ACADEMY
FINANCIAL, INC.
EVALUATE • ENVISION • EXECUTE

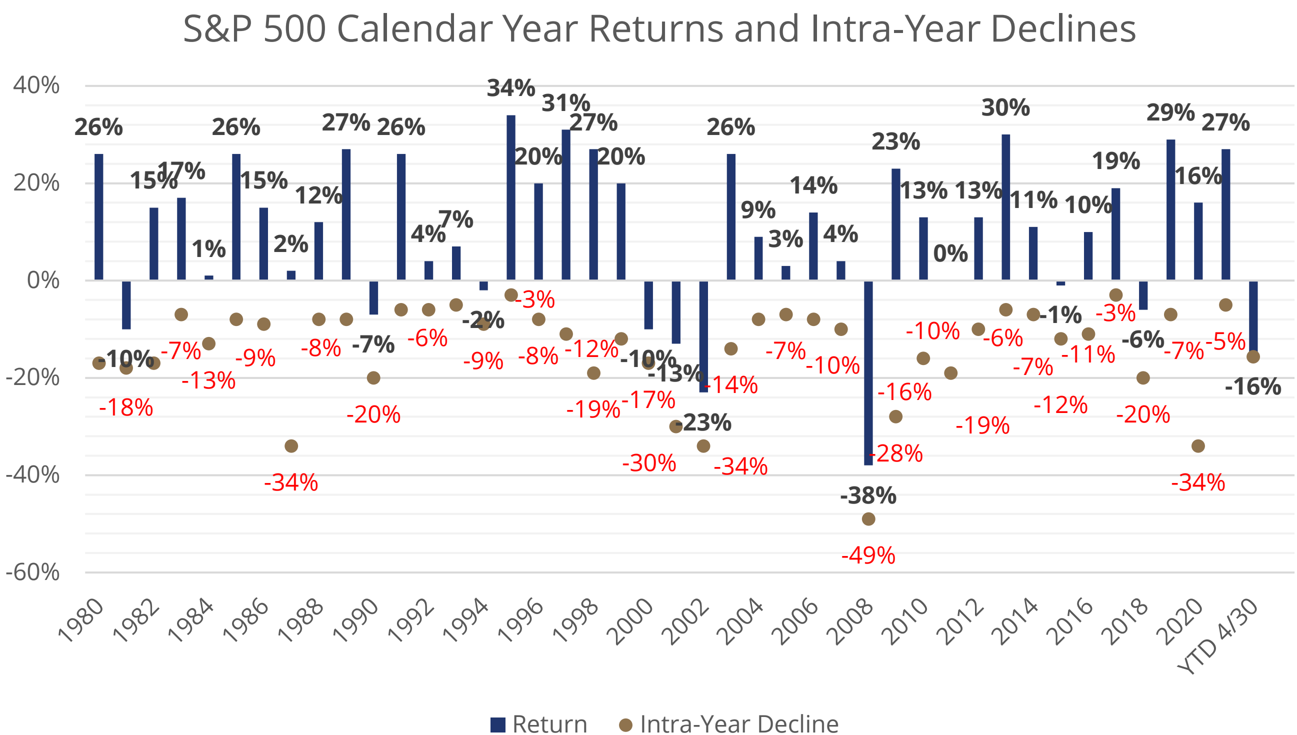
Summary

After a relatively uneventful 2021, volatility has meaningfully increased in 2022. The S&P 500 is down 18% from its January 3rd peak, while the sell-off in tech has sent the Nasdaq down 29% from its November 19th high. To make matters worse, bonds have also been hit with the US Aggregate Bond Index down almost 10%.[1]

Why has volatility increased so significantly? The war in Ukraine is causing a surge in commodity prices, COVID lockdowns in China are delaying supply chain recoveries, and the Fed is aggressively tightening monetary policy in response to 40-year high inflation numbers. The combination of these factors has added uncertainty to future growth forecasts. Given all the uncertainty surrounding the economic outlook, we expect volatility to remain high. However, it is important to remember that the US consumer has been resilient, the labor market is strong, and corporate profits are still growing.

