LAWSON KROEKER

As we see it

"The most important thing is to stay the course—not to get shaken out of the market during a difficult time."

- John W. Rogers, Jr.

The stock market ended 2018 on a note that surprised many as the upward progress achieved through September was offset by the fourth quarter's downturn. Having been spoiled by only positive performance from the S&P 500 since 2009, market commentators turned more dour than usual at the end of the year. So, what does history tell us about the current market compared to prior market downturns? Should we be concerned?

A recent study reported in the American Association of Individual Investors may help analyze the market's fourth quarter downturn. A common rule of thumb is to classify market downturns into one of three buckets—Pullbacks (market declines 5.0-9.9%), Corrections (-10.0% to -19.9%) and Bear Markets (-20% or more). Not surprisingly, the deeper the market's drop the longer required to recover from the bottom.

History tells us that pullbacks for the S&P 500 index (comprised of the market's largest firms) have typically lasted for a month on average and required two months to recover. Corrections lasted five months on average, but only needed four months to make up lost ground. True Bear Markets were certainly a more formidable foe—when they actually occurred—lasting seventeen months on average and about three years to recover. However, since December of 1989, we have only had three bear markets and three dozen pullbacks and corrections, yet the latter instances were often treated with the same discourse at the time as if they were full bear markets.

S&P 500 Average Decline and Recovery Durations (December 1989 Through July 2017)

Type of Decline	Number	Average Drop From Peak (%)	Duration (Months)	Time to Recovery (Months)
Market Cap-Weighted S&P 500 Index				
Pullback (5.0%-9.9%)	29	-7	1	2
Correction (10.0%-19.9%)	7	-15	5	4
Bear Market (>20%)	3	-42	17	36
Equal Weighted S&P 500 Index				
Pullback (5.0%-9.9%)	30	-7	1	2
Correction (10.0%-19.9%)	9	-14	3	3
Bear Market (>20%)	5	-35	11	11

Source: S&P Dow Jones Indices

Small-Cap Average Decline and Recovery Durations
(December 1994 Through July 2017)

Type of Decline	Number	Average Drop From Peak (%)	Duration (Months)	Time to Recovery (Months)
Russell 2000 Index				
Pullback (5.0%-9.9%)	24	-7	1	1
Correction (10.0%-19.9%)	12	-13	3	3
Bear Market (>20%)	7	-35	9	18
S&P SmallCap 600 Index				
Pullback (5.0%-9.9%)	31	-7	1	1
Correction (10.0%-19.9%)	16	-13	2	3
Bear Market (>20%)	6	-34	8	11

Source: CFRA S&P Dow Jones Indices

If we dig deeper into the market's resiliency, it is interesting to see the difference in the behavior of the smaller companies we often invest in. Most notable is that the smaller firms in the Russell 2000 index tend to have downturns that are less pronounced, last nearly half as long, and recover considerably faster. Combined with the attractive growth opportunities we often find in the small cap market, these defensive characteristics further strengthen our resolve in building portfolios incorporating smaller firms.

So where are we today? Whether history ends up categorizing the fourth quarter decline as a Correction or a Bear, investors must continue to look and move forward. While we never know what is around the corner, the New Year has so far brought an emerging recovery that moves us farther away from the dreaded bear territory. Present data would suggest we are in one of the lesser downturns that have happened—on average—more than once per year in the last 30 years.

As easily as the market could turn lower so could it continue to recover, already pushing us forward on the road to recovery. The days and weeks ahead will decide if the current market concerns are warranted.

Looking forward it is more important to focus on where we are going rather than where we have been. We know the key to long-term financial success is to stay on the path proven profitable time and again. Pullbacks, corrections and even bear markets come and pass, yet over time, the economy expands, enterprises grow, and long-term capital providers are rewarded. Knowing that timing the market is an unprofitable effort, our focus remains on deploying investor capital to the most promising opportunities. Our aim is to continue to invest in the businesses that will deliver compelling returns through all the turns and cycles that may lie ahead.