

We understand not wanting to open your statements when the market is down...

but we don't want you to stop reading our blogs because they are too dense. For our *visual learners*, we offer our thoughts on the current market environment in 10 charts! For our *auditory learners*, we provide our inaugural podcast.

Click on [this link](#) to hear the 30-minute podcast corresponding to this blog.

For those who prefer TLDRs, we provide a bullet point summary at the end of the blog.



1. Bond Trends Can Last for Very Long Time Periods

For charts showing bond yields (i.e. bond interest rates), it's important to keep in mind that **bond prices move in the opposite direction of yields**. We show this relationship graphically in the chart below where you can also see the long-term trends in the bond market's direction. Investors have made money in bonds fairly consistently for the last 40 years, shown by the rising orange line.

Relationship Between Bond Prices and Yields

When Yields Increase, Bond Prices Decrease

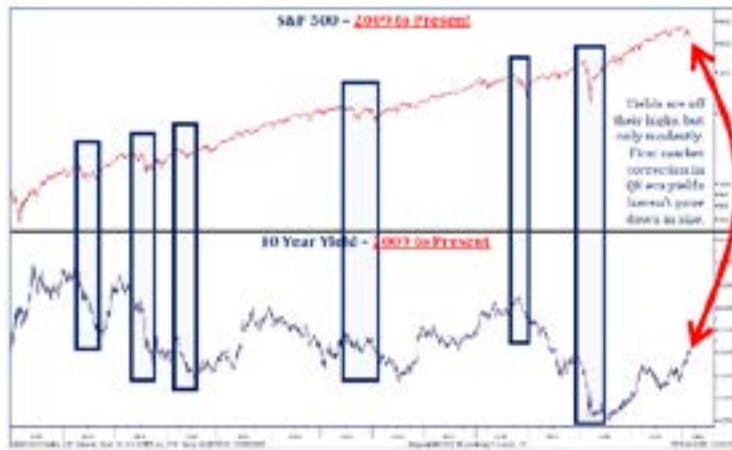


2. Bonds Offered Protection When the Federal Reserve was Easing

After 2008, bond yields consistently went down when equity prices fell, offsetting equity losses. Remember, when bond yields go down, bond prices rise.

Since the end of 2020, inflation concerns caused a change in bond trends. As demonstrated by the chart below, bond yields are now *rising* while stock prices are *falling*, removing their value as a hedge. When bond yields rise, their prices fall.

In The QE Years, Bonds Were A Hedge for Stocks... But Not This Time



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3. Historically, Bonds Haven't Protected You in Inflationary Times

The chart below shows bonds and stocks going down at the same time during the 1965 to 1982 inflationary period. To understand the magnitude of the possible moves in today's market, both bonds and stocks had lost more than 9% year-to-date as of the first week in May.

In the Inflation Years, Stocks and Bonds Declined Together



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4. Commodities Offer Protection Against Stocks in High Inflationary Periods

Historically, investing in commodities¹ has been one of the most straightforward ways to directly benefit from rising inflation. Over the last 50 years, in periods where inflation exceeded 2.5%, commodities generated the highest returns, outperforming stocks by approximately 30 basis points with lower volatility. We use stocks of commodity companies to hedge against inflation. Year-to-date, stocks of commodity companies have gone up while the stock and bond indices have gone down.

Asset Class Performance during Inflation Regimes



Sources: WisdomTree, Bloomberg, Morningstar, 1/30/1970-12/31/2020. Inflation proxied by IA SBBI U.S. Inflation Index, U.S. Large Caps proxied by IA SBBI U.S. Large Stock TR USD Index, Bonds proxied by IA SBBI U.S. LT Government TR USD Index, Commodities proxied by S&P GSCI Index (SPGSCI). Past performance is not indicative of future results. You cannot invest directly in an index.

5. In High and Rising Inflationary Environments, Commodities Perform Better Than Bonds

When inflation is > 2.5% and rising, commodities (demonstrated by the BCOM and SPGSCI indices) outperformed bonds by 2 to 3%.

