Zacks
INVESTMENT MANAGEMENT

Mitch on the Markets

Portfolio Manager Investing Insights

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3 Key Reminders for Navigating a Bear Market

With the U.S. equity markets hovering in bear market territory, now is a crucial time for investors to keep a steady hand. Down markets can cause even the most experienced investors to make rash, market-timing decisions that sometimes pay off – but usually don't.

The average length of a bear market is about 9.6 months[1], which suggests the markets could remain choppy and unpredictable for the foreseeable future. Here are three key reminders to help readers navigate this period.

1. **Resist the Urge to "Do Something"**

I will not predict how long this bear market will last or how deep it will go, but I can predict media narratives: *they will remain negative for some time.*

When investors see negative media coverage at the same time as a market selloff, it almost always creates an urge to "do something" in response, whether that be trimming equity exposure or selling out of stocks altogether. On the other side of the spectrum, investors may see intense selling pressure as a signal to "buy the dip" or to move more aggressively into battered-down categories of stocks. Neither impulse is a good one.

Selling out of stocks once the market is already in bear territory means locking in losses and increasing the likelihood that an investor is on the sidelines once the market mounts a recovery – which it eventually will. Approximately 34% of the market's best performance days have taken place in the first two months of a new bull market[2], and we only know the new bull market has begun with the benefit of hindsight. Selling out of stocks and waiting for confirmation that a new bull market has arrived almost certainly means missing the first several months of the new bull, which is a crucial time to be invested.

2. **Remember That Bear Markets are Factored into Return Expectations**

Most long-time equity investors know that the historical returns of U.S. stocks fall in the +8% to +10% range depending on the time period analyzed. But we sometimes forget that these expected, over-time returns factor in bear markets – even very significant ones like the 2000 tech bubble and the 2008 Global Financial Crisis. I still do not believe we are facing down

this type of bear today – the U.S. jobs market is still historically tight, household finances and the U.S. consumer are still healthy, and corporate profit margins are high. I believe sentiment has fueled declines more than fundamentals have.

At the end of the day, an investor's asset allocation should be established based on return expectations needed to meet a certain set of goals and objectives. If stocks are part of the asset allocation, which they usually are, then just remember that bear markets are always factored into your return expectations.

3. Participating in the Rebound is Now the Top Priority

On average, stocks decline by -36% during a bear market. While that feels like a very significant loss, it pales in comparison to what is gained during the bull markets that follow. Stocks gain an average of 114% during bull markets, which also last an average of 2.7 years. Bull markets are longer and stronger than bear markets.[3]

Once the market has crossed into bear market territory, the next 12-months return for equity investors has almost always been positive. The two exceptions since 1950 were the tech bubble bear market in 2001 and the Financial Crisis bear in 2008. Even with those two instances factored in, the median 12-month return for the S&P 500 following a bear market has been +23.9%. In other words, being invested once the stock market crosses the -20% level has paid off consistently throughout history.[4]

The issue is that there is no way to know *when* the market will stage its strong recovery, though history does tell us that it usually happens in close proximity to the scariest down days. Here's a key stat to remember: over the last 20 years, 70% of the stock market's best days have occurred within two weeks of its worst days[5]. This speaks to the perils of trying to time exit and entry points during heightened volatility like we're seeing right now. Doing so means potentially – if not probably – missing out on the market's best rallies that every equity investor needs to drive investing success.

Bottom Line for Investors

We know throughout history that bull markets follow bear markets – there have been 26 bear markets and 27 bull markets since 1928, and the bull markets have always recouped the losses and driven the market to new highs. In 92 years of stock market history, bear markets have taken up 20.6 of the years while the rest have been rising markets. According to historical data, stocks go up 78% of the time.

All that to say, stay patient here. While we cannot know when the new bull market will begin, history tells us that it will start before anyone knows it, and that some of the best gains will happen in those early days. Investors should not be on the sidelines when that happens.

ABOUT MITCH ZACKS

Mitch is the CEO & Senior Portfolio Manager at Zacks Investment Management. Mitch has been featured in various business media including the Chicago Tribune and CNBC. He wrote a weekly column for the Chicago Sun-Times and has published two books on quantitative investment strategies. He has a B.A. in Economics from Yale University and an M.B.A in Analytic Finance from the University of Chicago.

