



Research Insight

Stick With Your Plan and Keep Your Perspective

Keep calm and carry on

My team and I spend a good amount of our day monitoring the capital markets and keeping tabs on what the professional money managers who run the mutual funds you support are up to. These folks are paid to digest news and assess the ramifications, adjust their financial models when appropriate, and change positioning within their funds when warranted. During times like these, when volatility becomes extreme and headlines are changing by the hour, money managers have very challenging jobs.

Our job, in some ways, becomes easier when market losses turn ugly because it allows us to focus on the tried and true messaging about maintaining a level head and focusing on long-term investment outcomes. These are anything but platitudes. There have been aggressive market selloffs before, we are in the midst of one now, and there will be many more in the future.

We aren't sure where the next days or weeks will take us, and nobody can provide complete certainty there. What we are more certain about is that over the remaining time horizon of most investors, things will get better and a commitment to your investment plan is a superior approach to throwing in the towel when times get challenging for markets.

The goal of this piece is not to gloss over what we are experiencing in the markets right now. Market jitters related to higher levels of inflation and anticipation of rate hikes have boiled over because of geopolitical uncertainty coming out of Russia's Ukrainian invasion. The events unfolding have been difficult to watch, and all we can wish for is that we don't witness a catastrophic loss of life in eastern Europe. What we do want to offer is a longer-term perspective with the hope that it will provide some relief for frayed nerves. Panic selling is not a viable long-term investment strategy.

What's happening

In a nutshell, we are witnessing a significant increase in volatility as market participants attempt the impossible task of trying to discount the ramifications of Russia's attack on Ukraine. Potential activities on the part of the Fed and Bank of Canada seem to be on the back burner but concerns around what might happen there have not abated. The Canadian equity market peaked in November and to date has held up relatively well. Many individual names have faced steep losses, but strong commodity prices, excellent performance for financial stocks and limited representation of flagging tech stocks have resulted in a more muted decline for the S&P/TSX Composite. The situation

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Investment Products & Platform team

JAMES GAUTHIER

james.gauthier@iawealth.com

MICHAEL DIL

michael.dil@iagto.ca

PAVAN KHAIRA

pavan.khaira@iagto.ca

BHARTI PATEL

bharti.patel@iagto.ca

JOSHUA WON

joshua.won@iagto.ca

JUSTIN KIM

justin.kim@iagto.ca



south of the border has been more severe, with the S&P 500 sliding by 10.51% (in USD) from its January 3 closing high through market close on February 24 (although not

all of this should be attributed to Russia/Ukraine). The tech-heavy Nasdaq was down by 14.9% over the same period.

Recent returns of selected market benchmarks in CAD

Index	January 3 – February 24 Return
S&P/TSX Composite	-1.89
S&P 500	-8.08%
Nasdaq 100 (ZNO used as proxy)	-13.26
MSCI World	-16.0%
MSCI EAFE	-8.62%
FTSE Universe Bond (XBB used as proxy)	-4.90%
Barlays High Yield Very Liquid Index (ZHY used as proxy)	-5.35%

