CORDA

TOGETHER WE'RE INVESTED

What Can You Control?

September 30, 2022

Do you have a "Type A" personality or know someone who does? Type A behavior is characterized by ambition, competitiveness, drive, focus, and control. One definition of a Type A person also suggests aggressive traits, a need for quantity versus quality and an unrealistic sense of urgency. Apparently, it is commonly associated with risk of coronary disease and other stress-related ailments. We might argue some Type A characteristics are quite beneficial, until they become excessive and all consuming, perhaps causing harm to yourself and others - then it might be best to slow it down a bit.

Type A behavior can also be detrimental to your investment results. We recall a study by the University of California at Davis where they found women had better investment returns than did men. They tracked five thousand individual brokerage accounts and found that female investors did about 1.5% per year better than males. They concluded that males were predominantly over-confident and their number of buy and sell transactions far exceeded their female counterparts. Does this sound plausible?! It seemed that females were more thoughtful, less inclined to trade, and more willing to hold their positions far longer than males did. This probably doesn't shock many of you.

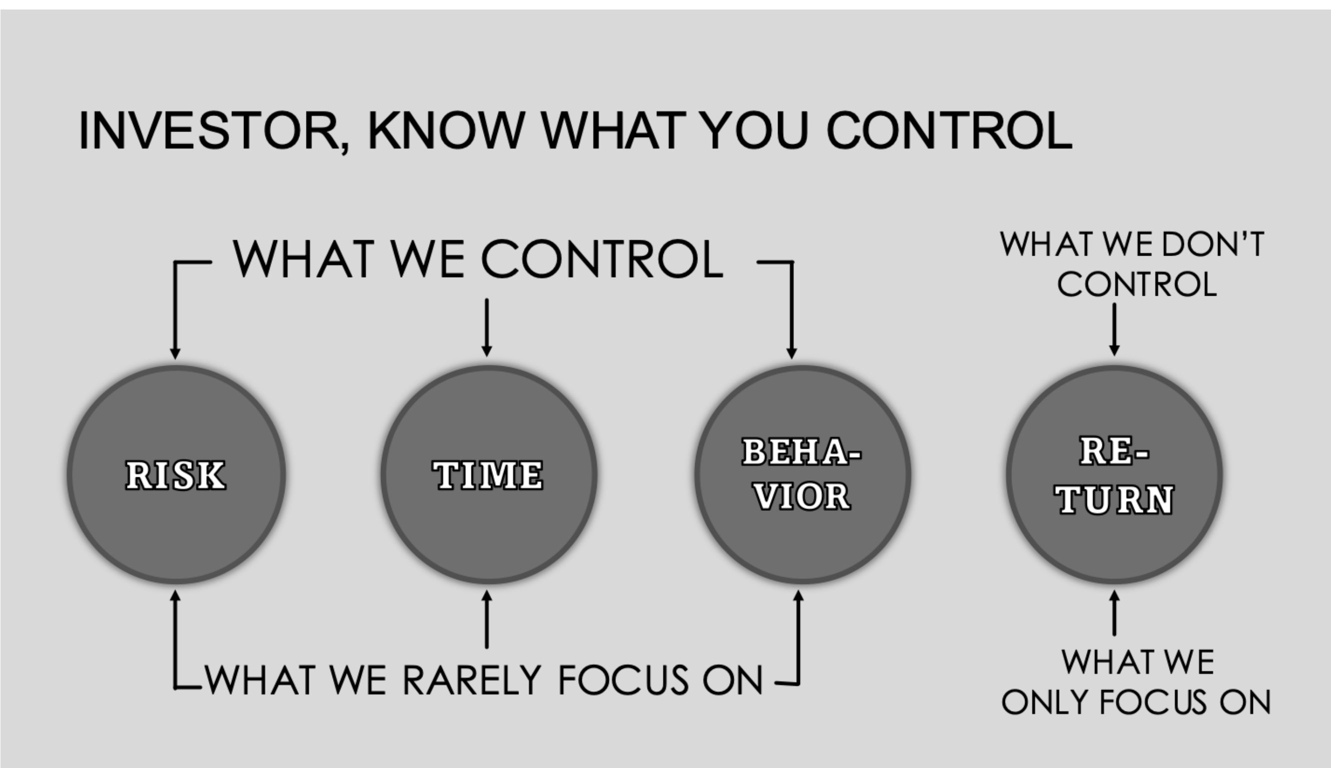
The reason we are going down this path is because we need to prepare ourselves for what's ahead in the next 6-12 months. A good word to describe this year's market would be – squirrely. We've referenced this word quite often around the water cooler this year. With so much turbulence and the market ping ponging daily, it hasn't been a smooth ride thus far in 2022. Frankly, going back to Q4 of 2018 when we had a 19.9% market correction, counting that and the spring of '20's pandemic meltdown and now here in '22, we've had more than our fair share of bear markets that might just tip the balance to a future string of good bull runs. We have had many client conversations of late where we are hearing a similar chorus of questions that we could summarize in 3 distinct ways: 1) how will you manage the portfolio in light of Federal Reserve's hawkish tone, 2) how are we going to invest if we are in a recession or with a recession looming on the horizon, and 3) what do you think of interest rates and/or the inverted yield curve? As you know, these questions aren't necessarily new. The market has been digesting and seeking to discount higher rates and recession possibilities all year long. Another question creeping in of course is one about the November elections and would CORDA manage differently based on potential outcomes?

