



Dear Friends and Clients,

The bull market that began in March of 2020 came dangerously close to an end. From March 23, 2020 through January 3, 2022, the S&P 500 Index gained 114% (excluding dividends). From that January 3 closing high through the recent low on May 19, the S&P 500 fell nearly 19%, narrowly avoiding the level at which bull markets end and bear markets begin.

While we wait uncomfortably to see if the S&P 500 can hold its recent lows, it is somewhat reassuring to know that bear markets that are not accompanied by recessions tend to be milder:

- Bear markets without recessions tend to last an average of about seven months, and we're already five months into it.
- The only bear markets that took more than 46 days to bottom after the initial 20% decline were associated with recessions—1970, 1973, 1982, 2001, and 2008.
- Bear markets not accompanied by recessions have historically experienced smaller declines, losing an average of 24%.
- Five of the past six non-recessionary bear markets saw the S&P 500 lose 22% or less.

Bottom line, if the U.S. economy is able to avoid recession over the next 12 to 18 months—as we expect—then this selloff may be over soon and stocks could potentially make a run at their previous highs by year-end.

That doesn't take away from the increasingly challenging environment consumers and businesses are facing as sky-high inflation shows few signs of relenting. Recession risk is rising, increasing the chances of a larger decline—the average recessionary bear market decline is 34.8%. The Federal Reserve has taken away the punchbowl, giving markets a hangover. The cure is lower inflation, but it will take time.

Those who believe this environment is like the 1970s, 2000-2002, or 2008-2009, may want to consider more defensive positioning of portfolios. Those are the types of environments where some companies don't survive. But if the economy stabilizes as the Fed hikes rates to tame inflation—the so-called “soft-ish landing” Fed Chair Powell aspires to achieve—then the best path forward may be to ride this out. Market timing is hard. The sharpest rallies tend to come during bear markets and are costly to miss for long-term investors.

Investors are anxious right now and understandably so. Legendary investor Warren Buffett tells us that situations like that are an opportunity to be greedy, not fearful. Sir John Templeton, another legendary investor, tells us bull markets are born on pessimism (and grow on skepticism, mature on optimism, and die on euphoria). Well, we have a healthy dose of pessimism right now to provide fuel for the next rally.

Buffett's advice makes sense but is difficult to follow in practice. For those who can fight off the temptation to sell when stocks are down and have an investing time horizon spanning more than a year or two, history suggests you will be positioned to do well. Bear market recoveries prior to record highs take 19 months on average. When not accompanied by recession, they take just seven months.

From a long-term investing perspective, that's not long to wait. Please contact me if you have any questions.

Best regards,

Victor



Victor S. Levy, J.D., LL.M., CLU, CFP®

1818 Market St | Suite 3232 | Philadelphia, PA 19103

Main: 215-875-8720 | Fax: 267-875-8756

vlevy@levywealth.com

www.levywealth.com

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All data is provided as of June 1, 2022.

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All index data from FactSet.

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