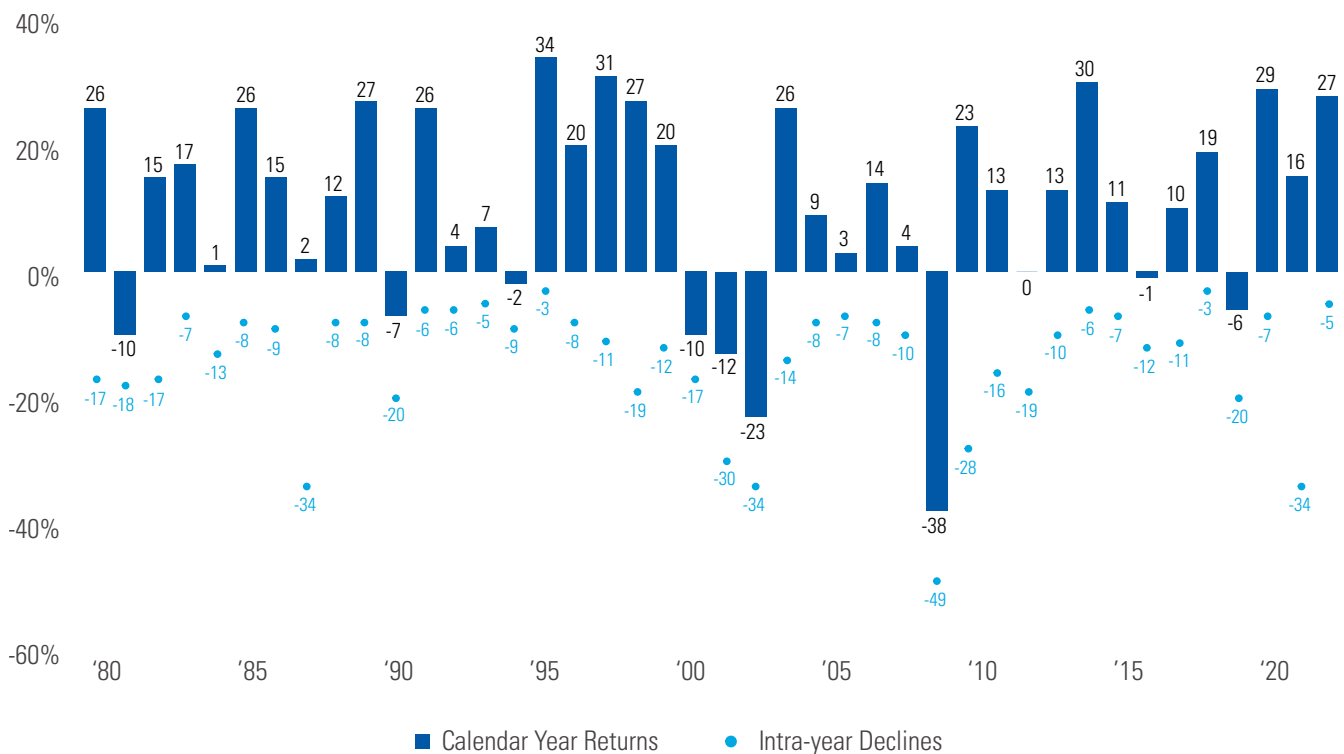
Source: Morningstar.

Volatility is normal

We must remember that volatility is a normal stock market dynamic. We witnessed an extreme amount of volatility in 2020 due to Covid, but that was bookended by 2019 and 2021 where general levels of volatility were rather low. Going back more than four decades, the average intra-year decline for the S&P 500 has been 14%, with a pullback of at least 10% occurring in 23 out of 42 years.

Despite these pullbacks, annual returns were positive in 32 out of 42 years, with an average return of 11%. Stock markets can be volatile in the short term, but sticking to a long-term plan through periods of market volatility can help investors stay on track towards reaching their financial goals.

