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Staying Calm Amidst Market Volatility

Dear Client,

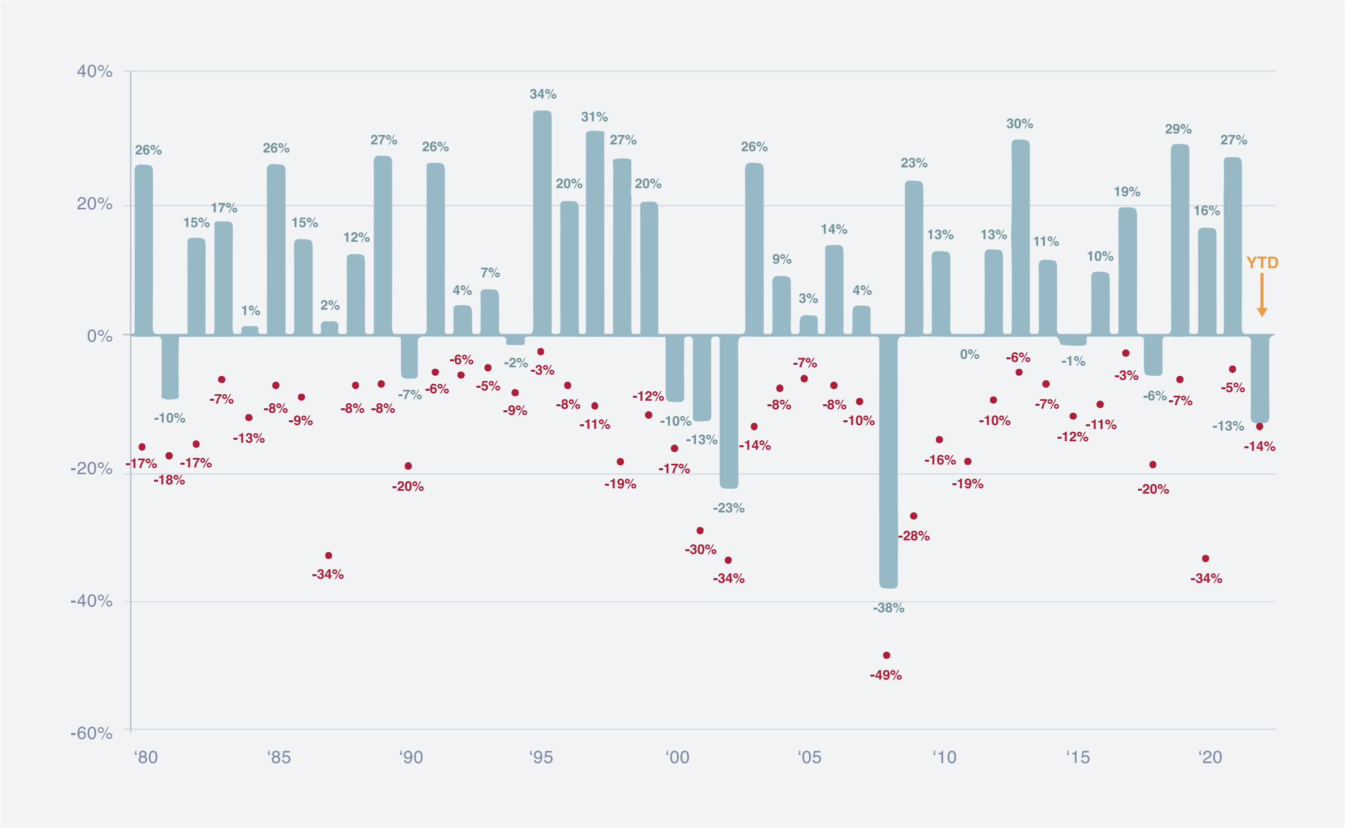
Volatility in the stock market persists, with few signs of letting up. For clients, we understand how unsettling the ups-and-downs can be, and we empathize with the difficulties in keeping a steady hand when the economy and markets feel as though they're in disarray. Even the most experienced investors can get rattled.

