Tuesday 26 July 2022

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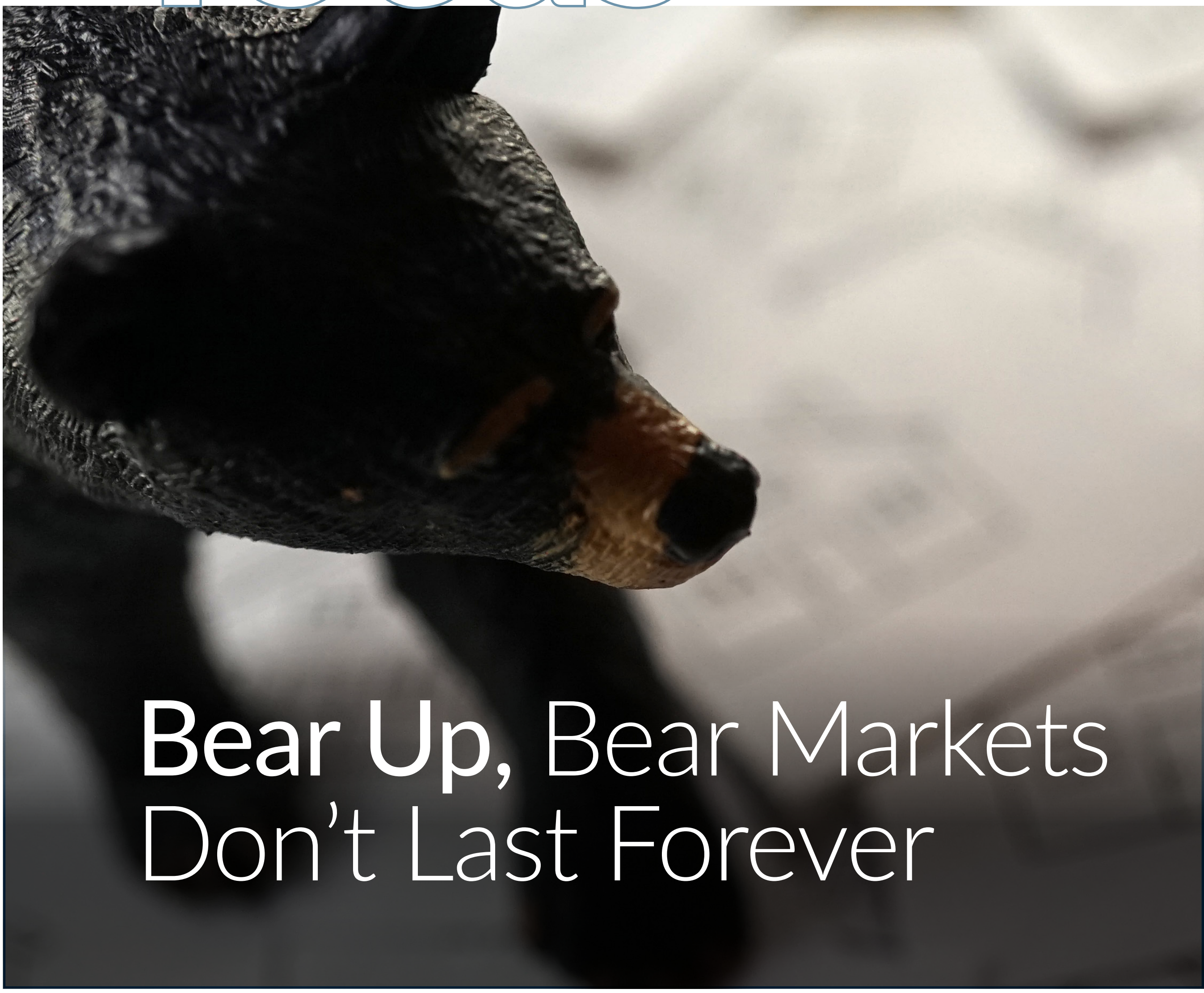


Bear Up, Bear Markets Don't Last Forever

It's official. Last month global stock markets officially hit bear market territory. For most, watching investment portfolios decline sharply is disconcerting. It's okay if you have questions and concerns — you are not alone. At such times it's easy to be tempted to batten down the hatches and remove all risk. While avoiding sleepless nights is important, it's a balance. History highlights long-term investors are better to be positioned for bull markets than hide from the bears.

...Since 1950 there have been 11 bear markets. All are different...

Nobody enjoys watching the value of their assets fall. Those who've been through previous market crises are typically calmer and understand, through experience, that bear markets don't last forever. For some, especially newer investors, watching assets decline in price can be extremely worrying. Fortunately, markets have picked up from recent lows over the past month. Unfortunately, we can't tell you whether the bottom is behind us or if there's more downside to come. What we can reassure you is that bear markets do end. They are a (thankfully semi-) regular occurrence and such turbulence is the price investors pay for earning higher returns over the long-term versus putting their money in more stable investments like the bank.

