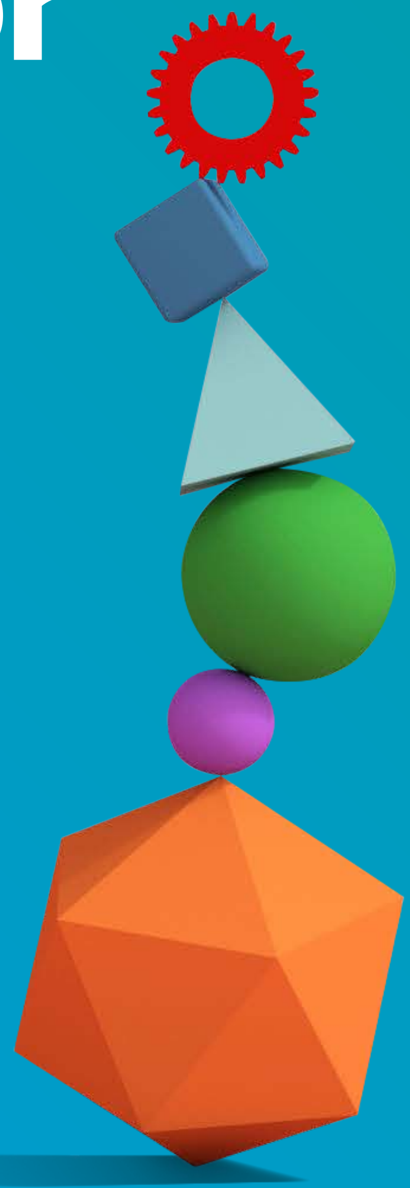
Mercer

investment performance and COVID-19

what should an investor know?

June 2021



welcome to brighter

COVID-19 Impact on Financial Markets – Bull vs. Bear The last fifteen months have undoubtedly been among the most unique in the history of the stock and bond markets. What makes the COVID-19 bear market (or market decline) particularly unique is that, of the major historical markets in history, it was the first and only to be caused by a non-financial related event. Unlike other crises, COVID-19 was the root of the problem causing the panic selling at the beginning of the pandemic at a speed unique to other market downturns.

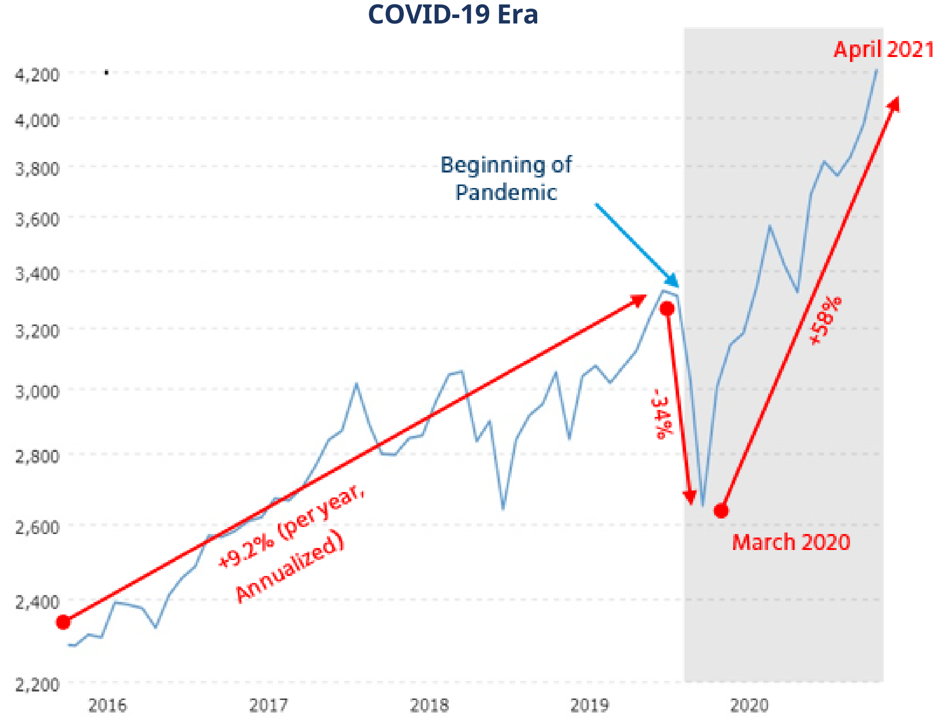
Results – Stocks, Bear From the beginning of the downturn on February 20th to March 23rd, 2020 (the market bottom) the U.S. stock market, as measured by the S&P 500, fell 34%, making it the second only to the fastest decline of the famed 1987 stock market crash, where the U.S. market, as measured by the Dow Jones Industrial Average at the time, fell 22% in a single day. Although the market in this case had an immediate recovery within the next week, it went on to lose a total of 33% before fully recovering nearly two years later in September of 1989.

