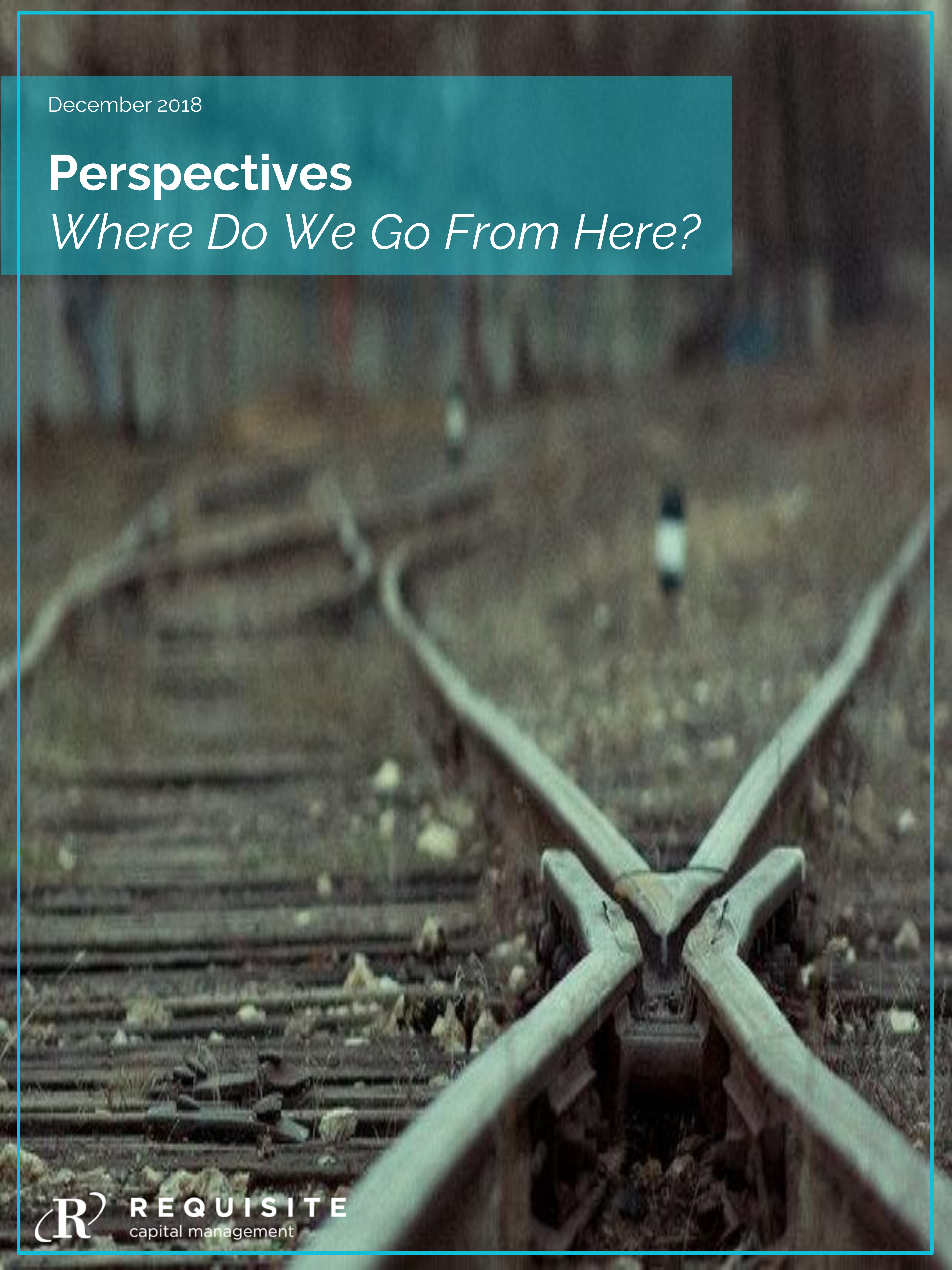
December 2018

Perspectives

Where Do We Go From Here?