While there is a natural ebb and flow to the economy, politics, central bank maneuvers, social changes, exogenous events and such, the lingering questions seem to never fade. We've just added new concerns over the past two years with flash points such as COVID-19, China, and Russia's advancement on Ukraine and its natural gas dealings with Europe. There will be new worries, threats, and opportunities in the years ahead that we'll have to adjust to as well, it's just never easy going through them in real time. As human beings - and investors - we'll have to gut things out like we always do!

For many of us and especially how we live our lives day to day, whether Type A or not, we seek to exert some sort of control over things. You rightfully survey the current situation, seek to address all the opportunities (and risks), and thoroughly assess the many variables and outcomes to develop a plan. Seems logical, right? With so much swirling around you, you carefully manage your life and control outcomes as best you can. It runs deep in your DNA; it is a survival instinct.

That said, seeking to control external factors that are wildly out of your control would be silly, right? Of course, a good therapist would agree to such a statement. So maybe you know this and have certainly grown to respect it. We all have conversations with ourselves, yes? The self-talk narrative sounds like this: There are many things I can't control, but today I will do things that I can. For example, I can wake 30 minutes early and exercise or take an additional long walk; I will eat an extra serving of fruit and vegetables; I will consume less alcohol; I can read more, spend less time on electronics or television, maybe even call a loved one or old friend I haven't spoken to in a long time and provide encouragement and words of affirmation versus admonishment and negativity – things directly in my control that can positively influence my life and those around me. These are small and simple steps where we have direct control of the outcomes. Do they sound familiar? What would you add?

Here's a nifty chart that you have seen us reference from time to time regarding how best to "control" things that can positively influence our investment results.



So, this is a long-winded way of preparing you for the continued barrage of recession and interest rate coverage that has yet to unfold, plus the November 8th election that happens to come exactly a week after the November 1-2nd Federal Open Market Committee (FOMC) meeting that could result in a possible 50 basis point increase to the Fed Funds rate. As you know, we will continue to use a “bottom up” approach to our analysis and seek to determine the health of our businesses and how they might fare in the years ahead. Seeking to game an election outcome would not be a wise decision. We have witnessed countless attempts that seem to backfire on investors, hoping for one outcome and assuming a market response that sometimes defies all odds and does/doesn’t happen according to your wishes. If you don’t expect there to be drama, then you are missing what the news cycle and elections are all about.

Negativity and skepticism are high right now - how do we know this? Virtually no questions from our clients about how to get more fully invested. The interest rate and recession questions stack the deck enormously in the bearish mentality camp. What isn’t normally considered is the short life spans of recessions and bear markets. Note from last quarter’s letter we detailed how bear markets on average last about 11 months and their magnitude are around -30%.

We Have Another Bear Market

S&P 500 Index Bear (And Near Bear) Markets (1950 - Current)

Start Date	End Date	S&P 500 Change	Months
8/2/1956	10/22/1957	(21.6%)	14.7
12/12/1961	6/26/1962	(28.0%)	6.4
2/9/1966	10/7/1966	(22.2%)	7.9
11/29/1968	5/26/1970	(36.1%)	17.9
1/11/1973	10/3/1974	(48.2%)	20.7
9/21/1976	3/6/1978	(19.4%)	17.5
11/28/1980	8/12/1982	(27.1%)	20.4
8/25/1987	12/4/1987	(33.5%)	3.3
7/16/1990	10/11/1990	(19.9%)	2.9
7/17/1998	8/31/1998	(19.3%)	1.5
3/24/2000	10/9/2002	(49.1%)	30.5
10/9/2007	3/9/2009	(56.8%)	17.0
4/29/2011	10/3/2011	(19.4%)	5.2
9/20/2018	12/24/2018	(19.8%)	3.1
2/19/2020	3/23/2020	(33.9%)	1.1
1/3/2022	6/13/2022	(21.8%)	5.4
Average		(29.8%)	11.0
Median		(24.6%)	7.2

Source: LPL Research, FactSet 06/13/2022
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.
[redacted]e S&P 500 stock index was first launched in 1957.
Performance back to 1950 incorporates the performance of predecessor index, the S&P 90.

