Emotional Investor Series

The COVID Crash of 2020

White Paper

The Emotional Investor Series explores how current events could lead investors to what we call *Emotional Market Timing* and how better understanding historic markets may help you make informed investment decisions.

The **COVID Crash of 2020** white paper examines the S&P 500's drastic 22 trading day drop of -33.79% and the results that followed.[1]

When the clock struck midnight on January 1, 2020, few people could have predicted the emotional and tumultuous effect COVID-19 would have on their lives. Nor could investors have anticipated the churning feeling they would have in their stomach as they watched the S&P 500 stock index for the 731 days that were to follow.

On February 19, 2020, the S&P 500 hit a new high of 3,386.15, representing a 4.93% index return for the year.[1] That would be the last high for the S&P 500 in a bull market that began on March 10, 2009, returning a remarkable 18.26% annual compounded rate of return during that time.[1] From that high, we would witness a significant decline in the market.

We knew little about COVID in January and February of 2020. This uncertainty transformed into worldwide economic disruption as the medical community and political leaders sought to understand the nature of this virus, how it was transmitted, and how to handle it.

The precarious nature of the virus led to broad stay-at-home orders and set in motion a worldwide disruption in economic activity. In the United States, we saw the unemployment rate reach 14.7% in April.[2] It felt as if we were riding a roller-coaster without being strapped in!

The S&P 500 began to act violently to these events. On Monday, March 9, the S&P 500 fell 225.81 points, which represented a -7.59% drop in value.[1]

On March 12, 2020, the S&P 500 fell 260.74 points, representing a -9.49% loss in a single day.[1]

Finally, on March 16, the S&P 500 plummeted 324.89 points to close at 2,386.13, losing 11.98% in a single day.[1] The drop in stock prices was so massive that the New York Stock Exchange suspended trading several times during those days.

As an investor, how would you have reacted as we headed towards the end of March 2020? Would you have held firm with your investment in stocks, or would you have employed what we call *Emotional Market Timing* and sold all of your stock investments at a loss?

We define Emotional Market Timing as when an investor, nervous about domestic, world, or market events, in essence, panics and engages in an almost spontaneous act of selling their investments.

While every market is different, and past performance is not an indication of future results, in our view, Emotional Market Timing may not be the ideal strategy to use when dealing with stock market fear. That is because Emotional Market Timing centers on alarm rather than conscious rational action.

We believe that the key to grasping the dangers of Emotional Market Timing lies in the understanding that markets will generally rise and fall in cycles, typically moving in large chunks, and many times in what we consider to be short periods.

The COVID bear market was no exception.

This bear market which started on February 19, 2020, would hit bottom by March 23, 2020, losing -33.7% of its value.[1] However, the S&P 500 would recover, making this the shortest Bear Market in the history of the S&P 500, lasting only 33 trading days.[3]

It is important to note that this is a short bear market from a historical perspective. From World War II through the end of 2021, the average bear market has lasted 12 months.[4]

The Trump and Biden administrations helped the market's recovery by passing multiple bills to stimulate the economy, this included help directed at specific sectors like small businesses, cash payments to taxpayers, increases in unemployment insurance, and rental assistance. The Federal Reserve also assisted by providing liquidity to the markets and keeping interest rates low.

This assistance from the government helped the S&P 500 recover. From when the S&P 500 hit bottom on March 23, 2020, through June 30, 2020, just over three months, the S&P 500 returned 39.3%.[1]

From the March 23, 2020 bottom through December 31, 2020, the S&P 500 would return 70.17%.[1] It would have a positive 18.39% return for all of 2020, including the COVID bear market.[1]

Despite COVID-19 and its variants remaining on the scene, causing disruption in 2021, from the bottom of March 23, 2020, through the end of 2021, the S&P 500 returned a cumulative 118.97% rate of return. This is a 55.50% annual rate of return.

It may be difficult not to employ Emotional Market Timing when events occur that disrupt the market, particularly something like a pandemic.

However, because the markets will generally rise and fall in cycles, typically moving in large chunks and many times in what we consider short periods, Emotional Market Timing may not be a prudent strategy to employ.

Sources:

1. Bloomberg and Dunham & Associates Investment Counsel, Inc.

2. U.S. Bureau of Labor Statistics: Unemployment Rate Rises to Record 14.7 Percent in April 2020; https://www.bls.gov/opub/ted/2020/unemployment-rate-rises-to-record-high-14-point-7-percent-in-april-2020.htm?view_full

3. Reuters: Say Goodbye to the Shortest Bear Market in S&P 500 History; https://www.reuters.com/article/us-usa-stocks-s-p500-bear-graphic/say-goodbye-to-the-shortest-bear-market-in-sp-500-history-idUSKCN25E2R9

4. Dunham Market Cycle Chart

Disclosures:

Investments are subject to risks, including possible loss of principal. Investors should consider the investment objectives, risk factors and expenses of any investment carefully before investing. Diversification does not guarantee profit or ensure against loss.

The S&P 500, or the Standard & Poor's 500, is a stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 Index components and their weightings are determined by S&P Dow Jones Indices. It differs from other U.S. stock market indices, such as the Dow Jones Industrial Average or the Nasdaq Composite index, because of its diverse constituency and weighting methodology. It is one of the most commonly followed equity indices, and many consider it one of the best representations of the U.S. stock market, and a bellwether for the U.S. economy. You cannot invest directly in an index.

A bull market indicates a sustained increase in price, whereas a bear market denotes sustained periods of downward trending stocks - typically 20% or more. The term “bull vs bear” denotes the ensuing trends in stock markets - whether they are appreciating or depreciating in value - and what is the investors’ outlook about the market in general. Bull markets generally coincide with periods of robust economic growth; investor confidence is on the rise, employment levels are generally high, and the economic production is strong. During the bearish phase, companies begin laying off workers, leading to a rise in unemployment and, consequently, an economic downturn.

No investment strategy or risk management technique can guarantee returns or eliminate risk in any market environment.

All examples are hypothetical and are for illustrative purposes only. We encourage you to seek personalized advice from qualified professionals regarding all personal finance issues. The solution for an investor depends on their and their family’s unique circumstances and objectives.

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