HIGHTOWER
Westchester

# My Window

*This market commentary is a bit different than the ones we typically write. Usually when we provide market commentary, we do so in the third person to provide overall commentary, not a personal narrative. This particular narrative was written by Peter Lang about his family and legacy and the lessons we can glean from history.*

First and foremost, I hope each of you and your loved ones are safe, healthy, and are beginning to find a rhythm in our new norm.

While staring out the window into my backyard on day one of officially working from home, I decided to write down some thoughts about putting the current events into perspective.

My thoughts immediately jumped to what my parents and grandparents went through many years ago. Both my maternal and paternal sides of my family are from Germany. Both of my grandfathers were frontline soldiers in World War 1 and both received Iron Crosses (similar to a purple heart). My maternal grandfather was a POW in Russia. One of our family's prized possessions is a letter he wrote my grandmother on a piece of birch bark tied with dried flowers saying he was OK. I try to wonder what things must have gone through both of their minds – my grandfather probably not exactly having sanitary or even safe conditions, my grandmother, relatively newly married, thinking she was going to be a young widow. At the same time the world was being ravaged by the Spanish flu of 1918, killing more people than the war itself. It is estimated that some 500 million people were infected and almost 50 million people died, with 675,000 deaths in the United States alone.

President Woodrow Wilson hardly ever mentioned the flu or measures taken to prevent it, and most businesses stayed open. At the time we were a largely agrarian society so social distancing was much easier standing in a corn field.

There are many investors and news outlets comparing the COVID-19 virus to the Spanish flu, in which millions of people died. Much of the economic effects of the 1918 influenza pandemic were relatively short term, with industries reporting mixed results. In what we are seeing as a similar trend, health care businesses fared better than those in services and more cyclical sectors. The key then, as it is now, is that you were well-diversified. When you look back on that time period, with something as devastating as that influenza pandemic was, the economy recovered and went on to do very well after that (see chart below).

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Fast forward 10-15 years to the Great Depression. I am sure some of our older clients have vague memories of it, but more than that, many of our clients grew up with their parents who came of age in the Great Depression, the same way many of the millennials of today grew up in the shadow of 2008-09.

It took the United States more than three years to recover after the devastating stock market crash of 1929. During the depths of the Great Depression, in 1931, the Dow Jones Industrial Average lost a little over 30% over the course of one month, according to data from Morningstar Direct.[1] When you look at the speed of the recent drawdown in markets, we are seeing something similar.

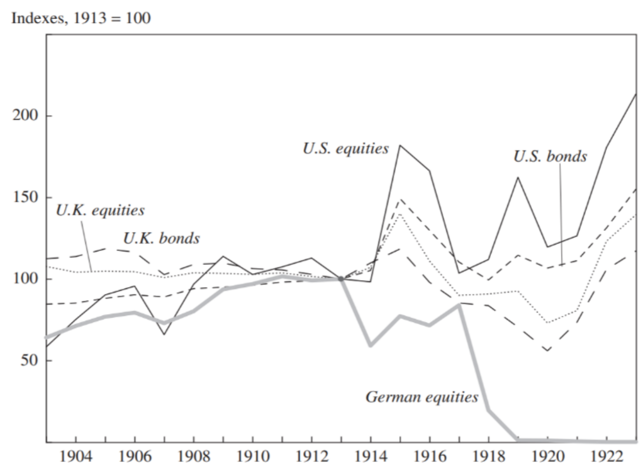
My parents were both born into relatively affluent households in different parts of Germany in the early 1930's, on the eve of the Holocaust. After the war, both of my Grandfathers went on to become successful merchants and shopkeepers – today we would call them entrepreneurs. Through their hard work, they were able to provide a stable home for both of my parents. Suddenly in the mid-late 1930's their world vanished. But both were lucky.

My mother's family fled the country in the late 1930's over the border to Belgium and sailed to America. They were lucky because one of my great-aunts and uncles had come to the states years before and were able to sponsor them for immigration. Could you imagine what it must have been like, fleeing their country with only a few of their worldly possessions to start all over again? But that's what they did. My grandfather stuck with his entrepreneurial spirit and started multiple companies, one of which is still around today in some form, although no longer owned by our family.