Market Reaction

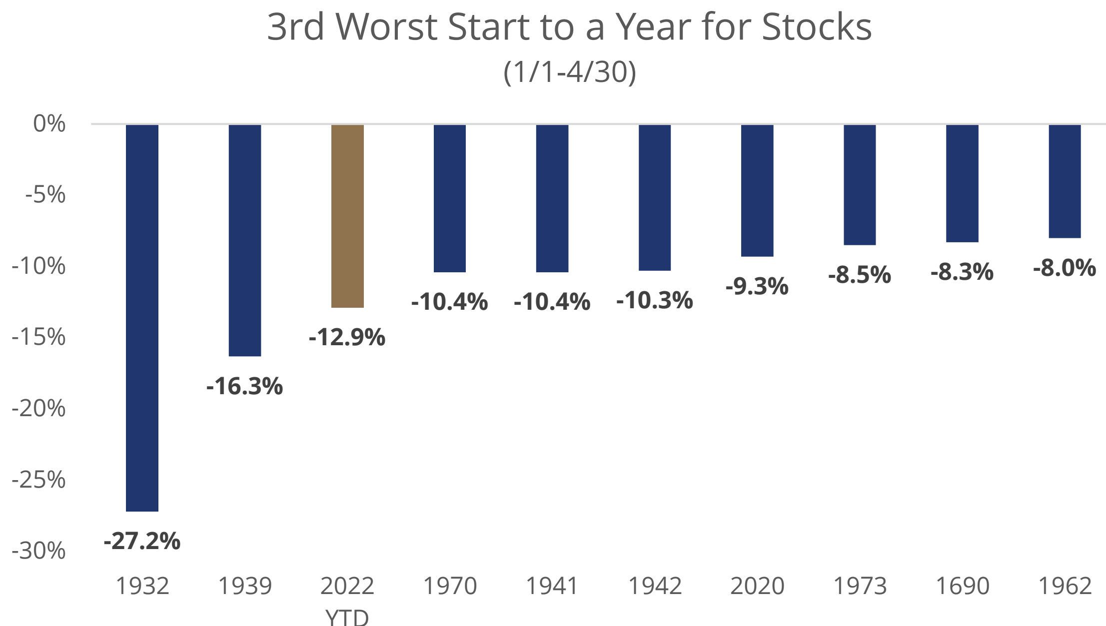
Although market drawdowns can be stressful, they are not unexpected. Since 1980, the average intra-year drop has been 14% and annual returns have been positive 32 of 42 years.



Source: YCharts

[1]Source: YCharts as of 5/12/22

The current drawdown in the market is in line with the historical average. However, it is unusual for the year to start like this. 2022 had the 3rd worst start to the year for stocks and the worst start to the year for bonds.