Results – Stocks, Bull What was equally unique and unexpected as the onset of COVID-19 and the sharp market decline, was the speed of the stock market recovery that followed immediately after the market bottom on March 23rd. Since then, the S&P 500 is up 81%, as of April 30, 2021. The international non-U.S. stock markets experienced a similar selloff and rebound during this timeframe. As a matter of fact, no major stock markets have returned less than 50% since the market bottom on March 23rd, 2020. When a runaway bull market, an upward moving market, delivers such extremely high returns over a period of time such as a year, it makes short-term performance returns (like a return for a 3-month period) look too good to be true and inflates longer term historical returns (like 3- or 5-year returns) to a lesser degree.

Results – Bonds Unlike stocks, the bond markets have not fared so well over the latest year. The most widely referenced bond index, the Bloomberg Barclays Aggregate Index, has returned -2.6% in 2021 through April 30th. The index has only delivered a negative return during four calendar years since 1980, with the last negative year being 2018 (-0.05%) and the worst being 1994 (-2.92%).

did you know?

Ever wonder where the terms ***Bull and Bear Markets*** come from? Interestingly enough, the actual origins of these expressions are not entirely clear. The terms "bear" and "bull" are thought to derive from the way in which each animal attacks its opponents. That is, a bull will thrust its horns up into the air, while a bear will swipe down. These actions were then related metaphorically to the movement of a market. If the trend was up, it was considered a "bull market". If the trend was down, it was a "bear market".



Pre/Post COVID Returns

Pre-COVID 5-Year Historical Trailing Return: 9.2%

Post-COVID 5-Year Historical Trailing Return: 16.3%

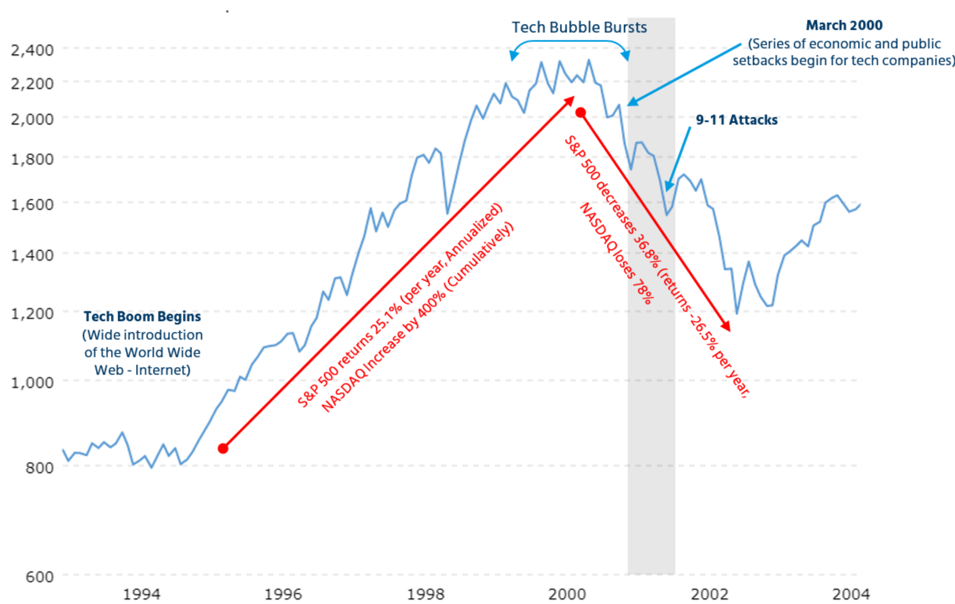
Historical Average 10.5%

Notable points:

