Portfolio Management, LLC

Building Wealth Wisely

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This Too Shall Pass

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We celebrated the longest bull market on record in August, with stocks quadrupling in value since the lows of March 2009. Unfortunately, 2018 ended with a thud. While the S&P 500 didn't officially reach bear market territory, we came close to a 20% decline at one point in the fourth quarter.

For the year, almost all investment markets declined in value, including stocks, bonds, real estate, and oil. It's rare for so many categories to be negative in the same year. Concerns about a rise in interest rates, an inverted yield curve, a mounting trade war, and a slowing economy all weighed on investment markets. Due to these worries, the fourth quarter turned out to be one of the most unfavorable periods for stocks in memory.

The U.S. economy is still performing well due to record low unemployment, rising real wages, and relatively tame inflation. However, there are signs that a trade war with China is taking a toll, and the housing market has been deteriorating over the past year. It looks like some degree of economic slowdown is inevitable in 2019.

In order for the current economic expansion to become the longest one on record this year, it will need to absorb tightening monetary conditions, growing debt levels, fading fiscal stimulus, weakening global trade, and possible impeachment proceedings. Concerns about a recession can become a self-fulfilling prophecy if waning confidence leads consumers and corporations to cut back on spending.

Most economists, however, are not forecasting a recession in 2019. Hence, investor pessimism could be overstated at this time, and the current market downturn might be viewed as a buying opportunity in hindsight. Stock valuations have tapered down to more reasonable levels, and bonds have become more attractive with the rise in yields. It's interesting to note that corporate insiders have been heavy buyers of their company stocks over the last quarter. Current conditions remind us of the famous quote by Paul Samuelson, "The stock market has predicted nine of the last five recessions."

Although past performance is not a guarantee of future results, positive returns tend to follow meaningful downturns. The table below shows the 1, 3, and 5-year results after the most negative quarters of S&P 500 returns since 1940.

S&P 500 Since 1940		**Forward Performance**		
Quarter Ending	**Quarterly Performance**	**One Year**	**Three Years**	**Five Years**
Sept 1974	-25.2%	38.13%	72.74%	117.46%
Dec 1987	-22.6%	16.81%	48.82%	108.97%
Dec 2008	-21.9%	26.46%	48.59%	128.19%
June 1962	-20.6%	31.16%	69.20%	94.84%
Sept 1946	-18.0%	6.45%	24.47%	115.41%
June 1970	-18.0%	41.87%	57.39%	56.30%
Sept 2002	-17.3%	0.26%	26.96%	66.32%
Averages	**-20.5%**	**23.0%**	**49.7%**	**98.2%**

Courtesy of Ben Carlson

No one knows for sure what happens from here – we could end up with a recession and cyclical bear market in 2019. But as with all previous downturns, we think this too shall pass. We remain confident in the principles of sound, long-term investing. We strongly believe market timing is not a viable investment strategy.

The benefits of being a long-term investor have always exceeded the distress of short-term declines. History shows we cannot build and preserve our nest eggs without assuming some reasonable level of risk. The more we avoid risk, the greater the chances our wealth will decline in purchasing power after taxes and inflation.

Periodic downturns are a normal part of investing. The stock market experiences a 15-20% decline every other year on average. We believe the best way to deal with volatility is to remain long-term investors and take advantage of the highs and lows by rebalancing portfolios along the way. For any client who would like to re-examine his or her investment goals, cash needs, time horizon or risk tolerance, please contact us at your convenience.

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