S&P 500 intra-year declines vs. calendar year returns



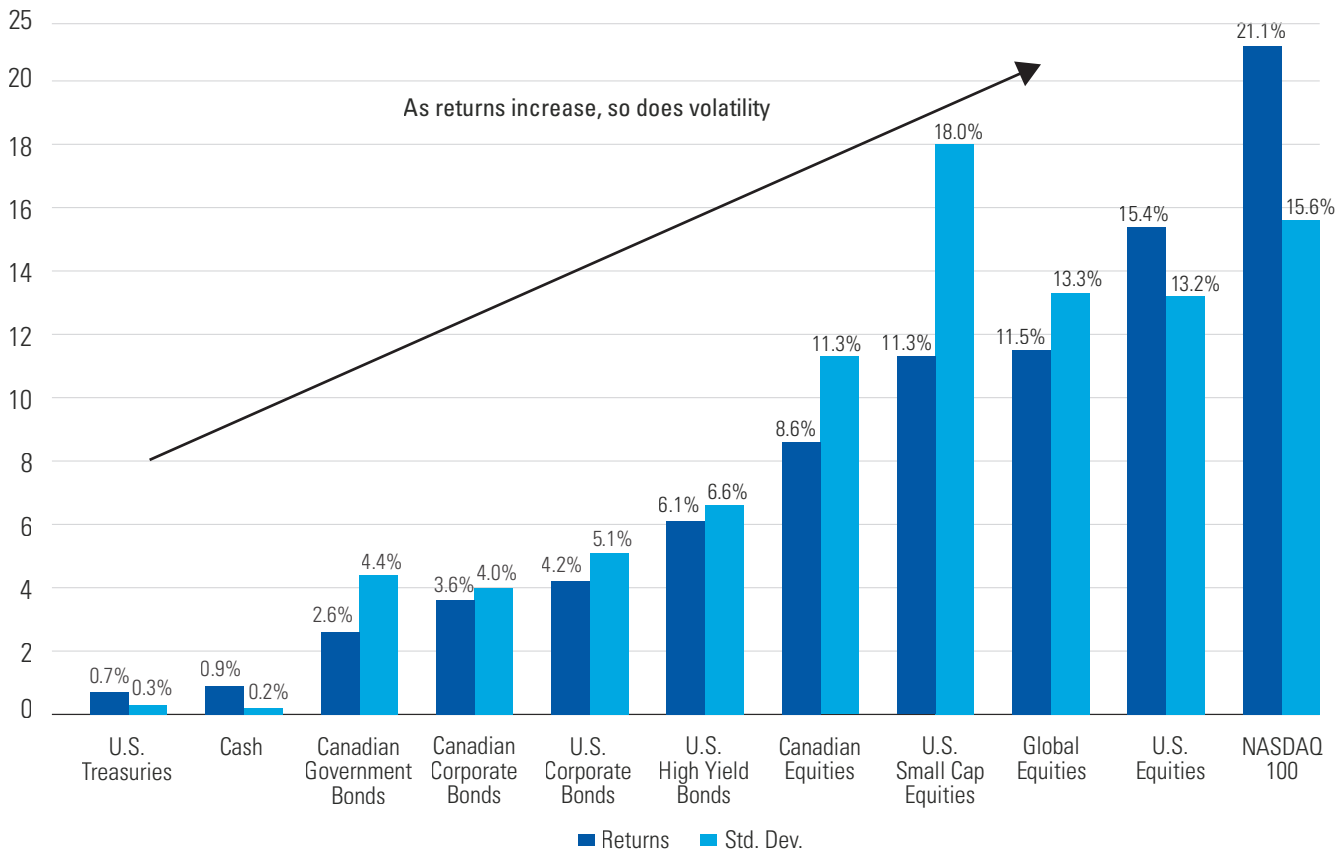
Source: J.P. Morgan Asset Management.



A higher level of volatility, with bouts that can sometimes be extreme, is an inherent trait of equity investing. In exchange for that volatility, however, comes the opportunity

to participate in an asset class that has historically provided better returns than other asset classes.

Asset class returns & volatility – trailing 10 years



Source: Morningstar, trailing 10 years as of January 31, 2022 using monthly returns. Returns are in base currency. U.S Treasuries = Bloomberg US Treasury Bills TR USD; Cash = FTSE Canada 91 Day Tbill; Canadian Government Bonds = FTSE Canada All Government Bond; Canadian Corporate Bonds = FTSE Canada All Corp Bond; U.S Corporate Bonds = ICE BofA US Corporate TR USD; U.S High Yield Bonds = ICE BofA US High Yield TR USD; Canadian Equities = S&P/TSX Composite TR; U.S Small Cap Equities = Russell 2000 TR USD; Global Equities = MSCI World NR USD; U.S Equities = S&P 500 TR USD; Nasdaq 100 = NASDAQ 100 TR USD.

But the world is coming to an end – I need to sell!

Geopolitics, conflicts and wars do have an impact on investor sentiment and returns. There is generally a flight to quality when things flare up significantly, and risk assets usually go in the opposite direction. The table that follows provides numerous examples of how the market behaved during and after a variety of geopolitical crises. In the moment, some of these events probably did feel like

the apocalypse was upon us, and readers likely remember their emotions during many of these situations. As it turned out, an average loss of 6% associated with these events was followed by an average gain of 14.2% in the subsequent 12 months.