Bear markets are (unfortunately) a normal part of investing

> *"You get recessions, you have stock market declines. If you don't understand that's going to happen, then you're not ready. You won't do well in the markets. If you go to Minnesota in January, you should know it's gonna be cold. You don't panic when the thermometer falls below zero."*

Peter Lynch, legendary investor

There is good news and bad news about bear markets.

The bad news is they are not abnormal. For investors who've only been in the market over the last decade or so that might not seem the case. Outside of the COVID crash in 2020, investors have had an unusually smooth run. But looking back through history, a bear market — typically defined by a –20% decline in stock prices — happens on average once every five or six years.

Since 1950 there have been 11 bear markets. All are different — in cause, depth, length, and recovery.

The past three have been among the more dramatic. The COVID crash was the fastest bear market in history. The Global Financial Crisis was the deepest downturn since the Great Depression. And the Dot.com crash was one of the longest and largest downturns on record.

On average, through all these bear markets, the decline has been –38% and it has taken 15 months for the market to fall from peak to trough but, as the chart below highlights, the range is broad. (And to be honest, looking back at previous bear markets doesn't provide you with much insight on what to expect this time round.)

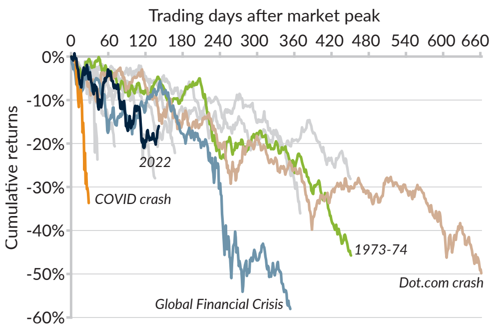
Over the long-term markets are more bull than bear

The good news is, firstly, markets are almost guaranteed to recover. On average, it has taken 2 years and 3 months for the market to reclaim the losses incurred during a bear market. The longest recovery period was just over 4 years following the Global Financial Crisis.

Also good news is that share markets typically perform very strongly on the other side of a bear market. The average return in the year following these bear markets has been 45%. The lowest return in a recovery year has still been a very healthy 23%. For the two years following a bear market the average return has been 63%, with the lowest being 42%.

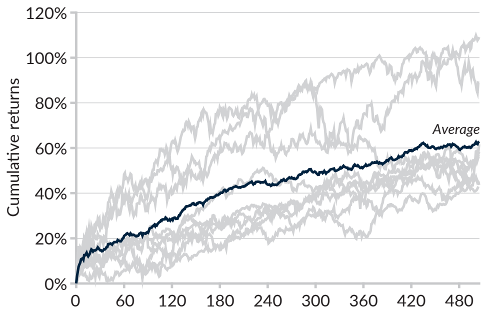
A further piece of good news is that bull markets considerably outweigh bear markets, both in time and returns. Since 1950, while the average bear market has lasted 15 months, the average bull market has lasted 3 years and 10 months. And, despite those semi-frequent sharp pullbacks, the market has delivered an average annual return of 7.8% pa. While bear markets feel painful at the time, when you look at long-term returns, they look like blips in the positive long-term trend. **Long-term investors are better to be positioned for bull markets than hide from the bears.**

BEAR MARKETS SINCE 1950



Source: Refinitiv, Bloomberg, Forsyth Barr analysis

RECOVERIES FOLLOWING BEAR MARKETS



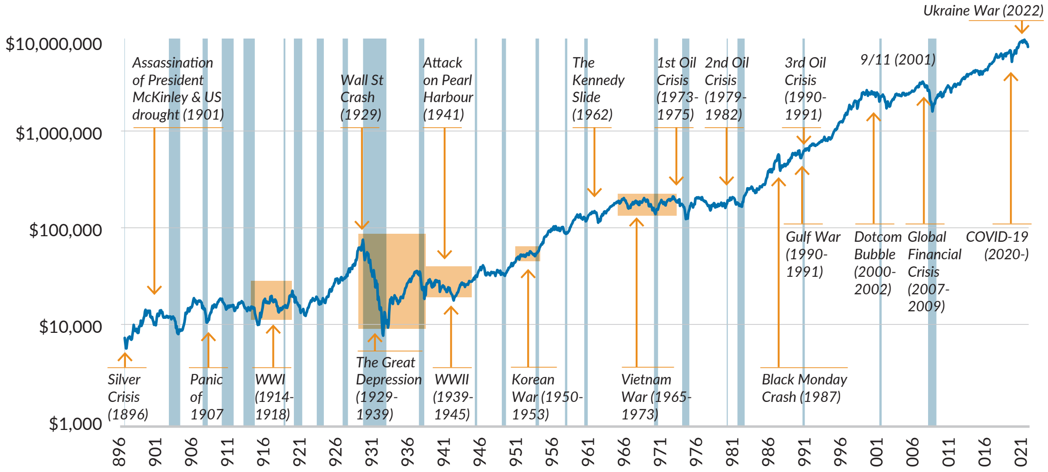
Source: Refinitiv, Bloomberg, Forsyth Barr analysis

