KLCM Advisors, Inc.

**July 2020**

## Staying the Course

Looking back at the first half of 2020, it seems as though six years, not months, have passed. After entering the year with a strong economic backdrop, including growing wages for the rank and file, we are now trying to bring the economy out of a self-induced coma. The spreading of the coronavirus and the subsequent attempt to flatten the curve via social distancing is undoubtedly the greatest demand shock ever placed on our economy. The health crisis led to significant selling in the equity markets as market participants dashed for cash resulting in the fastest bear market in history, taking only 16 days to fall 20%. As markets continued to fall, the Federal Reserve and Congress scrambled to develop monetary and fiscal programs to support the economy. The programs ultimately provided several trillion dollars of direct support to businesses, stimulus checks to individuals, and extended and expanded unemployment benefits. Throughout the stay at home orders, market volatility remained extraordinarily high as news flow was tenuous and reporting sensationalized. As states began to reopen for business, the stock market began to anticipate an economic rebound. Once again, markets set a record taking a mere 12 days to recover 20% off their lows, leading many to proclaim that a new bull market had begun.

With unemployment remaining in the 15% range while fears still abound over a second wave of the coronavirus, volatility remains elevated. The government is currently considering a second round of stimulus to boost the economy further. The first round of stimulus prevented credit markets from freezing up and allowed many companies to issue debt that they would not have typically had access to in a normal recession, let alone in a frozen economy. This helped companies avoid having to take more drastic actions with their workforces. In the short run, this stimulus has and will undoubtedly continue to have a positive impact on our economy. Unfortunately, there is no free lunch, and all this liquidity sloshing around has increased the chances and severity of a financial accident in the future.

In a world of elevated valuations, where nearly all financial assets are expensive, value stocks trade at an unprecedented discount. Many of these are discounted because the economic recovery is still in question. **We know for sure that a recovery has followed every economic recession and depression.** Economic activity will begin to accelerate from depressed levels, and earnings for these types of companies will grow quickly. These companies are financially strong, have ample liquidity, and many are heavily engaged in buying back their own shares. Special situations with favorable risk-reward characteristics and some cash to take advantage of continued turbulence round out our equity portfolios.

Our simple belief is that over any reasonable timeframe the equity markets will move higher. Patient investors ultimately are rewarded, though patience is tried at times. Our financial markets will continue to allow individual investors to accumulate wealth and allow prudent individuals to achieve their financial goals. Perhaps Benjamin Graham said it best, "*The best way to measure your investing success is not by whether you're beating the market but by whether you've put in place a financial plan and a behavior discipline that are likely to get you where you want to go.*" Once you've put your plan in place, it is important to stay the course as John Bogle, founder of The Vanguard Group, stated, "*Your success in investing will depend in part on your character and guts* *and in part on your ability to realize, at the height of ebullience and the depth of despair alike, that this too shall pass*." Both of these men using different investment philosophies were trying to make the same point; investment success is driven more by the amount of time you are in the market and sticking to a plan than trading in and out and trying to time the market. As the following chart highlights from the depths of Bogles' despair recoveries can, do, and will happen.

**Equity Bear Market Statistics Through History (S&P 500)**

| Bear Market Start | Bear Market End | Time (Months) | Max % Loss | Recovery 12-Months After | Recovery 24-Months After |
|---|---|---|---|---|---|
| October 2007 | March 2009 | 17 | -57% | 69% | 95% |
| March 2000 | October 2002 | 30 | -49% | 34% | 44% |
| August 1987 | December 1987 | 3 | -33% | 21% | 57% |
| November 1980 | August 1982 | 20 | -27% | 58% | 61% |
| January 1973 | October 1974 | 20 | -48% | 38% | 67% |
| November 1968 | May 1970 | 17 | -36% | 44% | 60% |
| February 1966 | October 1966 | 7 | -22% | 33% | 42% |
| December 1961 | June 1962 | 6 | -28% | 33% | 56% |
| August 1956 | October 1957 | 14 | -22% | 31% | 44% |
| AVERAGE | | 15 | -36% | 40% | 58% |

Source: Bloomberg

Each prior bear market had a different cause and reason why at their nadir, things could never get better. While the solutions were similarly different, ultimately, the issue at hand was resolved, and our economy and market moved forward. One year later, investors on average were almost back to where they started, and after two years were well ahead of prior high-water marks, provided they stayed the course.

Our best and brightest scientists and researchers, when focused on a problem with an unlimited amount of capital, will find a solution for the coronavirus, and life will go on. Betting against the resiliency of the United States has been a losing bet for the entirety of history. Patience will be rewarded, and as Don Connelly stated, "*There have been a lot of lucky sprinters in history, but there have been no lucky marathoners. It takes planning and perseverance to win a marathon.*"

Have a fabulous summer!