Market Perspective

Global stocks are clearly in the midst of a significant bear market, and for the first time since the 2008 Financial Crisis it appears that neither the Federal Reserve nor the Federal Government are coming to the rescue. This is unsurprising as it is largely believed that the current market downturn is primarily the resulting backlash from too much fiscal & monetary stimulus in recent years. As is always the case in a down market it is unclear where and when the market will bottom out or how long it will take for markets to recover. Adding to the volatility is the uncertainty of whether the market is simply "correcting" prices that had soared too high or if we are actually on the verge of a recession.

First let us look at the numbers. At the end of September the global stock market (MSCI ACWI) index was down 26.1% from it's peak in early January. The market last reached this level in October 2020, meaning we are essentially flat over the last two years. Despite the downturn, the index has still provided a 7.5% average annualized return over the past ten years.

Source: MSCI; CFA Institute

Long-term investors understand that down markets are an inevitable part of the natural market cycle. But investors are also human, which makes that fact harder to digest when the down market goes from theory to reality. Fortunately, we have plenty of history to draw from to help provide context.

Since 1968 there have been been seven market downturns at least as severe as the current one. While they differ in their duration and severity, once they bottomed out they all experienced exceptional growth in subsequent years.

			Forward Returns		
Market Peak	**Market Trough**	**% Down**	**1 Year**	**3 Year**	**5 Year**
11/29/1968	5/26/1970	-36.1%	44.5%	54.6%	30.7%
1/11/1973	10/3/1974	-48.2%	30.8%	52.3%	71.3%
11/28/1980	8/12/1982	-27.1%	57.4%	83.5%	219.7%
8/25/1987	12/4/1987	-33.5%	20.7%	43.1%	90.9%
3/24/2000	10/9/2002	-49.1%	30.1%	49.8%	95.1%
10/9/2007	3/9/2009	-56.8%	66.6%	97.9%	174.8%
2/19/2020	3/23/2020	-33.9%	69.8%	-	-
1/3/2022	N/A	-25.2%	-	-	-
		Average:	45.7%	63.5%	113.7%

Returns Shown use S&P 500 Index; Source: Yardeni Research & Yahoo Finance

As the chart illustrates, market downturns have historically been exceptional buying opportunities. These historical examples are reinforced by what we are seeing in today's market as projections for future stock market returns are the highest they have been in years. Even more, for more conservative portfolios, the bonds we are buying today are yielding the highest interest rates we have seen in over a decade. While we cannot predict whether the market has further to fall or when the bottom will be reached, both the history and the data indicate the eventual recovery will be strong.

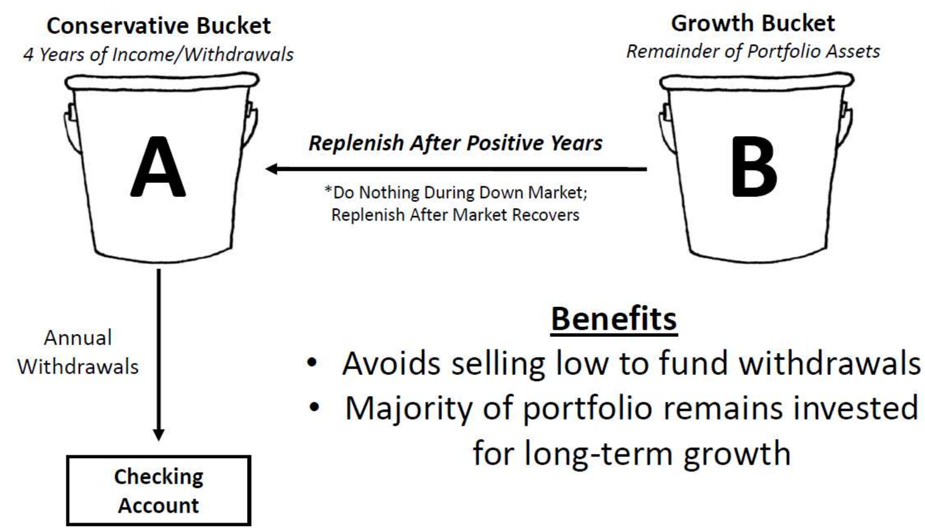
The biggest unknown is whether we are heading for a recession, which would inevitably mean a drop in future earnings for many stocks. Since the stock market is forward-looking, it typically drops prior to a recession, as many believe is the case today. By the time the economy is contracting, the stock market has often already bottomed out and began growing again. The volatility we are experiencing right now is because of this recession uncertainty and is likely to continue until some general consensus is reached.

While a decrease in future earnings could create more downside risk than we have seen so far, there is some comfort in current valuations. In contrast to the past several years, global stocks are fairly inexpensive relative to earnings. In some parts of the market, stocks appear downright cheap. The result is that while poor future earnings could still push stocks lower, there is nowhere near as much room for them to fall from a valuation standpoint.

Source: Yardeni Research

Fight or Flight is our most primal instinct, which means that when something bad is happening around us we feel the need to act and to do something about it. While that instinct was likely critical for our ancestor's survival, it is counterproductive as investors. For long-term investors the only real danger is fear and bad decision-making. Otherwise, this is simply an expected part of the market cycle and is baked into our projections and cash-flow models.

For shorter-term investments this is why we focus so much on planning. By understanding your timeframe and income needs we can implement a bucket strategy where we are cordoning off several years of income into safer investments, allowing the market to recover and avoiding the need to sell during a down market. This year has demonstrated the need for and benefits of the bucket strategy.



The Bucket Strategy