My father's tale was a bit more distressing, not leaving Germany until 1939, with all of his possessions in one suitcase, he and his sister waving goodbye to their parents on the train platform as they left for England. They too were lucky; they had an uncle living in London who took them in and a few months later their parents managed to get to London as well. Sadly, my grandfather passed shortly after arriving in London, leaving my grandmother to work odd jobs to support my father and his sister. From there my father lived through the blitz, being evacuated to the country, and finally on a harrowing voyage across the ocean to America.

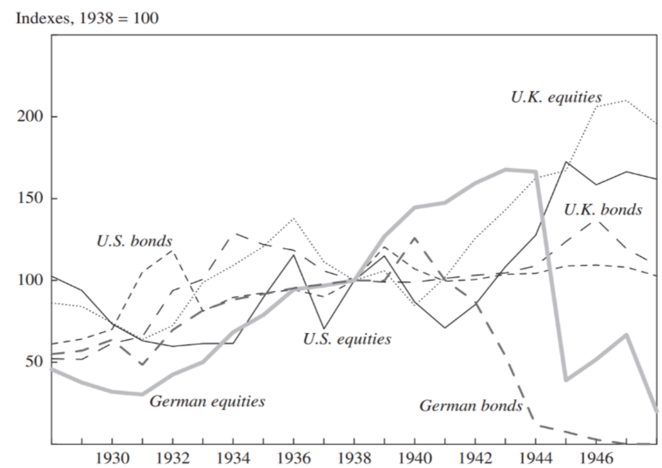
Aside from the millions who died in the war, over 12 million were killed in the Nazi death machine. At that time, the stock and bond markets underwent turmoil as well. As you can see below, markets were volatile throughout both the first and second world wars, but over time trended higher.

**Figure 3.** Inflation-Adjusted Total Returns for U.K., U.S., and German Securities before and after the First World War




Source: Global Financial Data.

**Figure 11.** Inflation-Adjusted Total Returns for U.K., U.S., and German Securities before and after the Second World War




Source: Global Financial Data.

One important lesson of history is that major wars can arise even when economic globalization is very far advanced and the leadership position of an English-speaking empire seems fairly secure. The second important lesson is that the longer the world goes without a major war, the harder one becomes to imagine (and, perhaps, the easier one becomes to start). When a crisis strikes complacent investors like we are seeing now, it causes much more disruption than when it strikes battle-scarred ones. For financial markets, unexpected events or black swans like COVID-19 are worse.

After the war, prosperity came to America and my parents met as teenagers, got married, and eventually made the huge move to the suburbs in the late 1950's. My father eventually settled on his career in financial services in the late 1960's.

His early career in the market was the 1970's and the great bear market, the Vietnam War Era, oil crises, Watergate. Many deem the bear market of the 1970's as the "forgotten bear market". Rapid-fire growth ended with a mild recession, accompanied by a relatively high inflation rate of about 6%. The bear market began just as Richard Nixon was elected president after a tumultuous year of assassinations and riots. The weak economy added to a tense national atmosphere dominated by the growing U.S. involvement in Vietnam. Over the last 50 years, 1970 joins 1987 and 2009 as the only years when the S&P 500 fell 25% from its highs and still finished positive on the year.[1]

Then we come to the great market crash of October 1987. The "Black Monday" stock market crash of October 19, 1987, saw U.S. markets fall more than 20% in a single day. It is thought that the cause of the crash was precipitated by computer program-driven trading models that followed a portfolio insurance strategy as well as investor panic. Sound familiar?! It took us just 16 trading days to enter this current bear market. The historical average is usually months!

I joined my father in 1991, figuring I would give this Wall Street thing a try.

Beginning in the summer of 1997, we had what many called a “mini-crash” where a number of Asian countries experienced a financial crisis that would wreak havoc on their currencies and the broader emerging markets in general. The MSCI Emerging Markets Index proceeded to get chopped in half over the next year or so, dropping 56% from 1997 to 1998.[1] U.S. markets brushed off the turmoil for the majority of this period with the S&P 500 up 21% while emerging markets fell. Then in August of 1998, the Russian government was forced to devalue their currency and default on their debt as their own problems came to light. Hedge fund Long-Term Capital Management blew up in the process and markets everywhere were negatively affected.