But we also believe now is a time to remain patient. In volatile times, I like to remind myself that short-term volatility is the price all investors pay for attractive long-term returns. As legendary investor Benjamin Graham once said, "price fluctuations have only one significant meaning for the true investor. They provide an opportunity to buy wisely when prices fall sharply and to sell wisely when they advance a great deal."

It is also helpful to remember that stock market volatility is not only normal and natural, it is also very common. The chart on the next page is a bit messy, but I'd encourage you to take some time to study it, as the message is important. Looking back to 1980, the average intra-year decline for the S&P 500 is -14%[i]. Basically, in any given year, we should expect the market to fall more than -10%. That's normal.

But it is also true that since 1980, the S&P 500 has finished positive in 32 of the 42 years. Even though a sharp selloff was likely in any given year (see all the red numbers below), the stock market still went up 76% of the time. Staying patient almost always pays off.

S&P INTRA-YEAR DECLINES VS. CALENDAR YEAR RETURNS



Source: J.P. Morgan

As we wrote in our recent Q2-2022 client letter, "we think investors should brace for more market volatility in the coming weeks and months, as well as the possibility that the market correction is not yet over … corrections frequently span months." Setting the expectation that more volatility is ahead can help investors stay even-handed when it does in fact occur.

That being said, if you are ever feeling the impulse to 'do something' about the volatility, please call us first—in all likelihood, if your goals have not significantly changed in the past few months, then your investment portfolio should not change either.

What's Driving Current Market Volatility?

Ascension's Investment Committee no longer believes concerns over interest rates and inflation are the primary drivers of market volatility, as is often cited in the media. These issues have been widely known and discussed for months now, and are very likely baked-into stock prices already. Higher rates are putting pressure on high valuation areas of the market, to be sure, but there is more at work here.

The new factor in today's market that concerns us the most is China's lockdowns, which we think are driving current volatility and could contribute to more pressure in the weeks ahead. China's economy accounted for 18.1% of global GDP in 2021[ii], and it is responsible for nearly one-third of global manufacturing output. An economic slowdown in China would be meaningful to the world.

Against all odds and certainly against their economic interests, China is doubling down on their zero-Covid strategy. Lockdowns in manufacturing hubs like Jilin province and in major cities like Shenzhen and Shanghai have shuttered factories and stores and resulted in a drastic decline in exports. China's exports rose 3.9% in April year-over-year, a sharp fall from the 14.7% growth rate posted a month earlier. Consumer spending and factory output also fell for the month while infrastructure spending stalled. China's jobless rate has also reached a 2-year high of 6.1%[iii].

A slowdown in China's economic output can have ripple effects across supply chains and on global economic growth in general. Large commodity exporters like Brazil, Chile, and Australia have seen sagging sales in copper, oil, and iron ore to China, while manufacturing countries like Germany, Taiwan, and South Korea are worried that China's significant link in the supply chain will be compromised. U.S. companies sell to China's market and also import key materials, making just about every developed economy exposed.