Source: Morningstar as of 4/30/22

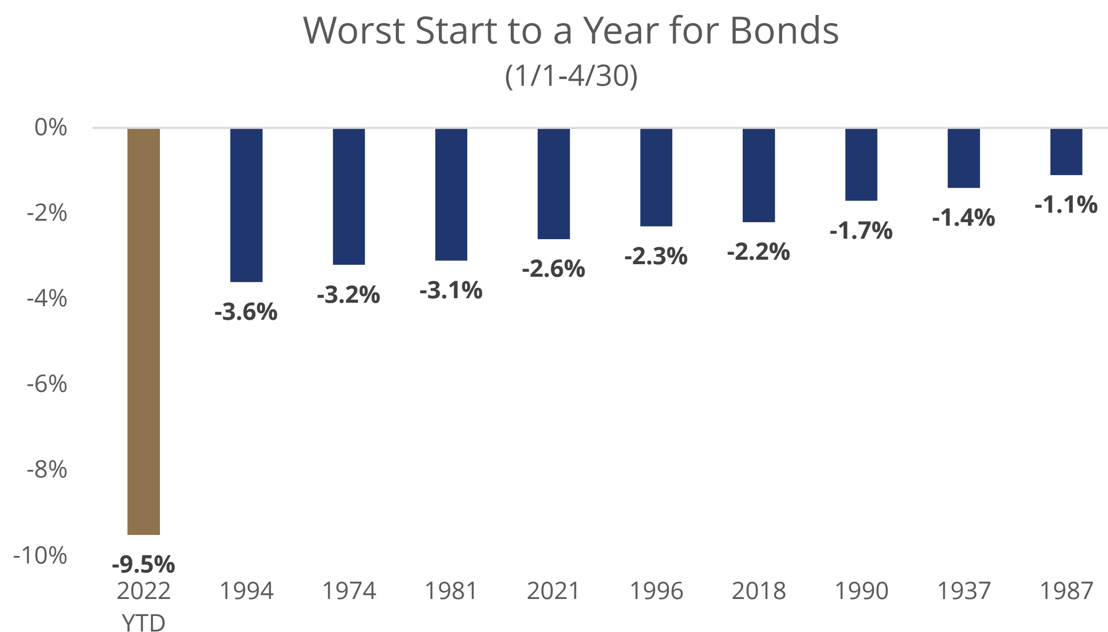
Looking at the other nine worst starts for stocks, the next eight and twelve months average double-digit returns. Through multiple wars, recessions, pandemics, and other crises, the S&P 500 has always recovered and surpassed its prior peak.

Year	First 4 Months	Next 8 Months	Next 12 Months
1932	-27.2%	26.2%	54.6%
1939	-16.3%	19.0%	17.7%
2022 YTD	-12.9%	?	?
1970	-10.4%	16.0%	32.1%
1941	-10.4%	-1.4%	-11.5%
1942	-10.3%	34.1%	61.2%
2020	-9.3%	30.5%	46.0%
1973	-8.5%	-6.7%	-12.6%
1960	-8.3%	9.5%	24.2%
1962	-8.0%	-0.8%	10.8%
Average	*-12.2%*	*14.1%*	*24.7%*

Source: Morningstar as of 4/30/22

The fixed income market has largely been reacting to The Fed's response to inflation. The target for the federal funds rate was raised by 0.50% at The Fed's May meeting. It was the

first increase of that size in more than 20 years and it is likely that there will be at least two more 0.50% hikes this year. In addition, the Fed announced it will begin the quantitative tightening process in June by allowing bonds on its balance sheet to mature without reinvestment. This policy change in combination with other market risks has led to the worst start to a year for bonds in history.