BEAR MARKETS SINCE 1950

Peak	Trough	Breakeven	Peak to trough decline	Peak to trough (number of days)	Time to recover losses (days)
2 Aug 1956	22 Oct 1957	24 Sep 1958	-21.6%	446	337
12 Dec 1961	26 Jun 1962	3 Sep 1963	-28.0%	196	434
9 Feb 1966	7 Oct 1966	4 May 1967	-22.2%	240	209
29 Nov 1968	26 May 1970	6 Mar 1972	-36.1%	543	650
11 Jan 1973	4 Oct 1974	31 May 1978	-48.2%	631	1335
20 Nov 1980	12 Aug 1982	2 Mar 1983	-27.1%	630	202
27 Aug 1987	26 Oct 1987	30 Nov 1988	-31.3%	60	401
27 Mar 2000	9 Oct 2002	14 Mar 2006	-49.0%	926	1252
31 Oct 2007	9 Mar 2009	7 May 2013	-58.1%	495	1520
12 Feb 2020	23 Mar 2020	24 Aug 2020	-33.7%	40	154
4 Jan 2022	??		-21.9%		
Average			**-37.8%**	**464**	**811**
				15 months	**27 months**

Source: Refinitiv, Bloomberg, Forsyth Barr analysis

DOW JONES INDUSTRIAL AVERAGE: BEAR MARKETS ARE MERE BLIPS ON POSITIVE LONG-TERM RETURNS



Source: Refinitiv, NBER. Dow Jones Industrial Average Capital Index, Forsyth Barr analysis

Why don't we hibernate through bear markets?

As we've discussed before — the question we're often asked is "can't we avoid the downturns — sell at the top, buy again at the bottom?". Unfortunately, the evidence is clear. While there will always be someone who successfully calls the top of the market each time, there are extremely few (if any) who do it consistently.

> *"The idea that a bell rings to signal when to get into or out of the stock market is simply not credible. After nearly fifty years in this business, I don't know anybody who has done it successfully and consistently. I don't even know anybody who knows anybody who has."*

Jack Bogle, investor, founder of Vanguard

Furthermore, to effectively complete the trade you also have to get your timing right and get back in at the bottom. This makes it doubly difficult to execute successfully. And if you don't get back in at the bottom you miss out on the typically strong returns that follow a bear market.

To emphasise just how costly those missed returns can be, if you invested $10,000 in the MSCI All World Index on 1 January 1980 it'd be worth around $462,000 today. Over that period there have been over 11,000 trading days. If you missed just the 10 days with highest returns (less than 0.1% of trading days) you'd have just over half that, around $239,000. If you missed the top 20 days you'd have less than a third, about $147,000. Many of those high return days come during the periods after a bear market.

RETURNS FROM $10,000 INVESTED IN 1980

1 January 1980 to 19 July 2022	Dollar value today	Annualised Performance
Fully Invested (MSCI World AC Index)	$462,103	9.42%
Missed 10 best days	$238,770	7.74%
Missed 20 best days	$147,483	6.52%
Missed 30 best days	$96,997	5.48%
Missed 40 best days	$66,972	4.57%
Missed 50 best days	$47,668	3.74%
Missed 60 best days	$34,834	2.97%

Source: Refinitiv, Bloomberg, Forsyth Barr analysis

So then, what can investors do?

The best advice is not to panic and to stick to your investment plan. That is what it is there for, to keep emotions at bay and help navigate choppy periods in markets in order to successfully meet long-term goals.

It's important to remember investors benefit from owning good businesses which grow their underlying value over the long-term. Today's good businesses have not only endured previous bear markets but have flourished on the other side.

> *"A market downturn doesn't bother us. It is an opportunity to increase our ownership of great companies with great management at good prices."*

Warren Buffett

...Your response should be fit for purpose for you...

For those investors with excess funds it's worthwhile considering starting to take advantage of more favourably priced assets. The silver lining of lower asset prices is that they'll provide better returns in the long run. Recently, legendary investor Howard Marks said he believed the time was right to start buying. When asked about the risk of prices going lower, he responded "in which case we'll buy some more".

We understand though that not everyone will be comfortable taking more risk in turbulent times — avoiding "sleepless nights" is valuable. We also appreciate that sometimes plans formed in more stable times don't feel as comfortable when things become challenging — as boxer Mike Tyson once plainly put it, "everyone has a plan until they get punched in the mouth". Taking advantage of the recent tick up in share prices to realise some cash might be appropriate for some. It is quite possible that we'll see more volatility ahead. Another option might be to take advantage of the highest interest rates in around 7 or 8 years now on offer in defensive assets like bonds.

There is no one size fits all answer. Your response should be fit for purpose for you. If at any stage you'd like to discuss the current challenging investing environment, investment options and opportunities, or review your investment plan, please contact your adviser — that's what they're there for and they're always happy to help.

Matt Henry CFA
Head of Wealth
Management Research

Understanding that sudden changes in financial markets can cause concern or indicate opportunity, your Forsyth Barr Investment Adviser is available to provide you with advice and assistance at any time.

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