We believe there is a light at the end of the tunnel. Considering the Nasdaq hit a high last November and the S&P 500 the first week of 2022, we are anywhere from 9-11 months along the path of a tough bear market. What's important now is to plan for the market hitting bottom well before the recession is over. Recall, markets and share prices move ahead of fact and the bottoming process will occur with plenty of recession chatter still in the air. The key here is that the initial stock market moves off the bottom could be significant, even in the face of an adverse economic backdrop.

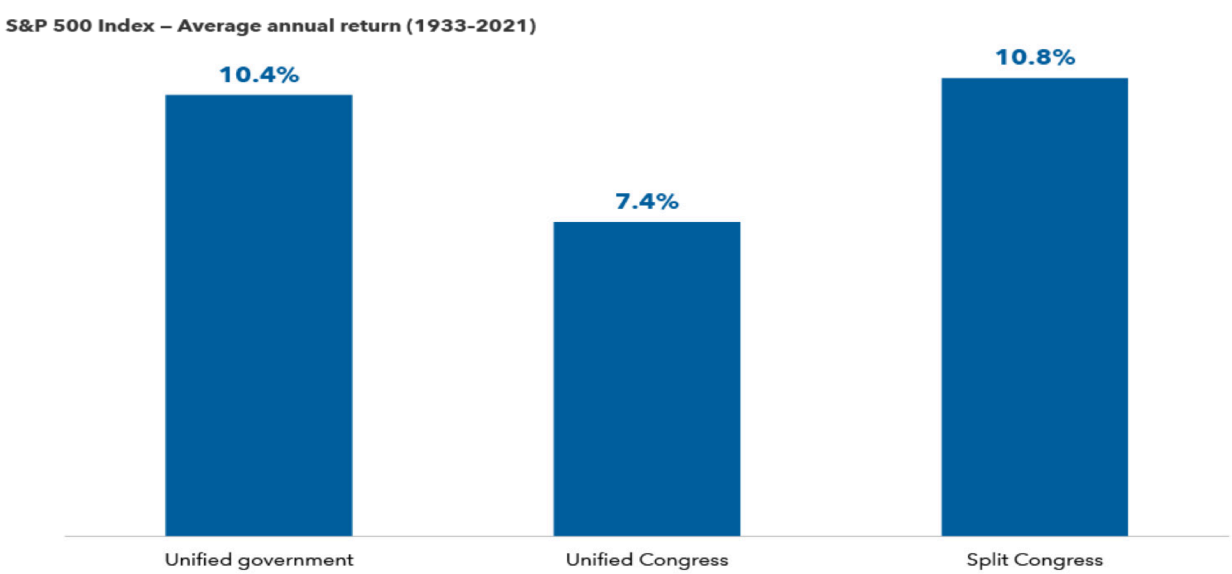
Equity market bottom	GDP bottom	Days in between	Equity market return by the time that GDP bottomed	Equity market return by the time that GDP started rising again
3/31/2020	6/30/2020	91	20%	30%
2/28/2009	6/30/2009	122	25%	44%
10/31/1990	3/31/1991	151	23%	22%
7/31/1982	9/30/1982	61	12%	31%
9/30/1974	3/31/1975	182	31%	50%
12/31/1957	3/31/1958	90	5%	13%

Source: Bloomberg, JPMAM. 2022.

Note the number of days between the market bottom and the time until GDP bottomed measured against the magnitude of the bounce that takes place before a recession is "officially" declared over. The key is if you plan to wait until the "all-clear" signal is produced, you may miss the large returns that are achievable during the early stage of a recovery. Such acute timing is difficult if not impossible to carry off.

While we pointed out that bear markets last an average of 11 months with an average decline of 30%, the bull markets that follow typically last 4.4 years with an average cumulative return of over 155%.

As for elections, they have historically had little impact on long-term results. Certainly, you can desire and hope your candidate gets elected to office, but if you find you're backing the wrong candidate or party, there's still much to cheer for as the equity markets do well in almost all scenarios. See below, and make sure to note how the split category has the highest rate of overall return.