[1] Hartford Funds. 2022. https://www.hartfordfunds.com/practice-management/client-conversations/managing-volatility/bear-markets.html#:~:text=Watch%20for%2020%25%3A%20Market,of%2010%25%2D19.9%25

[2] Hartford Funds. 2022. https://www.hartfordfunds.com/practice-management/client-conversations/managing-volatility/bear-markets.html#:~:text=Watch%20for%2020%25%3A%20Market,of%2010%25%2D19.9%25

[3] Hartford Funds. 2022. https://www.hartfordfunds.com/practice-management/client-conversations/managing-volatility/bear-markets.html#:~:text=Watch%20for%2020%25%3A%20Market,of%2010%25%2D19.9%25

[4] Wall Street Journal. June 14, 2022. https://www.wsj.com/articles/bull-markets-winners-dragged-the-s-p-500-into-a-bear-market-11655184522?mod=hp_lead_pos7

[5] J.P. Morgan 'Guide to the Markets.' 2022. https://am.jpmorgan.com/us/en/asset-management/adv/insights/retirement-insights/guide-to-retirement/

IN FOCUS THIS WEEK

- **Federal Reserve's inflation concerns**
- **U.S. consumer spending ticks higher**
- **Consumer sentiment falls**

The Federal Reserve is More Concerned About Inflation Than Recession

In comments made this week by Federal Reserve Chairman Jerome Powell, he made it clear that the Fed would rather curb inflationary pressures than protect the economy against potential recession. This line of thinking harkens back to the era of Fed Chairman Paul Volcker, who intentionally (and famously) tipped the U.S. into a recession in the early 1980s by raising rates into double-digit territory to tamp down 1970s inflation. Some of the Fed's work today is cosmetic, in our view – they want to give the appearance that they are fighting inflation when in reality inflation is largely a supply-driven issue. The Fed may be concerned that higher prices will change consumer psychology into expecting future inflation, which could be self-fulfilling. We see a distinct possibility that later in the year supply issues tied to the war, China lockdowns, and pandemic backlogs still being worked through could ease inflation pressure as the Fed is raising rates, giving the appearance that the Fed's plan is working.[1]

U.S. Consumer Spending Ticks Higher, but at a Slower Pace

Americans are still out spending in the U.S. economy, but at a slower overall pace. In May, consumer spending rose by a seasonally adjusted 0.2%, the slowest pace of increase in 2022 but still a sign that households are hanging on. Personal incomes grew by 0.5% in May, which was consistent with April's increase but failed to keep pace with inflation. Once adjusted for inflation, personal after-tax income fell by 0.1% in May, which can be a hindrance to overall spending. Retail sales fell for the first time this year, but largely as consumers continue to shift spending from goods to services. Orders for long-lasting durable goods like refrigerators, cars, and washing machines continued to increase, rising 0.7% in May and marking the 7th increase in eight months. Orders for nondefense capital goods, which is a good indicator for business investment, also ticked higher by 0.5% in May. The housing market continues to be resilient as well, as the number of U.S. houses that went under contract also rose. As likely expected, consumers pulled back at the pump, with gasoline sales falling 8.2% compared with the same week last year.[2]

Meanwhile, Consumer Sentiment Falls to All-Time Lows

Even as consumers spend slightly more and experience higher wages – within one of the strongest labor markets in decades – their attitudes about the U.S. economy continue to darken. The University of Michigan's Consumer Sentiment Index, which is a bellwether for how consumers feel about the U.S. economy, fell this month to its lowest point ever. This reading is one of the key reasons we believe the bear market may not have much further to go – consumers feel worse today than they did during the depths of the Great Recession, when millions lost their homes and the jobless rate was approaching double digits. The bar for the U.S. economy is arguably as low as it can be, meaning even slightly better than expected data could fuel a stock market rally, in our view.[3]

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[1] Wall Street Journal. June 29, 2022. https://www.wsj.com/articles/powell-says-pandemic-could-alter-inflation-dynamics-11656509259?mod=djemRTE_h

[2] Wall Street Journal. June 30, 2022. https://www.wsj.com/articles/inflation-consumer-spending-personal-income-may-2022-11656531317

[3] Yahoo Finance. June 24, 2022. https://finance.yahoo.com/news/consumer-sentiment-university-of-michigan-june-final-142848659.html

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