The Market is Tanking. Time for Some Longer-Term Perspective.

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The market sell-off that began in late January, which seemed to be initiated by concerns over rising inflation and the prospect of higher interest rates, picked up aggressively yesterday as selling seemed to feed on itself. The sell-off spilled into Asia, then to Europe, and North American equity markets are all over the place today. Is this being driven by algorithmic trading? Mass selling of ETFs? Leveraged participants being forced to liquidate? The end of the world? The specific catalysts for the plunge may be uncovered as the dust settles, but they don't really matter for our purposes here.

What we hope to do with this piece is to offer a bit of perspective and take a hard look at some long-term market realities that should be kept in mind as the temptation to panic grows. First, take a deep breath. Then note that we have not yet witnessed anyone on Bay Street vacate the premises through an open window. Finally, remember that the chances you will need all of the money in your investment portfolio tomorrow are very low. Indeed, what's far more likely is that there probably is no reason for you to touch it for five, ten or even twenty years. The long game is the one that should always be kept in mind, and tinkering with one's portfolio in reaction to short-term market transgressions often proves to be detrimental.

The Perspective You Need

Yesterday's 1,175 point drop in the Dow Jones Industrial Average was the headline grabber. It was the biggest point decline in the history of the index, but that figure "only" equates to a 4.6% dip. That's a big number, but it would not even crack the Top 100 list of the worst daily percentage declines for the index historically. (Note that we frequently cite U.S. stock averages in this piece as there is more comprehensive data available for those markets).

We consider the broader S&P 500 index to be a more representative proxy for the U.S. market, and through yesterday's close it was off a little more than 8% from its peak just a couple of weeks ago. That's pretty painful stuff, but since the beginning of the year, the index is only marginally lower. The selloff for Canadian stocks was not as acute yesterday, with the S&P/TSX Composite registering a decline of "just" 1.7%, leaving its YTD loss at 5.4%.

Table I: Index Returns through Feb. 5 Market Close (% in Local Currency)

Index	YTD Return	Drawdown from Peak
S&P 500	-0.9	-8.2
TSX	-5.4	-6.6

Source: Bloomberg

Despite the recent losses, investors who have remained in stocks over the past few years are still basking in their profits.

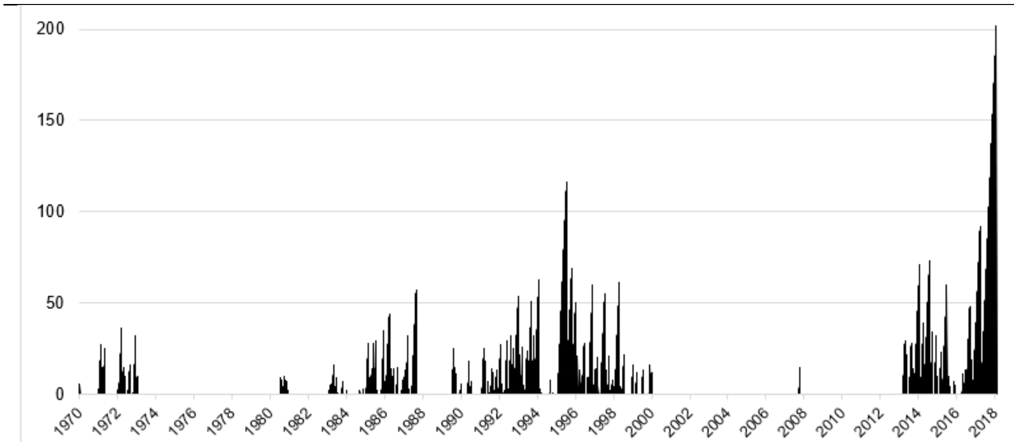
Table II: Annualized Returns Through Feb. 5 Market Close (% in CAD)

Index	1 Yr	3 Yr	5 Yr
S&P/TSX Composite	1.9	3.5	6.9
S&P 500	13.0	11.1	19.5
MSCI EAFE	18.8	8.3	13.0
MSCI World	14.7	9.7	16.3

Source: Bloomberg

So was the market due for a selloff? Maybe. Sentiment is not the best predictor of market direction, but what's for certain is that we enjoyed a market rally that was pretty much uninterrupted during 2017 and early 2018 and investors were feeling pretty good about things. As shown in Chart I, the S&P 500 was within 3% of its all-time high for much of the year. That's an unprecedented statistic, and record-high after record-high quite possibly left some investors forgetting that the stock market can sometimes be a painful place.

