The Intersection of COVID-19 and Your Portfolio

Each of us has our own unique emotional journey when we find ourselves at the intersection of a viral pandemic and a global equity market decline of nearly 25%. As the number of infected people continues to grow, so might one's anxiety about the spread and potential impact of the virus. We know you may have some questions about how this might impact your investments – and to that end we'd like to share some perspective with you.

Let us begin with the punchline. While the tragic and far-reaching public health implications of COVID-19 should not be minimized, as they are likely to be deeply rooted and long-lasting – the long-term effect on your *portfolio* will be neither of those.

Markets will recover and once again reach new all-time highs and our collective psyches will similarly rebound. As hard as it is to envision today, the unrelenting anxiety many of us feel today will fade into a comfortable contentment once again. We've seen many difficult markets come and go…and undoubtedly, we'll see many more together as client and advisory firm.

In fact, markets are notoriously strong at eventually shrugging off events that are downright terrifying. The typical pattern is that markets initially decline due to the uncertainty and fear that comes with any new concern (such as COVID-19), but then uncertainly wanes and investors return to corporate and economic empirics – which invariably pushes stock prices higher. Oddly, those higher prices often occur without an accompaniment of fanfare or easily identifiable "good news."

Time like these remind us why it is so important for great investors to have long memories. It is easy to forget that we have had 33 bear markets (at 20% or more decline) in the U.S. stock market since 1900 – and of course, those have been followed by 33 robust recoveries. Those recoveries overcame previously unfathomable circumstances such as the Great Depression, world wars, oil embargos, double-digit inflation, and yes…other pandemics. Despite what you see in the headlines, this time will be no different. The circumstances and fact patterns leading to the decline are, of course, uniquely fear provoking, but the result is the same – the market will recover. We thought it would be helpful to graphicly depict the worst 25 bear markets in history and the subsequent one-year performance that followed them:

The 25 Worst Market Declines & the Subsequent One-Year Return

U.S. Stock Market, 1/1926–12/2019. Values Expressed as Percentages.

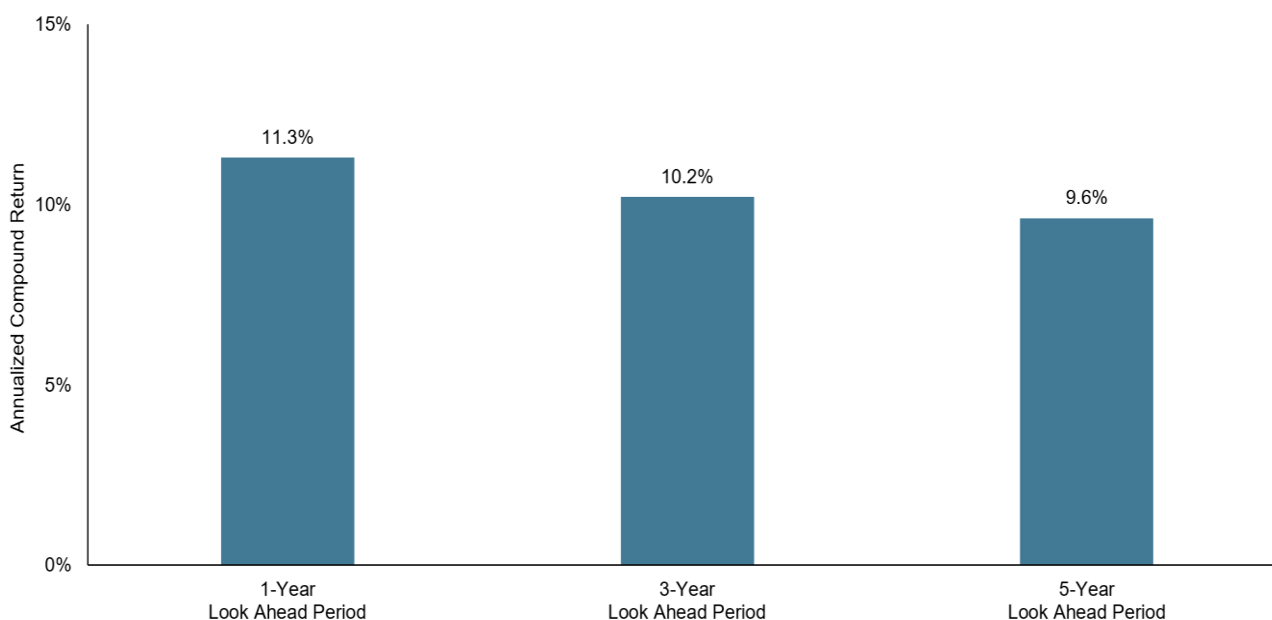
Although the data on the previous page are irrefutably compelling, there is no denying that little else can provoke fear of losing hard-earned money like a fierce, short-term stock market correction such as what we have experienced this past week. Predictably, the natural fear-based human emotional reaction is to sell off assets to reduce one's exposure.

Understandably, the goal is trying to reduce further losses and ease a troubled mind, but the result is often damaging to long-term wealth. We must not give in to the urge to take action because the news today is bad. Seasoned investors know that market prices react immediately to new information – particularly to bad news. By the time the events become "news" the price change from that news is already reflected into current market prices. Selling stocks after bad news has already caused stock prices to fall simply isn't good strategy. To potentially time the markets in order to make profits or avoid potential losses, we would need to trade *before* events become news. And, of course, we don't know the future news, so any action would be complete speculation. And you are a Rockwood client, so you know that we are not in the guessing business.