Conflict and the stock market

S&P 500 performance around geopolitical events

Event	Date	Base Date	Duration of		Selloff (%)	1-Wk from Bottom	1-Mo from Bottom	3-Mo from Bottom	6-Mo from Bottom	12-Mo from Bottom
			Selloff (trading days)	Recover Prior Level (trading days)						
WWII Germany Annexes Czechoslovakia	15-Mar-39	10-Mar-39	22	108	-20.5	2.0	8.3	8.5	23.2	18.9
WWII Germany Attacks France	09-May-40	09-May-40	22	745	-25.8	10.6	10.9	17.1	18.0	9.2
WWII Pearl Harbor	07-Dec-41	04-Dec-41	17	201	-10.8	6.2	6.5	-3.8	-1.1	15.3
N. Korea invades S. Korea	24-Jun-50	22-Jun-50	17	43	-12.9	5.5	11.2	19.2	29.2	31.4
Suez Crisis	29-Oct-56	05-Nov-56	17	131	-6.8	3.3	4.9	-1.4	6.2	-6.0
Berlin Wall	13-Aug-61	22-Aug-61	25	18	-3.9	1.4	4.1	8.0	6.2	-14.6
Cuban Missile Crisis	14-Oct-62	15-Oct-62	7	9	-6.6	2.0	15.0	22.7	30.0	36.5
Assassination of Kennedy	22-Nov-63	21-Nov-63	2	1	-2.8	3.8	6.7	11.5	16.0	23.9
Authorization of Military Operations in Vietnam	07-Aug-64	17-Jul-64	15	36	-3.2	0.5	1.7	4.8	7.3	5.8
Six Day Israel Arab War	05-Jun-67	08-May-67	20	40	-6.5	3.5	3.3	6.5	7.7	13.0
Israel Arab War/Oil Embargo*	16-Oct-73	29-Oct-73	27	1475	-17.1	6.3	7.3	5.6	-2.0	-28.2
President Nixon Impeachment Proceedings*	06-Feb-74	30-Jan-74	9	16	-6.6	1.8	9.1	0.9	-10.8	-13.3
Shah of Iran Exiled	16-Jan-79	26-Jan-79	9	34	-4.6	1.1	1.3	1.9	8.7	19.7
Iranian Hostage Crisis	04-Nov-79	05-Oct-79	24	51	-10.2	3.6	7.7	16.4	7.3	29.3
Soviet Invasion of Afghanistan	24-Dec-79	17-Dec-79	12	6	-3.8	3.5	9.4	-2.9	11.6	29.6
Invasion of Grenada	25-Oct-83	10-Oct-83	22	304	-6.3	2.8	2.1	-3.7	-0.8	4.3
Bombing of Libya	15-Apr-86	21-Apr-86	20	7	-4.9	1.2	5.7	6.2	5.0	23.5
First Gulf War	16-Jan-91	01-Jan-91	6	8	-5.7	0.3	15.4	19.9	20.7	34.1
Clinton Impeachment Proceedings	19-Dec-98	07-Dec-98	6	5	-3.9	4.1	6.2	13.4	13.4	23.0
Kosovo Bombing	24-Mar-99	19-Mar-99	4	9	-4.1	1.6	7.5	5.6	1.4	21.0
9/11*	11-Sept-01	10-Sept-01	6	15	-11.6	4.3	11.1	18.5	19.4	-12.5
Iraq War	20-Mar-03	21-Mar-03	7	16	-5.3	3.6	8.0	15.8	20.0	32.8
Arab Spring	25-Jan-11	27-Jan-11	2	3	-1.8	2.2	4.0	6.6	1.9	3.1
Intervention in Libya	19-Mar-11	18-Feb-11	18	29	-6.4	3.3	5.0	0.9	-3.3	11.7
Russia-Ukrainian Conflict (Crimea)	14-Mar-14	07-Mar-14	6	13	-2.0	1.1	-0.6	5.2	7.8	11.5
Intervention in Syria	22-Sept-14	18-Sept-14	21	12	-7.4	4.2	9.5	8.4	13.0	9.1
Brexit Vote	23-Jun-16	08-Jun-16	14	9	-5.6	5.1	8.3	8.0	13.4	20.9
Airstrike on Syrian Airbase	07-Apr-17	01-Mar-17	32	16	-2.8	0.6	2.7	5.1	4.2	4.2
Russian-Ukrainian Conflict	03-Jan-22	—	50		-9.3					
Median (excludes current Russia/Ukraine event)			16	16	-6.0	3.3	7.0	6.6	7.8	14.2

*Recession Related. Source: Deutsche Bank, 1832 Asset Mgmt.