Source: Capital Group, Strategas

Valuations are Attractive – Opportunity in Lower Prices

Long-term investors should pay close attention to the current value of asset prices. The following is a recent excerpt from David Kelley, Chief Strategist at J.P. Morgan Asset Management, where he wrote a piece called "The Scales of Fundamentals and Price:"

- At the end of last year, the 10-year Treasury bond was yielding just 1.52%, offering investors neither income nor any real protection in the event of a stock market selloff. Today, with a yield of 3.68%, it offers both. Moreover, across fixed income markets investors can find much better opportunities with TIP yields turning positive and yields more than doubling since the start of the year across investment grade corporate bonds, high-yield bonds, municipals, and mortgage-backed securities.
- At the end of last year, the forward P/E ratio on the S&P 500 was 20.9 times, 24% above its 25-year average of 16.9 times. As of Friday, it was at 15.6 times, 8% below that long-term average. Moreover, within equities, non-mega cap stocks and value stocks are at a steeper discount to their long-term averages.
- At the end of last year, the forward P/E ratio on the MSCI-ACWI ex U.S. was 14.3 times. Today it is 10.9 times. This valuation is not only low in absolute terms, but it is also very low relative to U.S. equities. It should also be seen in the context of a dollar exchange rate which has risen by an extraordinary 17.8% so far this year to its highest level in real terms since the mid-1980s.

For many investors, there is, of course, plenty of pain embedded in today's cheaper valuations. However, bull markets always start in the basement of investor despair.

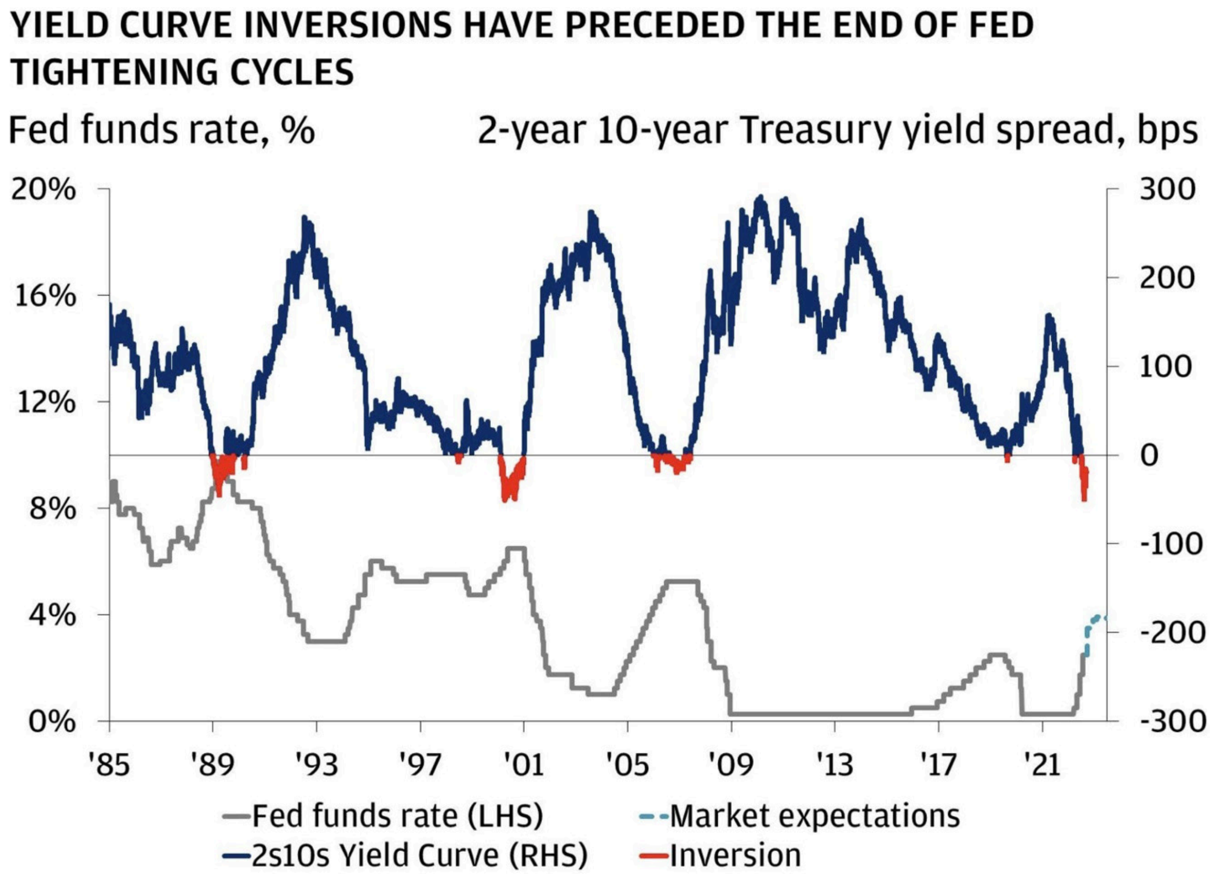
There are plenty of things that could go wrong in the next year. However, there are also plenty of things that could go right.