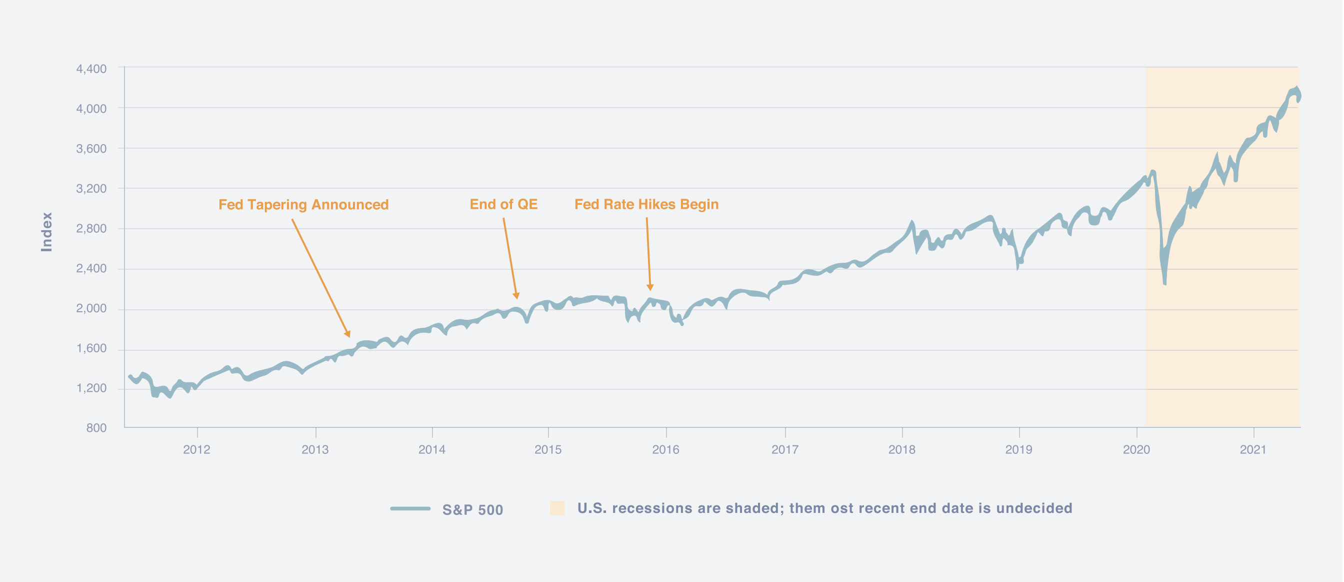
We cannot know how long and how far China's lockdowns will go, but in our view it does not seem likely the government would allow the economy to fall into recession. The uncertainty is weighing on markets, and frankly the outcome could go either way—China could deliver a positive surprise to markets by reopening sooner-than-expected, or deliver a negative surprise with additional lockdowns. Time will tell, and we will be monitoring the situation closely.

The media continues to cite rising interest rates and a too-hawkish Fed as the main culprits for market volatility, but as we've written before, history also shows that rising rate campaigns carried-out by the Federal Reserve have rarely coincided with negative stock market returns.

Since 1950, the Fed has implemented 13 monetary tightening campaigns, featuring several rate hikes in each. The S&P 500 went up in all but two of them, delivering a median gain of +14% (price return) while the Fed was actively raising rates[iv]. Rising rates do not necessarily mean falling stocks – in fact, they rarely do.

In the Fed's most recent tightening cycle, they moved the fed funds rate from 0.5% in December 2015 all the way up to 2.5% in December 2018[v]. Market volatility accompanied the moves, but as shown in the chart below, stocks moved higher as rates moved higher. This is not to say that stocks will surely go up as the Fed tightens in this cycle, but it's a good reminder that higher rates are not an automatic negative.

THE S&P 500 OVER THE LAST DECADE



Source: Federal Reserve Bank of St. Louis

Conclusion

For readers who are feeling the weight of the selling pressure and are having doubts over whether the market or economy will recover, we would encourage you to reach out to us directly. We understand how challenging it can be to experience big swings in the market from day-to-day, and we are here to talk you through it and to guide your decision-making process.

We encourage you to remember that stock market volatility is not only normal and common, it is also not very significant when considering an investor's true time horizon—unless an investor decides to sell or make changes as a result of the market's short-term swings. Remember, day-to-day moves will not permanently alter a portfolio's expected returns over the next 10, 15, or 20 years. And it's the long-term that matters most.

Sincerely,

Paul Thompson, Jr CFP

Sources:

[i]Source: JPMorgan
[ii]Source: World Bank
[iii]Source: S&P Global
[iv]Source: NYU Stern; Federal Reserve
[v]Source: Federal Reserve