The losses were again quick and unforgiving for stock markets around the globe as you can see the damage done in just two short months:

- S&P 500 -15.4%
- Small Caps (S&P 600) -25.5%
- Mid-Caps (S&P 400) -21.8%
- Emerging Markets (MSCI EM) -26.7%
- Foreign Stocks (MSCI EAFE) -11.5%

The crazy thing is that stocks recovered relatively quickly following the dramatic fall. These were the total returns from September 1998 through March 2000:

- S&P 500 +59.8%
- Small Caps (S&P 600) +48.4%
- Mid-Caps (S&P 400) +81.2%
- Emerging Markets (MSCI EM) +113.9%
- Foreign Stocks (MSCI EAFE) +49.0%

This was the last leg higher before the technology bubble burst and the S&P 500 was eventually cut in half over the ensuing 2-3 years.

So, the Tech Bubble and crash of 2000, followed shortly thereafter by 9/11, and the horrific times we witnessed and lived through then. Many felt that event alone would cause a recession. It was months later that we realized the recession started in early 2001, not September, and the added stimulus after 9/11 helped pull us out of the recession that was already underway.

Fast forward a few more years and the crash and recession of 2008 – 2009. Markets were down over 50% peak to trough and the S&P ended down 37% in 2008. By the time the indexes made their lows in March of 2009, most stocks had already started moving ahead. And from the lows of 2009 we had an 11-year unpreceded bull market, brought on by unbelievable technological advances.

Could any of you imagine working from home on laptops that cost $1,000 with a cell phone that probably costs as much, and being able to have a video conference call making you feel like you’re sitting right there with the other people, on a free service? And oh, we can order food, a car and virtually anything and have it delivered to our door? We live in wonderful times and that does not mean we won’t have setbacks, either individually or as a country, but the one thing I know about America is we seem to come back stronger and more determined each time, and better for it.

We tell our kids that you learn more from failure than success, so shouldn’t we take the current times to learn and prepare for the next time?

Oh, and let’s not forget that over the last 20 years we have seen the following global epidemics/pandemics:

AIDS, SARS, Swine Flu, MERS, ZIKA, Ebola, the last five occurring in the last 18 years. And yet after each we learn, we prepare, we get a little better. Maybe it does not seem that way at the time, but we are clearly more prepared for

COVID-19 than we would have been without the prior six.

The mind plays funny tricks on us, called survivorship bias, where we only remember certain aspects of events and try to trick ourselves into believing it was not as bad and we reacted better than we thought. Economist Daniel Kahnamen and Amos Twersky spend their careers studying how we react to economic events, with the former winning the Noble Prize for his work.

Since 1929 there have been 14 Bear Markets suffered by the S&P 500 (drop of 20% or more,) the deepest being the 86% drop in 1929, the shallowest being the one in late 1990, and the longest being the drop of 1937 to 1942 of 60%. Each one seemed especially dark and foreboding but keeping your goals and your wits about you will serve you well, as after each one the market regrouped, the leadership changed, and the market made new highs.

My point in writing all this was as much to help me come to grips with the current state of affairs as it was to share with all of you that we have been through worse as nation and a world but yet we keep coming out stronger and more resilient.

Will the current pandemic cause wide-spread disruption? It already has. Will this push us into a recession? Yes, it probably will. But let's look at the other side, the positives.

Several large companies including retailers are looking to hire an estimated 500,000 people over the coming days and weeks to keep up with demand. Multiple large companies have either announced raises for hourly employees or one-time bonuses, paid sick leave, and other enhancements to their employees. Are they doing this solely because they are nice people? That's a possibility, but it is also a sound business decision. The CEO of one large company told all his 45,000 employees they will be paid for full 40-hour work weeks even if they work less than that. Was one reason he did this because it costs his company $20,000 to hire and train each new employee? Yes, I'm sure. But to any of his hourly employees, that doesn't matter; all that matters is they know that while they may have to worry about getting sick and caring for their family, at least they don't have to worry about their next paycheck.

What about all the people working remotely, like yours truly? The last few summers I have spent 4-5 weeks working remotely, many of my clients knew, some didn't. I was able to prove to myself that with technology today it's possible to be about 90% effective working remotely. Now I did have the benefit of the rest of our great team working in the office to help provide the excellent client service our clients have come to expect, and while it might be a bit tougher going forward than it was last summer, so far most of last week my team was remote while I came into the office, and it went off with few problems that we could not overcome.

We will be putting our tech capabilities to the test and figuring out how this will all work, but we will do it together, and we will remain committed to our clients and all that you entrust to us. We will help you keep the current environment in perspective, because that's what you expect from us.

**To discuss this commentary further, please contact us at 914-825-8630.**

**hightowerwestchester.com**

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