L&M WEALTH MANAGEMENT

Market Update
June 13, 2022

How did the US stock market do during the month of May? Was it:

A) Down more than -10%
B) Down between -5% & -10%
C) Down between 0 & -5%
D) Up

Perhaps it's not the most technical of indicators, but when Lester Holt is talking about the markets on Nightly News, that's almost always a bad sign. What is technical though, is the definition of a "bear market" in US stocks: this requires a decline of -20% on a closing basis (not during the trading day). So, if the market reaches -21% at 3:30 PM, and it recovers to -19.5% by the market close at 4:00, then, no bear. Because of that technicality, we only today (on June 13) met the requirements for a bear market in 2022. But it sure feels like we've been in a bear market for months.

Starting 2022, it appeared for several reasons - inflation, the Fed, Ukraine, supply chains, mid-term elections, and COVID - that we might run into more volatility than average. But what is average volatility? In mid-term election years since 1950, the average top-to-bottom decline has been -17%. So far, the market has reached as low as -22% in this decline, which seems both horrible in the moment and perfectly typical in the context of history.

Like all declines of this magnitude (this is the 27th bear market since 1928,) this decline has its own precipitating (in this case, two) causes: significant inflation and the risk of recession as the Federal Reserve attempts to reduce that inflation. These issues go hand-in-hand because the action the Federal Reserve must take to curb inflation, by design, must also slow the economy. The Fed must attempt to thread the needle (or, as they call it, a "soft landing") by taking enough action to slow inflation but not so much that it causes a recession. Not wanting to be too committal, Fed Chair Jay Powell has said there's a good chance of a "soft-ish landing."

We look at it this way: since March 2009, we've had one of the great runs in all of market history. Even taking the bumpy last 2.5 years, even including the global pandemic that has killed tens of millions of people worldwide, and even considering this recent decline, global equity markets are still up by more than 8% since January 1, 2020. But that's short-term.

Much longer-term, $1 invested in the S&P 500 in 1972, the year Rusty Lipsitz founded L&M, would today be worth around $37. This reveals the progress of global business, capitalism, and the boon of compounding returns over decades. In order to have earned anything like those returns, investors had to tolerate dozens of declines like this one…indeed that $37 was worth $46 just a few months ago.

Our clients have benefited from these returns because they didn't panic when the market fell by 19% in 2018, or when it fell by 34% in early 2020. At a time when even famous and formerly successful investors (see Cathie Wood and Bill Miller) have lost their minds, it's easy to second-guess a solid and disciplined long-term approach. But history has shown, time and time again, that declines like this one are temporary.

Our mission continues: not to insulate you from short or intermediate term volatility, but to protect you from long-term regret – the regret that has always followed fear-driven exits when, eventually, inevitably, markets resume their long-term advance. And following every one of the bear markets that has ever occurred, markets *have* resumed their advance.

Each bear market is different, but the historical evidence for recoveries is compelling. If we take as predictive the fact that every prior bear market in history has been followed, eventually, by new all-time highs, we should also notice that many of the steepest declines have been followed by spectacular gains. Indeed, a 20% loss requires a 25% gain to recover, and a 50% loss requires a 100% gain. Consider three (granted, well-mined) data points:

1. Since 1984, there had been only 18 days on which more than 29% of stocks on the NYSE and more than 33% on the NASDAQ reached their 52-week lows. Only once was the S&P 500 index lower a year later, and that was by -0.2%. It was positive 17 times. The median 1-year return following days like these was 32.0%. Thursday, May 12, 2022 was the 19th such day. (Jason Goepfert)
2. Since 1957, this current decline is the 27th time the S&P 500 index has fallen by more than -15% in 5 months. In all but 2 of these instances over the past 65 years, the market has been positive over the following 12 months, with an average gain of nearly 20%. (S&P)
3. Since 1928, 2022 is the 5th worst start to a year, as measured by the worst first 100 trading days. In 1932, 1939, 1940, and 1970, the market was up each time during the rest of the year.

It's darkest before dawn: in the moments when markets make us feel like there's no reason for optimism, that's historically been a good time for long-term investors to be optimistic. It's also been a good time for investors to deploy cash.

Finally, a reminder that our investment advice and financial plans are designed in preparation for market declines of 30%, 40%, and more. As always, please don't hesitate to reach out to us at any time for any reason.

And the answer is 'D' – The S&P 500, which measures US stock performance, ended April at 4,131.93, and it ended May at 4,132.15 – a gain of 0.005%.