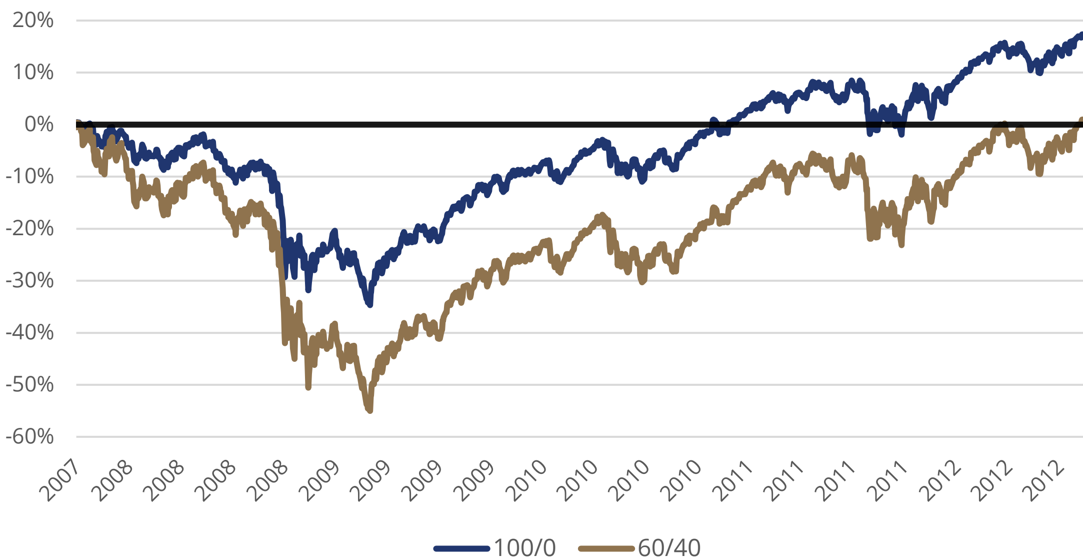
Source: Morningstar as of 4/30/22

Going forward, the increase in interest rates will provide more income and return potential. Historically, returns following the worst starts have almost all been positive. 2022 has certainly been much worse than other similar periods for bonds, but there is potential to recover from this low point as market participants reinvest at higher interest rates.

Year	First 4 Months	Next 8 Months	Next 12 Months
2022	-9.5%	?	?
1994	-3.6%	0.8%	8.6%
1974	-3.2%	9.2%	8.6%
1981	-3.1%	9.7%	17.1%
2021	-2.6%	1.1%	-8.5%
1996	-2.3%	6.1%	7.1%
2018	-2.2%	2.3%	5.3%
1990	-1.7%	10.9%	15.2%
1937	-1.4%	3.0%	6.7%
1987	-1.1%	3.9%	7.3%
Average	*-3.1%*	*5.2%*	*7.3%*

Source: Morningstar as of 4/30/22.

When the market is down, it can be useful to remember the importance of portfolio construction. Diversification allows investors to capture upside while reducing risk for better risk-adjusted returns. A portfolio of invested in 100% stocks at the peak in October 2007 did not recover from the Great Financial Crisis bear market until April 2012. However, a 60/40 portfolio recovered a year and a half earlier in November 2010.



Source: YCharts. 100/0 portfolio is composed of SPY. 60/40 portfolio is composed of SPY and AGG.

What Should You Do?

- *Maintain composure and stick to your investment plan.* The team at Academy Financial builds portfolios and financial plans assuming that there will be market drawdowns. It is extremely difficult to predict when they will happen but utilizing a disciplined process can produce asset growth and downside protection.
- *Stay invested when you feel the worst* – sentiment does not have a great track record for guiding investor behavior. Since 1970, average one-year equity returns following peaks in consumer sentiment were 4.1%, but average returns following the bottoms in sentiment were 24.9%.[2] In our view, investors should be thinking less about how much further markets will fall and more about what could cause a positive shift and how to position correctly for that change.
- *Reach out to your Academy Financial Planner* – we want to make sure you feel confident with your assets. If you have questions, are interested in adding more protection, or want to review your long-term plan, don't hesitate to contact us.

Blake Gaulden, CFA, CFP®

Chief Investment Officer

The S&P 500 Index is the Standard & Poor's Composite Index of 500 stocks and a widely recognized, unmanaged index of common stock prices. You cannot invest directly in an index. Past performance does not guarantee future results. Diversification cannot eliminate the risk of investment.

The information contained in this report does not purport to be a complete description of the securities, markets, or developments referred to in this material. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. Any opinions are those of Academy Financial and are not necessarily those of Lincoln Financial Advisors. Expressions of opinion are as of this date and are subject to change without notice. This information is not intended as a solicitation or an offer to buy or sell any security referred to herein. Investments mentioned may not be suitable for all investors. Investing involves risk, and investors may incur a profit or loss.

Forward looking statements may be subject to certain risks and uncertainties. Actual results, performance, or achievements may differ materially from those expressed or implied.

Registered associates of Academy Financial, Inc. are registered representatives of Lincoln Financial Advisors Corp. Securities and investment advisory services offered through Lincoln Financial Advisors Corp., a broker/dealer (member SIPC) and registered investment advisor. Insurance offered through Lincoln affiliates and other fine companies. Academy Financial, Inc. is not an affiliate of Lincoln Financial Advisors Corp.

CRN-4746473-051722