500 Index** is an unmanaged market capitalization weighted index used to measure 500 companies chosen for market size, liquidity and industry grouping, among other factors.

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