If, over the next year, China transitions to a post-COVID economy, some ceasefire or settlement is reached in Ukraine and the Fed pivots to a less hawkish stance, financial markets could be expected to react positively. Bonds bought today could benefit from lower Treasury rates and tighter credit spreads. U.S. equities could rebound as uncertainty diminished and the economy transitioned to a slow-growth, low-inflation environment. And investments in international equities could benefit from both better local currency returns and a retreat in the dollar from its current super-high levels.

Some of these events could, of course, take longer to play out and the global economy will undoubtedly face new challenges. ***However, perhaps the most important thing for investors to consider at the start of the fourth quarter is that, while at the start of the year most major asset classes were priced for perfection, today many have been discounted for disaster.***

Finally, the yield curve is telling us a few things. For one, we might be nearing the end of the Fed tightening schedule. All indications are that the economy is braking hard, and one must wonder if the Fed will now go too far and cause a significant slowdown as opposed to a light one. Since they waited too long to tighten, why should we assume they'll get it right this time and not be overly restrictive?!

The following chart compares the 2-year Treasury yield to the 10-year Treasury yield and when it goes negative usually we are at some sort of inflection point with the FOMC beginning an easing period in the Fed Funds rate. It's interesting to note how some influential market prognosticators such as Jeremy Siegel and Jeffrey Gundlach are now voicing concerns the Fed has gone too far and are advocates for one or two small increases and then possibly easing off the pedal.



One last thought when it comes to control. There is one distinct advantage we all have when it comes to interfacing with the market every day. Recall how historically over 40% of the overall stock market return comes by way of dividends? If forced to make a prediction, then we'd answer with a dividend forecast. If a business is paying or has paid a dividend consistently over time, it would be highly unusual for it to decrease or suspend the dividend in the next quarter or two. Out of 30 or 35 businesses that we might own, perhaps one or two might reduce their dividends due to some fundamental situation, but we are plainly counting on the vast majority of our holdings to continue to pay and increase their dividends in the coming years. Unfortunately, we can't make any guarantees, but it's as close to a sure thing that we can find in the capital markets. Outside of that, we can control our thoughts and actions each day, but most everything else is out of our control.

So, think positively about the future and expect a whole bunch of drama in the coming weeks and months. You won't be able to avoid it, but you can adjust your temperament as to how you approach it, and not get sidetracked because of it. Stick to your strategy and don't lose control of your emotions. An opportunistic time is fast approaching, and we want you to be ready to capitalize.

Here's to a calm and cool demeanor as we enter Q4 and an early favorable view towards 2023.

Best wishes from the CORDA Team.

P.S. – from the mental archives comes an all-time favorite courtesy of Rudyard Kipling that paraphrases ever so brilliantly what we are channeling here, so a verse or two or all four from ***If*** —

If you can keep your head when all about you
Are losing theirs and blaming it on you;
If you can trust yourself when all men doubt you,
But make allowance for their doubting too;
If you can wait and not be tired by waiting,
Or, being lied about, don't deal in lies,
Or, being hated, don't give way to hating,
And yet don't look too good, nor talk too wise;

If you can dream—and not make dreams your master;
If you can think—and not make thoughts your aim;
If you can meet with triumph and disaster
And treat those two impostors just the same;
If you can bear to hear the truth you've spoken
Twisted by knaves to make a trap for fools,
Or watch the things you gave your life to broken,

And stoop and build 'em up with wornout tools;
If you can make one heap of all your winnings
And risk it on one turn of pitch-and-toss,
And lose, and start again at your beginnings
And never breathe a word about your loss;
If you can force your heart and nerve and sinew
To serve your turn long after they are gone,
And so hold on when there is nothing in you
Except the Will which says to them: "Hold on";

If you can talk with crowds and keep your virtue,
Or walk with kings—nor lose the common touch;
If neither foes nor loving friends can hurt you;
If all men count with you, but none too much;
If you can fill the unforgiving minute
With sixty seconds' worth of distance run—
Yours is the Earth and everything that's in it,
And—which is more—you'll be a Man, my son!