



MassMutual

Market Update

August 6, 2024

Courtesy of The Davis Financial Group

As of the time of this writing, U.S. equities are down significantly, Japan has been clobbered, bonds are rallying, commodities are selling off, the Volatility Index (also known as the VIX) is flying, headlines are red, the talking heads are talking, and fear is building!

And yet...

Let us take a breath to recognize what, if anything, has changed.

In the last week, humans have, as humans tend to do, created a bit more chaos than normal...but fundamentally, nothing really has changed. Yes, the U.S. presidential election is now closer, and yes, the Japanese Central Bank did a silly thing, and yes, the recent job data is weaker than hoped, and as shocking as Robert F. Kennedy, Jr.'s announcement of his Ursus escapades was...none of them was truly material enough to send markets down as much as they fell. So, what happened?

Should we sell? Is this the beginning of the end? Are we about to enter another Global Financial Crisis?!

Honestly? Markets just go down sometimes and, candidly, it can be healthy...particularly when viewed through the lens of history and rationality. I know that statement doesn't make headlines, but it's historically accurate and (I believe) fundamentally correct.

As such, what follows today is a (hopefully) rational and objective approach to what has occurred and a perspective on what may follow. Given the speed at which markets are moving, we are (unfortunately) going to skip the pithy anecdotes, introductory stories, and funny (to the author at least) repartee (although I have a great one on vegan paint that my dearest readers should see soon...).

With that, let us begin.

We have met the enemy, and he is us...

Let's start with some statements.

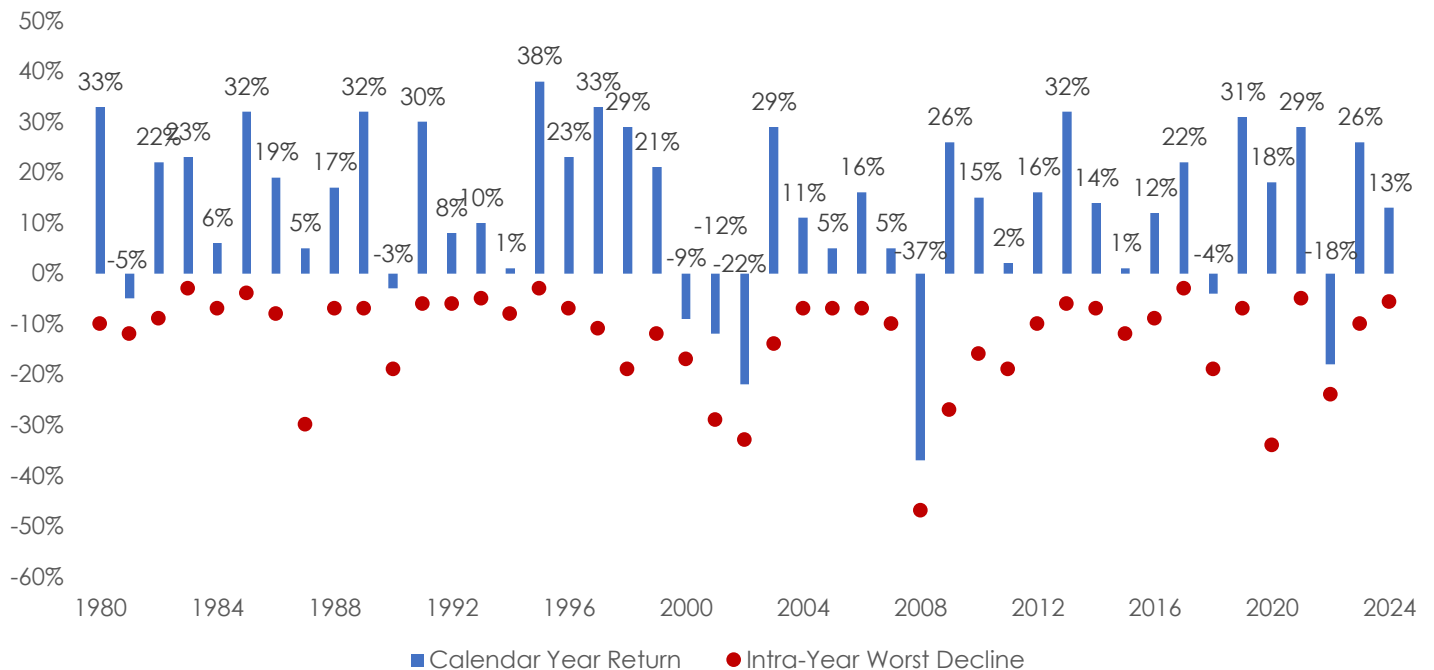
Since 1928, the stock market has dropped more than 5% in 94% of the years and 10% or more in 60% of the years.

Since 1928, the stock market has been negative 47% of the roughly 24,000 individual days and positive only 53% of the days.

It is the nature of markets, and it is the nature of humans. We create cycles and pendulums, and those pendulums swing both ways...and, frequently, too far to either side. This, to some extent, is human nature.

Which brings us to Chart 1:

Chart 1: Standard & Poor's 500 Intra-year Losses vs. Calendar Year Returns since 1980¹



The red dots show how much the Standard & Poor's 500 lost in each year. So, in 1980, the market lost 10%, in 1981 the market lost 12%, and so forth. The blue bars, however, show the full calendar years' returns for each year INCLUDING the losses. So, in 1980, even though the market lost 10% at one point, the full January 1st through December 31st calendar year return was 33%!