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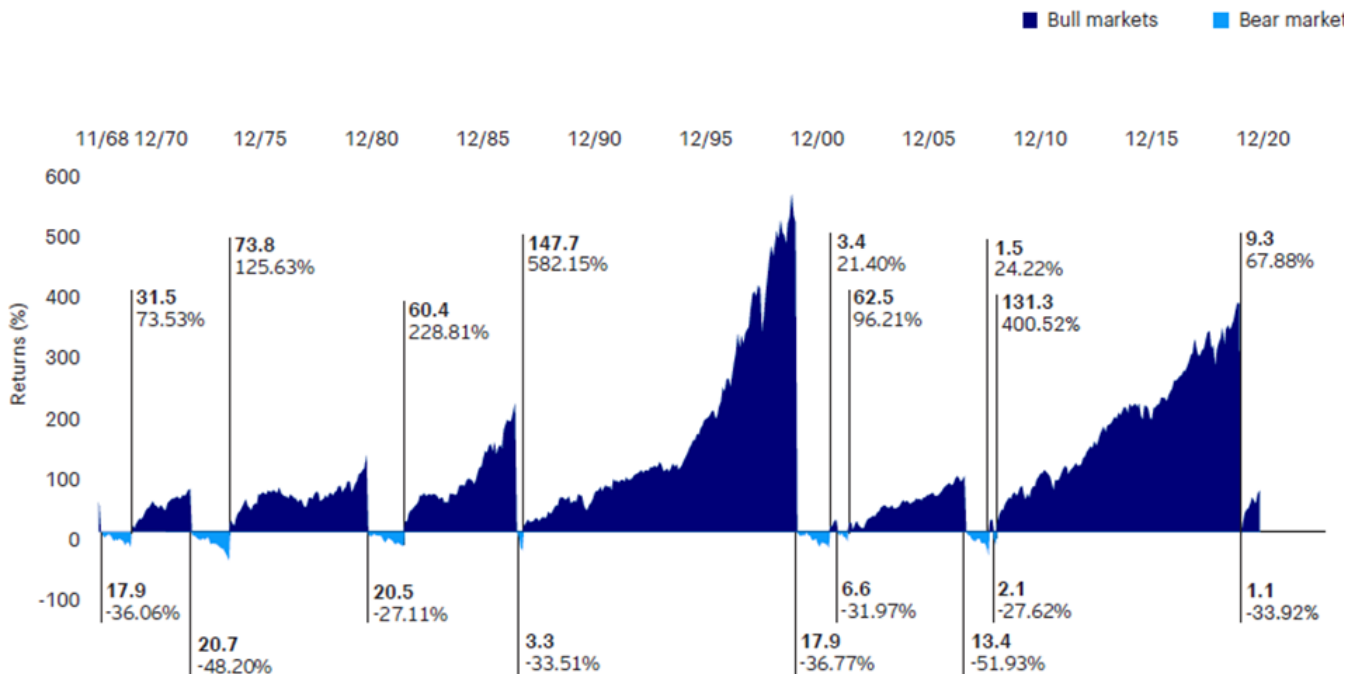
What if the sell-off gets worse?

There are only a few certainties in life: death, taxes and the fact that a bull market always follows a bear market. Perhaps that is of little consolation to investors facing big losses, but it is the optimistic reality. A bear market is defined as a loss of 20% or more for stocks. We are not there yet, and perhaps broader markets will not ultimately reach bear market territory, but the problem with bear markets is that you never know how severe they will be or how long they will last.

There have been 11 bear markets for the S&P 500 in the last 65 years or so, with the average slide being 34.3% and an average duration of close to 11 months. For perspective, the bull markets coming out of those downturns has averaged 55 months in length with the average gain for those run-ups being 155%.

The historical performance of the S&P 500 Index during U.S. bull and bear markets

The bold numbers calculate the duration of months for the market, either being bull or bear, and the percentages cover the total return for the time period.



In the chart above, the dark blue time periods indicate bull markets when the S&P 500 rose 20% or more from its previous low. The light blue time periods indicate bear markets when the S&P 500 declined 20% or more from its previous high.

On average, when the market is evaluated from 11/29/68 – 12/31/20, there were bear markets or losses for 349 days, and bull markets or gains for 1,764 days. Data shown is as of the last bull market through 12/31/2020.

Source: Invesco, using data from Bloomberg L.P. Returns from 11/29/68 – 12/31/20. The S&P 500 Index is an unmanaged index of 500 stocks used to measure large-cap U.S. stock market performance. Investors cannot invest directly in a index. Index returns do not reflect any fees, expenses, or sales charges. This chart is for illustrative purposes only and not indicative of any actual investment. These returns were the result of certain market factors and events which may not be repeated in the future. Past performance is not guarantee of future results.