Even for disciplined investors that avoid speculation, after many years of strong market returns one may often forget that market corrections and recoveries are the norm, not the exception. A shrewd investor understands that short-term declines are inevitable in the long-term upward trajectory of the market. Even in years of strong market returns, temporary stock market declines of 15% are not unusual. Stocks are volatile assets, and accordingly have provided historically higher rates of return to patient investors that understand their nature. Moreover, staying invested following market declines is quite a profitable endeavor. In fact, shown below is a portrayal of the rewards investors reap for level-headedness after market declines:

Average Annualized Returns after Market Decline of More than 10%

U.S. Large Company Stocks, 1/1926–12/2019



In US dollars. Past performance is no guarantee of future results. Declines are defined as months ending with the market below the previous market high by at least 10%. Annualized compound returns are computed for the relevant time periods after each decline observed and averaged across all declines for the cutoff. There were 1,127 observation months in the sample. January 1990–present: S&P 500 Total Returns Index. S&P data © 2020 S&P Dow Jones Indices LLC, a division of S&P Global. All rights reserved. January 1926–December 1989; S&P 500 Total Return Index, Stocks, Bonds, Bills and Inflation Yearbook™, Ibbotson Associates, Chicago. For illustrative purposes only. Index is not available for direct investment; therefore, its performance does not reflect the expenses associated with the management of an actual portfolio. There is always a risk that an investor may lose money.

We know from experience that market contractions or recessions can test our will. They will subject us to the natural instinct to sell holdings to prevent further loss. However, intellectually we know that selling when the market is down leads to wealth crippling losses, since we would naturally then wait for the market to rise until we would feel “comfortable” enough to reinvest our assets. This type of emotion-based buying and selling behavior is the direct path to locking in losses and missing out on the inevitable market recovery.

What should you do when the market goes down?

1. Acknowledge that stock market declines are a normal and expected event.
2. Recognize that trying to predict the timing and magnitude or market declines with any accuracy is futile.
3. Remind yourself that times like these are precisely why you own bonds in your portfolio. They act as a shock absorber and provide you with dry powder to purchase stocks whose prices have fallen.
4. Remember that your portfolio was engineered for down markets. Remain committed to your goals.
5. Remind others who are less-well advised (or those that are prone to panic) that the current volatility, while not comfortable, should be expected from time to time.

Finally, in a quiet moment, please take the time to pat yourself on the back for having the clear-eyed confidence to continue to execute your strategic investment plan.

We know it isn’t easy – we understand how you feel. We have felt the same way. A market decline combined with empty sports arenas, surging hospitals, shuttered schools, and grim-faced news anchors is going to test your resolve. We’ve written before that it takes maturity and self-confidence to make decisions in your own long-term best interests. Do your best to ignore the temporary market downturn and the cacophony of media noise that has accompanied it. Too many investors make poor decisions to attempt satisfy their short-term emotions. We won’t let it happen to you! We already know that you, like us, are investors for the long haul…and our decisions must be made to vehemently protect your investments from the emotion of the moment.

Personal Note from Rockwood’s President About a Scary Day in the Markets

By: John Augenblick, written on March 9, 2020

Today’s date is March 9, 2020. Even though the Dow Jones Industrial average dropped by more than 2,000 points today amid a Coronavirus panic and oil price war – I am particularly fond of that day of the year, specifically the calendar day March 9th.

I don’t even have to look it up – or even check my sources. The date March 9, 2009 is forever ingrained in my mind. I remember it because it was the first day of the recovery from the particularly nasty bear market brought about by the credit crisis in 2008-2009. Nobody rang a bell on March 9, 2009 to let everyone know it was the end of the fierce bear market that worsened the downtrodden psyche of the long-weary stock investor. Nobody announced on the news that day that it was the bottom of a 54% drop in stock prices in the U.S. That’s not how it works.

Here is what the media announced in 2009 well *after* the market bottom came and went: (1) Unemployment rose sharply to 9.5%, which was higher than the parameters used to stress test our

nation's banks at the time. (2) The GDP continued to shrink. (3) Two American automotive icons, GM and Chrysler, filed for bankruptcy. (4) More banks failed. (5) And, that a healthy assortment of other seemingly apocalyptic events that seemed unthinkable would continue to unfold.

All of those events happened after March 9, 2009 and yet, stock prices went up…way up. In fact, as of today, since that date the U.S. Market has delivered a 10-year annualized total return of 17.8% per year since the crisis bottom in March 2009 (that I had to look up). It would have been a terrible shame to miss out on those returns; and, it would be similarly shameful to miss out on the recovery from this bear market (whenever it arrives).

If an investor waited around in 2009 for good news to buy stocks, they missed out on one of the best buying opportunities in the past nine decades. Market data experts know that waiting for good news as a trigger to buy stocks doesn't work – markets are too efficient at pricing securities. Scary Time Magazine covers are likely a better predictor of positive expected returns.

Market data experts also know that the timing of the bear market bottom cannot be predicted, but odds are that stock prices will be higher next year on March 9, 2021 than they are today on this March 9, 2020. Which of course, is exactly why well-advised investors don't sell stocks during times of market panic. Unlike many investors, you have the wherewithal to remain calm and poised while others teeter anxiously on the precipice of wealth crippling behavioral finance mistakes (like selling stocks *after* their prices have fallen).

On another note, I also met my wife on March 9, 2003, which helps remind me that some March 9's will be better than others.

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