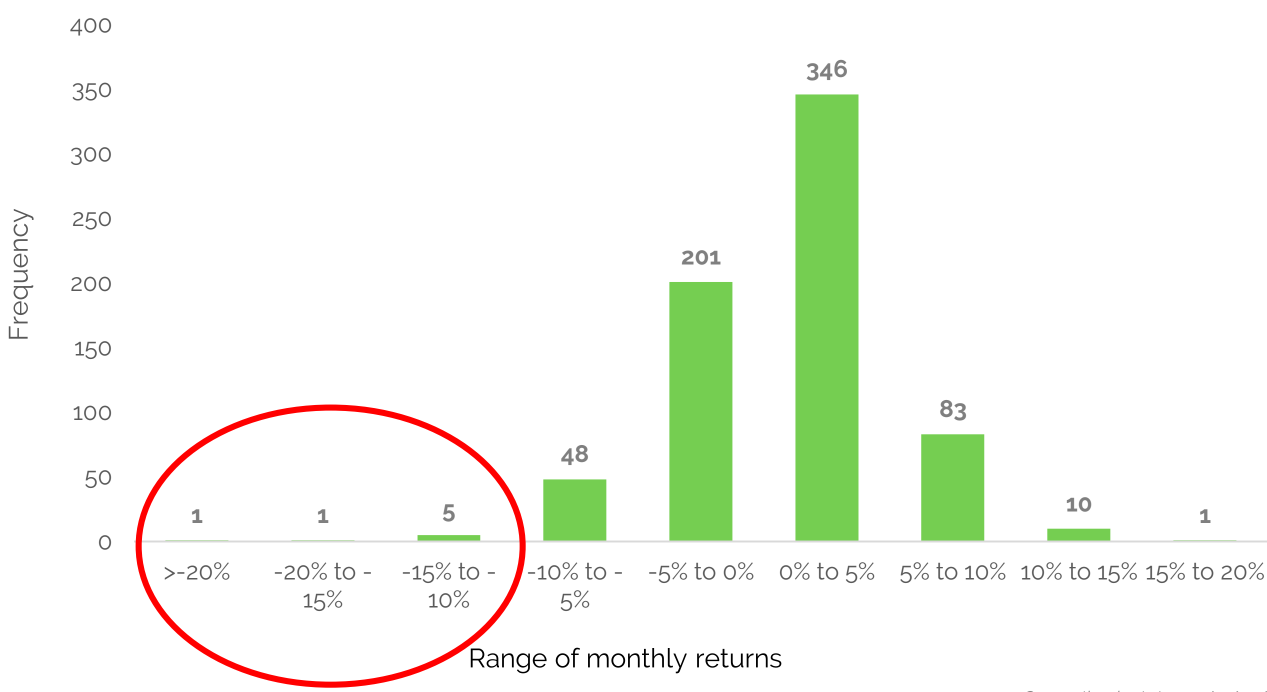


REQUISITE
capital management

December 26, 2018

Where Do We Go From Here?

S&P 500 Monthly Returns (December 1960 - November 2018)



Source: the chart store 12/21/2018

Staying the Course

December is setting up to be one of the worst months for the S&P500 over the last six decades. As of Monday's close (Christmas Eve), the S&P is down 15.7% in December alone. It seems the only thing stopping stocks from going lower is the closing bell. The market is experiencing what feels like an outright buyers strike as bad market technicals, global political, policy trade wars and now, a government shut-down are outweighing the bevy of strong fundamentals (+3% GDP, low unemployment, low inflation and strong corporate profits). Fear in the market has clearly overwhelmed economic reality. Famed professor Jeremy Siegel aptly noted, "Fear has a far greater gap on human action than the impressive weight of historical evidence."

Since December 31, 1960 (696 months), the S&P500 has experienced monthly losses greater than 10%, only seven times, clearly a rare occurrence. When rare occurrences happen, they don't feel rare at all, and this is when fear can overwhelm a well thought out asset allocation plan.

S&P 500 Monthly Drawdowns Greater than 10% (December 1960-December 2018)

Date	Monthly Return
February 28, 2009	-10.65%
September 30, 2002	-10.87%
November 30, 1973	-11.09%
September 30, 1974	-11.52%
August 31, 1998	-14.46%
December 24, 2018	-15.74%
October 31, 2008	-16.80%
October 31, 1987	-21.54%

Source: the chart store 12/21/2018. December 1-December 24 returns: money.net

The economic environments prior to these extreme sell-offs were all very distinct. In the early 70s, President Nixon took the dollar off the gold standard. This was followed by a crippling oil shock that saw oil quadruple from $3 to $12 per barrel. In 1998, markets had to digest an Asian financial collapse, Russian Ruble devaluation and the failure of the famous hedge fund Long Term Capital Management. By 2002, we were at the tail end of the bursting of the tech bubble, while in both 2008 and 2009, global markets were on the brink of financial collapse, due to the massive amount of leverage in the banking system. The reasons for the October crash of 1987 are still debated today, but most will point to computer program trading as the root cause. Regardless of the time period, headlines were terrible and investor sentiment shaken.

Warren Buffet reminds us that, “the market is a device for transferring money from the impatient to the patient”-wise words to remember during these times.

We know the benefits and math of being a long term investor, but long term performance is actually a series of short term data points. If we can’t sit through the short term, then we will never earn the long term returns stocks have generated. What happened after these large drawdowns? What if investors would have been able to stay invested over the next one year? Two years? The following table highlights these draw-downs and how markets fared one and two years later.

Annualized One and Two Year Returns after Monthly Drawdowns Greater than 10% (December 1960–December 2018)

Date	Monthly Return	One Year Later	Two Years Later (Annualized)
February 28, 2009	-10.65%	53.62%	37.22%
September 30, 2002	-10.87%	24.40%	19.02%
November 30, 1973	-11.09%	-23.76%	1.79%
September 30, 1974	-11.52%	38.15%	34.24%
August 31, 1998	-14.46%	39.82%	27.53%
December 24, 2018	-15.74%	???	???
October 31, 2008	-16.80%	9.80%	13.11%
October 31, 1987	-21.54%	14.80%	20.46%

Source: the chart store S&P 500 (Total return) December 1-December 24 returns: money.net

“History doesn’t repeat itself, but it often rhymes.”

-Mark Twain

In Conclusion

We believe in allocating portfolios to both public and private market investments. While private investments have the potential to generate returns in excess of public markets, they are less liquid and mandate a longer term time horizon. While public investments provide daily liquidity; they also provide daily volatility, which can be difficult to sit through in the extremes. Emotions can run rampant in the public markets and fear is very much in play right now. As uncomfortable as this market is, history shows that this too will pass.

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