So yes, things could get worse, but we do know that investors who have held for a full market cycle have typically ended up in good shape. Investors who have had the patience to hold for multiple market cycles have

profited nicely, despite taking numerous gut punches along the way in the form of market corrections and bear markets.



Everyone talks about the long term, but I can't take this anymore!

Investors who work with investment advisors have the benefit of a portfolio built around their risk tolerance, return expectations, time horizon and other specific needs. If you have a very long-term time horizon and are willing to take on more risk with the expectation of higher returns, there is a good chance that most, or maybe all of your portfolio is exposed to stocks.

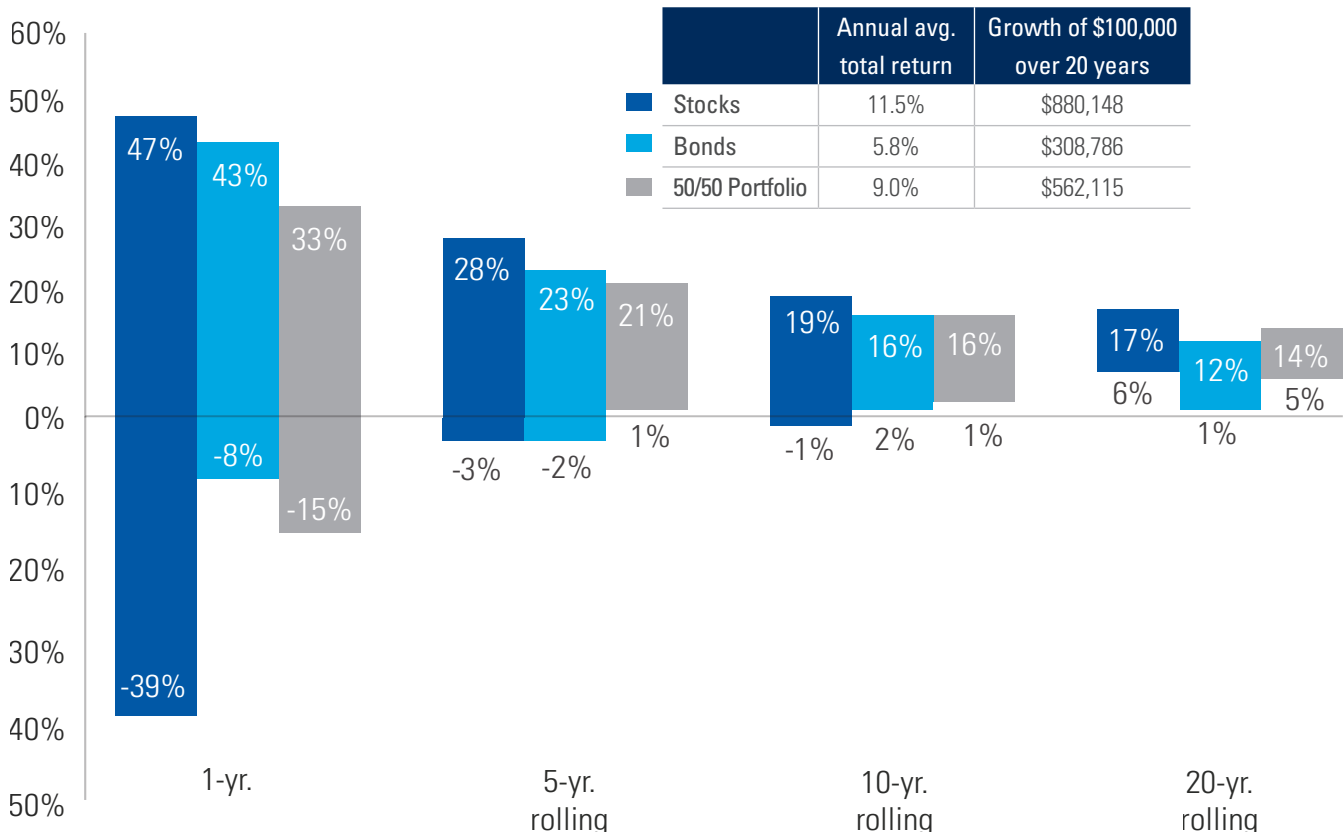
As the next chart illustrates, a pure stock portfolio, based on the performance of the S&P 500 in local currency returns going all the way back to 1950, would have lost as much as 39% over any 12-month period. Hopefully that's the level of risk you bargained for. On the flipside, the best 12-month return for every 12-month period going back to 1950 was 47%.

