

# In the Markets Now

Looking ahead from a difficult 2022

We believe in the old saying: a picture is worth a thousand words. Here, we aim to recap recent market action and provide some perspective to investors.

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## HOW DO STOCKS PERFORM AFTER A BAD YEAR?

Though many may still be “crossing the t’s and dotting the i’s” on 2022, we’d all be forgiven for wanting to just put a year like 2022 behind us. Spurred on by historic inflation, rapidly rising interest rates, and heightened geopolitical tensions, the S&P 500 had one of its worst years in recent memory (while the bond market had one of its worst years ever). [As our own Michael Antonelli put it](#), “That was a painful 365 days to be an investor.”

But what’s done is done, and so we look ahead to 2023. At a high level, there are both many headwinds and tailwinds to account for ([and Baird has some tremendous pieces](#) that break down many of those issues in depth). In short, the Fed is still raising rates, geopolitical tensions have decidedly not come off the boil, and recession risk is elevated. On the other hand, inflation is coming down, the consumer is proving resilient, and the international economic picture is actually brightening a bit. It is both a volatile and complex landscape to assess.

But let’s put all of that aside for a moment and dig into a somewhat simpler exercise. Here, we look at the 15 worst years for the S&P 500 in roughly the last century, and then examine how the index performed in subsequent years (see table). **The good news is there’s a lot of green there, and often fairly quickly after the conclusion of the rough year in question.** Of the years worse than 2022, only the Great Depression saw the bear market persist much into the future. And as there is debate about whether a recession will even materialize, we can at least conclude that the economic outlook is brighter than that of the early 1930s. In the end, the average five year return is 11.1%, which is actually higher than the all-year average.

Worst years for S&P 500 in last century		Performance following that year:		
		One year later	Three years later (ann.)	Five years later (ann.)
1931	-43.3%	-8.2%	11.7%	22.5%
2008	-37.0%	26.5%	14.1%	17.9%
1937	-35.0%	31.1%	5.6%	4.6%
1974	-26.5%	37.2%	16.4%	14.8%
1930	-24.9%	-43.3%	-7.1%	3.1%
2002	-22.1%	28.7%	14.4%	12.8%
2022	-18.1%	-	-	-
1973	-14.7%	-26.5%	7.7%	4.4%
2001	-11.9%	-22.1%	3.6%	6.2%
1941	-11.6%	20.3%	22.0%	17.9%
1957	-10.8%	43.4%	17.3%	13.3%
1966	-10.1%	24.0%	8.0%	8.4%
1940	-9.8%	-11.6%	10.2%	17.0%
2000	-9.1%	-11.9%	-4.1%	0.5%
1962	-8.7%	22.8%	17.2%	12.4%
Average		7.9%	9.8%	11.1%

We also ran similar numbers using a 60/40 portfolio. Much of this year’s pain has come from the simultaneous selloff of two asset classes – stocks and bonds – which had long been expected (or hoped?) to hedge one another. While that notion may have been busted somewhat, there is at least good news again in the data: forward returns for a stock/bond mix from deeply negative years are quite positive across history, especially on the heels of a rapid tightening cycle like the one we just experienced. In many ways, the outlook for both stocks and bonds is improved markedly after the year we just experienced.

Still, past performance is no guarantee of future returns. There are several examples of multiple down years in a row (though only two since World War II) and, as noted above, economic headwinds remain. **Of course, there’s never been a point in history where there haven’t been headwinds, and the market still averaged a return of ~10% a year over the last century regardless.** While we don’t know exactly when the bear market will end, we do know that it almost always occurs when the economic data is still challenged and the headwinds still prominent. So, as we move into a new year, remember the table above, and when volatility inevitably rears its ugly head, lean on your Baird Advisor for help shoring up your plan and staying the course.

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