Squint a bit and you'll notice three things:

- 1) Every year there are losses.
- 2) Most calendar years are positive.
- 3) The average annual return has been quite strong.

This, of course, doesn't mean the future will be the same. Yet if we believe capital markets are representations of capitalism, and capitalism is driven by human incentives...then there is every reason to believe the future will likely rhyme with the past as a) human nature hasn't changed, and b) those incentives still very much exist.

Yes, but what if...

Inevitably, the question remains: What if this sell-off is the next "big one"? In October 1987, the market fell 20.5% in a SINGLE DAY! In 1974, the market fell 50%, and in 1929, the market lost nearly 90%!

There are two ways to approach this question: the current environment and with historical perspective.

As to the first, in the United States, we are currently in an environment with:

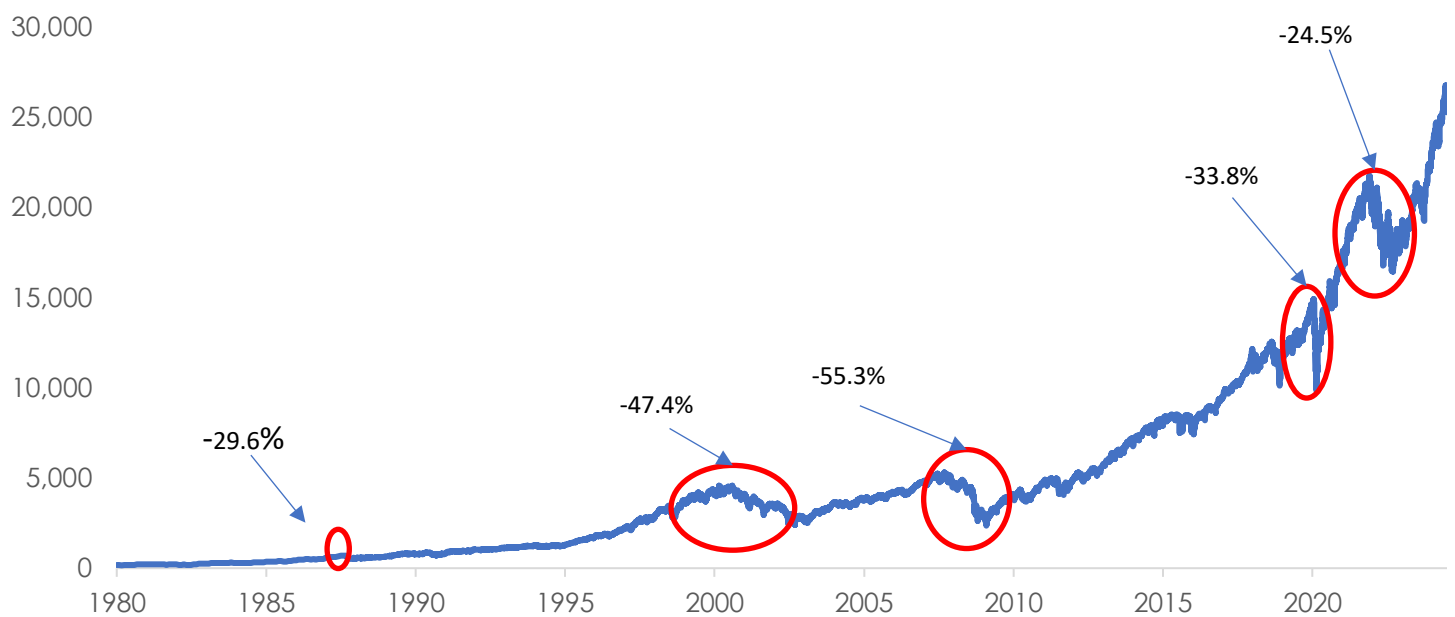
¹ Source: WMIT Research, Bloomberg

- Very low unemployment
- Low(ish) and falling inflation
- The world's most sophisticated central bank (which, yes, is likely a little behind)
- A growing economy
- A very sophisticated (albeit occasionally flawed) banking system
- The world's most liquid and diversified capital market that not only provides capital for productive purposes, but also provides incentives for ingenuity and innovation

Is the market a tad expensive? Yes. Is the market a bit optimistic? Yes. But given the above, I see no reason to believe equity markets will not continue to produce returns above inflation for those that provide capital for productive purposes.

As to the second, Chart 2 provides a historical perspective.

Chart 2: Growth of \$100 in the Standard & Poor's 500 (since 1980)



Historically, I take two things from this chart. First and foremost, when left invested, US equity markets have generated remarkable returns for its investors. Second, the massive generation-defining crises have largely disappeared into the distance with enough time. The "dot com" bubble bursting changed an entire generation of employees and risk taking and yet is largely unnoticed in the chart above. The Black Monday of 1987 would be hidden if I hadn't highlighted it, and the Global Financial Crisis...what was referred to as "the end of capitalism as we know it"...is a mere blip on the radar now that enough time has passed.

In short, focus on the long term and try to ignore the short term. Capital markets (as a representation of capitalism) are alive and well and, while it's likely to be a bit volatile in the near term, I lean toward this being the market "throwing its toys out of the crib," and not a major turning point. Regardless of the short term, we continue watching closely and are at your service. Please let us or your financial professional know how we can serve you.

Daken J. Vanderburg, CFA
Chief Investment Officer
MassMutual Wealth Management

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