Chart I: S&P 500 Consecutive Days Within 3% of All-Time Highs

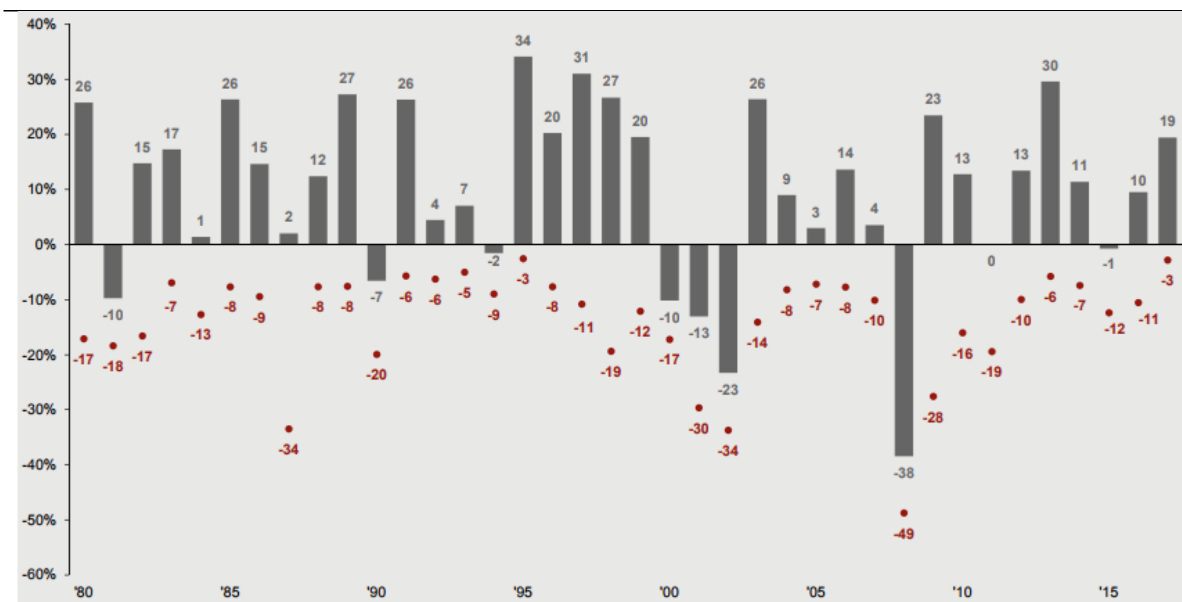


Source: Bloomberg

The worst drawdown for the S&P 500 was, in fact, just 2.8% in 2017. That represented the smallest drawdown for the index in any calendar year going back as far as our data allowed (1928). The median calendar year drawdown since 1928 was 13%, and even if you exclude the downturns that ended up being bear markets (down 20% or more), the median calendar year decline was still 9.9%. So losses, even double-digit losses, are completely normal.

What's also important to understand is that just because markets experience a dip doesn't mean they can't pull out a gain during the calendar year. Take a look at Chart II, which represents the S&P 500 and goes back to 1980. The red dots represent the biggest market drawdown for the indicated year and the grey bars represent the calendar year return for the index. Big drawdowns are a regular occurrence, but the market still showed annual positive returns in 29 of 38 years.

Chart II: S&P 500 Intra-Year Declines vs. Calendar Year Returns

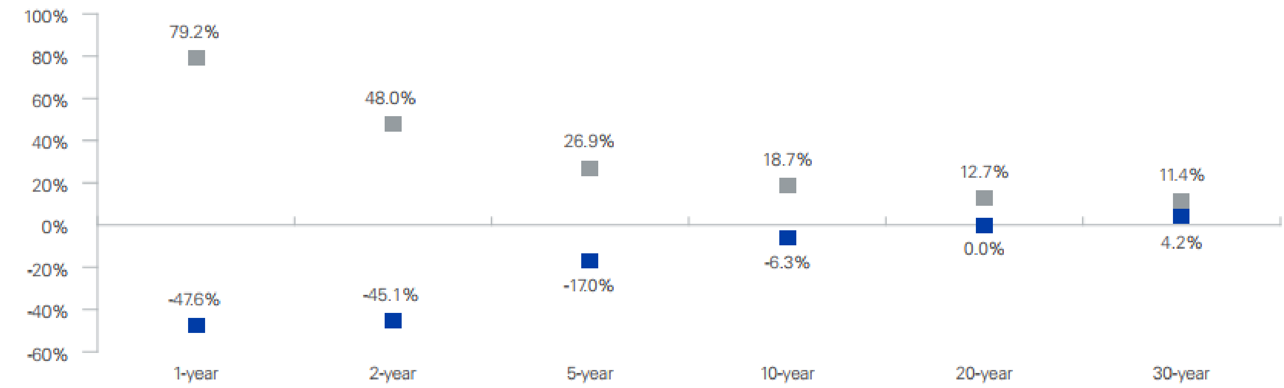


Source: FactSet, Standard & Poor's, J.P. Morgan Asset Management

Another bit of perspective we want to illustrate is that when it comes to stock returns, having a long-term mindset can result in reduced volatility along with better odds of making money, even during the worst of times. Chart III illustrates rolling returns for the S&P/TSX Composite over various time horizons going all the way back to 1920. Clearly, a shorter time horizon may lead to outsized gains – or losses – but a longer-term perspective buffers extremes and increases the odds of making money.

Check out the rolling 20- and 30-year figures. The index has NEVER posted a loss over any period of those lengths. Even an investor moving into the market in 1929 – just ahead of the Great Depression and the biggest stock market crash in history – would have broken even in 20 years. Over 30 years, an investor moving into the market at the worst possible time would have still earned an annualized 4.2%. When the time horizon is that long, gyrations in the market over two days, two months or even two years become irrelevant.

Chart III: Rolling Returns for the S&P/TSX Composite – Dec. 1920 to Dec. 2016



Source: Bloomberg

The bottom line is that the best way to build wealth in the long-term is to develop a plan, with the help of your financial advisor. Maybe more importantly, you need to stick with that plan, and helping on that front is perhaps where your advisor can be the most invaluable. Market corrections happen sometimes, and so do bear markets, but patience and discipline are generally rewarded in the long-term.

In closing, we often go back to the word of wisdom of some of history's greatest investors when things start to get ugly for the market. They can bring comfort and are useful in helping to restore perspective. Here are some of our favourites.

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"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

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

"Buy when there's blood in the streets, even if the blood is your own." - Baron Rothschild

"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

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