When you start increasing the time horizon, however, you see a fascinating thing happen. The return variation begins to narrow as the holding period increases. When extending things out as far as 20 years, the minimum historical return for stocks was 6%. In other words, you could have invested in the equity market at the most inopportune time of the past 70 years (based on month-end levels) and still made a 6% annualized return in stocks. This is why patience matters.

Investors with less tolerance for risk and shorter time horizons most likely hold a portfolio comprised of a combination of stock and bond exposures. The preceding chart shows that the variability between the best and worst performance over all time periods measured is less than that of a pure stock portfolio. That really is the point, and the numbers illustrate that a balanced portfolio has tended to be more resilient over shorter time periods.

Range of stock, bond and blended total returns

Annual total returns, 1950–2021



	Annual avg. total return	Growth of \$100,000 over 20 years
Stocks	11.5%	\$880,148
Bonds	5.8%	\$308,786
50/50 Portfolio	9.0%	\$562,115

Source: J.P. Morgan Asset Management.



I bought at the top of the market – I’m doomed

Not really, although this is where long-term thinking becomes especially important.

Let’s assume you were the worst market timer of all time and moved all-in when the market was peaking as the Roaring Twenties came to a close. This meant you were looking at the Great Depression down the barrel of a gun. You would have lost more than 80% of your money in three-and-a-half years if you had invested in the S&P 500. That’s probably the level at which despondency sets in. You would have seen World War II come and go and would have witnessed the beginning of the baby boom while still being under water. But by late 1954, you would have been back to even. If you held on for an additional 10 years, your return would have been almost 170%. Keep in mind that these numbers are before dividends.

In closing

The best way to build wealth over the long-term is to first develop an investment plan with the help of your financial advisor. The next step is to stick with that plan, even when the clouds look the most ominous. It is this step where the advice and guidance of a professional advisor can be most invaluable. Market corrections sometimes happen, and so do bear markets, but patience and discipline are generally rewarded in the long-term.

We like to reflect on the wisdom of some of history’s greatest investors when market conditions go pear shaped. It can bring comfort and help restore perspective. Here are some of our favourite insights:

“Buy when there’s blood in the streets, even if the blood is your own.” – Baron Rothschild

“Only buy something that you’d be perfectly happy to hold if the market shut down for 10 years.” – Warren Buffett

“The time of maximum pessimism is the best time to buy, and the time of maximum optimism is the best time to sell.” – Sir John Templeton

“Forecasts may tell you a great deal about the forecaster; they tell you nothing about the future.” – Warren Buffett

“In investing, what is comfortable is rarely profitable.” – Robert Arnott

To summarize this scenario, if you had put all your eggs into one basket and bought stocks at the worst possible time in modern history and not added another dime to your investment portfolio, you still would have ended up with a decent return over a period that is certainly long (35 years or so, 25 to breakeven), but completely in-line with most people’s investment lifespans. Admittedly, this is an extreme scenario and it is hard for us to foresee an outcome this unfortunate for clients who deal with professional advisors.

“Opportunities come infrequently. When it rains gold, put out the bucket, not the thimble.” – Warren Buffett

“The idea that a bell rings to signal when investors should get into or out of the market is simply not credible. After nearly 50 years in this business, I do not know of anybody who has done it successfully and consistently.” – John Bogle

“I will tell you how to become rich. Close the doors. Be fearful when others are greedy. Be greedy when others are fearful.” – Warren Buffett

“If you have trouble imagining a 20% loss in the stock market, you shouldn’t be in stocks.” – John Bogle

“The investor’s chief problem – even his worst enemy – is likely to be himself.” – Benjamin Graham

“Sometimes buying early on the way down looks like being wrong, but it isn’t.” – Seth Klarman

“Look at market fluctuations as your friend rather than your enemy; profit from folly rather than participate in it.” – Warren Buffett

“You want to take risk when others are fleeing from it, not when they’re competing with you to do so.” – Howard Marks

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Recommended List: The list presents a selection of funds that we believe are among the best of their peers and offer unique characteristics that can add value when used in a well-diversified investment portfolio tailored to a client's investment objectives.

Hold: The fund remains on the Recommended List, but is not recommended for adding to or selling from client's portfolios.

Sell: The fund is no longer on recommended list.

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