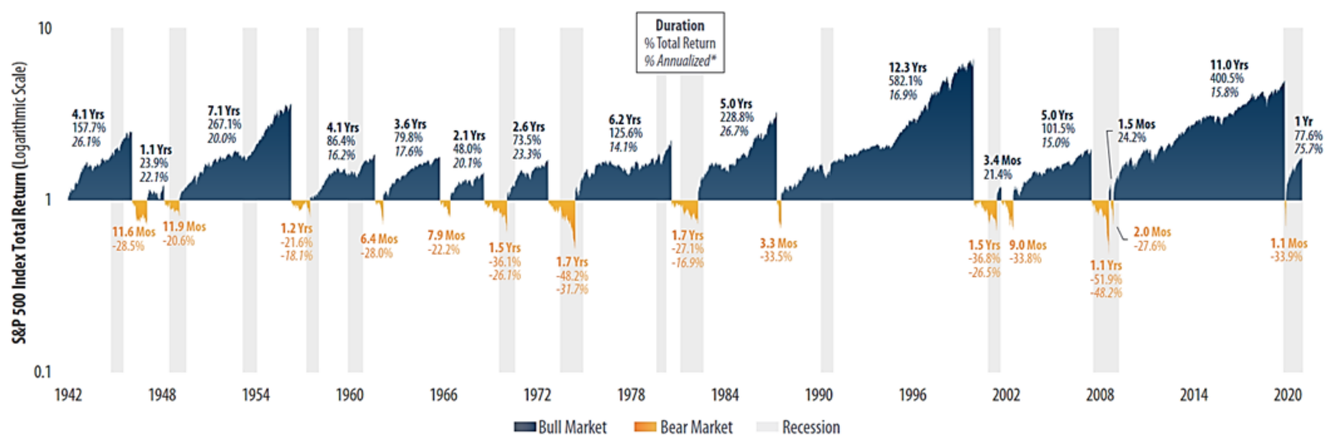
- The S&P 500 returns essentially doubled over the last 5 years.
- 4 of the last 5 years were more or less consistent with the long-term stock market performance average.
- While the rebound is welcome news, the current return environment is not sustainable.
- Although bull markets tend to last longer than bear markets, they do have a limited life.
- Complacency and/or overconfidence and excessive risk taking can lead to disappointing or even devastating results in the short- and long-term.
- The sharp stock market rebound may lead many investors to take on more risk than they had in the past.

Past Events – Similar Outcomes Notable events of the past have led to similar market experiences and reactions by investors. Many parallels can be drawn between current investor behavior and that of the "Tech or Dot-Com Boom" of the late 1990s when investors invested and bet heavily on the continued performance of technology stocks, mostly internet stocks in their infancy. The Nasdaq Composite Index had risen 400% between 1995 and March 2000 only to lose nearly 80% of its value from its peak, resulting in a market crash known as the "Tech Wreck". The graph below depicts returns before and after the "Tech Wreck".

S&P 500 Performance
COVID-19 Era



Other notable bull and bear markets



Source: First Trust Advisors L.P., Bloomberg. Daily returns from 4/29/1942 - 3/31/2021. *No annualized return shown if duration is less than one year. **Past performance is no guarantee of future results.** These results are based on daily returns–returns using different periods would produce different results. The S&P 500 Index is an unmanaged index of 500 stocks used to measure large-cap U.S. stock market performance. Investors cannot invest directly in an index. Index returns do not reflect any fees, expenses, or sales charges. This chart is for illustrative purposes only and not indicative of any actual investment. These returns were the result of certain market factors and events which may not be repeated in the future.

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Conclusion Although COVID-19 is the first crisis of its kind to severely affect the stock markets causing a bear market followed by the fastest bull market rebound in history, it is only one of several crises to have a similar effect with the Tech Bubble being only one example exhibiting both investor overconfidence as the market rapidly increased and fear caused by the severe stock market decline. Although the details may vary, all bear market crashes like Tech Wreck and the 2008 Mortgage Meltdown, have similar characteristics with similar outcomes, with the most stressed areas of the market, being hit the hardest. It is times like these that investors using different securities, bonds and stocks, to “diversify” their risks works over the longer term while the market settles down and reverts to some “normalcy”. The investors that stay the course with diversified portfolios are rewarded over the long run.