Inflation > 2.5% and Rising		
	Correlation vs. S&P Index	Average Annualized Return
U.S Long-Term Govt Bonds	0.06	1.30%
SPGSCI Index	0.10	3.61%
BCOM Index	0.07	4.12%

Inflation <= 2.5%		
	Correlation vs. S&P Index	Average Annualized Return
U.S Long-Term Govt Bonds	0.09	4.27%
SPGSCI Index	0.15	-1.51%
BCOM Index	0.12	-1.79%

Sources: WisdomTree, Bloomberg, 1/30/1970-12/31/2020. U.S Long-Term Govt Bond proxied by IA SBBI U.S. LT Government TR USD Index. Past performance is not indication of future results. You cannot invest directly in an index.

¹ Why We're Bullish on Commodities in 2021 by Jianing Wu, Senior Analyst, WisdomTree 3/15/21

6. Commodities Could Have a Long Runway

Although commodities have rallied about 50% versus the S&P 500 during the current cycle, history shows there is likely more to go. In the 1970s, the commodity index relative to the S&P 500 went up 839%. From 2002 to 2007/08 it was up 202%. In addition to energy, we like other materials including copper, uranium and agricultural commodities and continue to add equity exposure to these sectors.

Because commodity companies have dramatically underperformed in the last 10 years, they are very small percentages of equity market indices. To have a meaningful impact on a portfolio, we believe that investors should add exposure directly to these sectors through individual stocks and ETFs rather than investing in the S&P Index.

Again. Certainly Overbought Today... But Structurally Not So Much

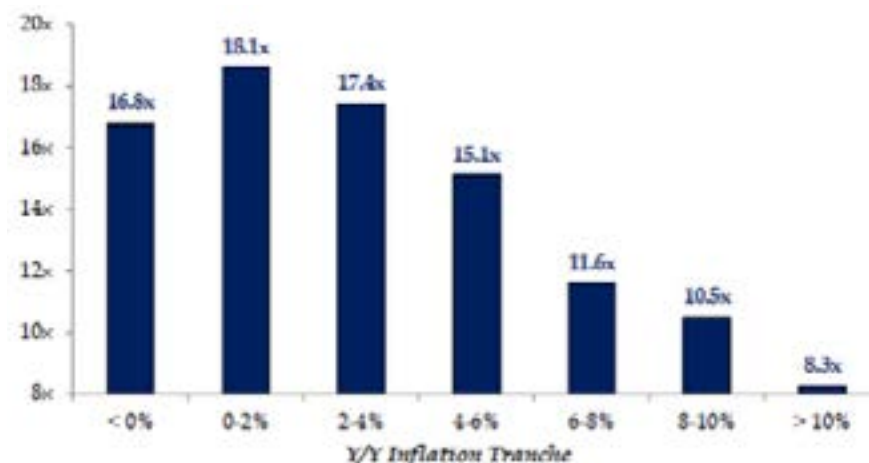


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7. Price Earnings Multiples are Lower When Inflation is Higher

P/E multiples represent the stock price an investor is willing to pay for a given level of company earnings.

S&P 500 Average Trailing P/E's by Inflation Tranche



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8. The Year-to-Date Decline in the Market is Fully Attributable to Multiple Compression

Earnings for the S&P 500 have held up relatively well. What has changed is what people are willing to pay for those earnings. When interest rates are higher, investors are willing to pay less.

Cumulative % Change in S&P 500 Price, EPS, & P/E



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Don't fight the Fed...

In response to the Covid crisis, the Federal Reserve put money into the financial system by buying bonds and lowering interest rates. A rising tide lifts all boats, and stocks went up across the board, which historically occurs when the Fed eases.

Times have changed. In response to persistent inflation, the Fed is now taking money out of the financial system by raising interest rates and planning to sell bonds. When the tide goes out, we see who is swimming naked. In this case, stocks of unprofitable high growth companies have plummeted.

The current environment is challenging, but it will not last forever. In our closing charts, we remind investors of the long-term trends in equities.

9. Over the Last 100 years, the Market has Gone up 52% to 100% of the Time for a Wide Variety of Time Periods

On any given day, the odds of the S&P 500's price being higher are only slightly over 50/50 (52.43% to be exact). If you go out a year, they rise to 69.33%. However, for any **5-year period** over the last 100 years, the odds of a positive S&P 500 total return have been 89.1%.

Positive Returns by Timeframe

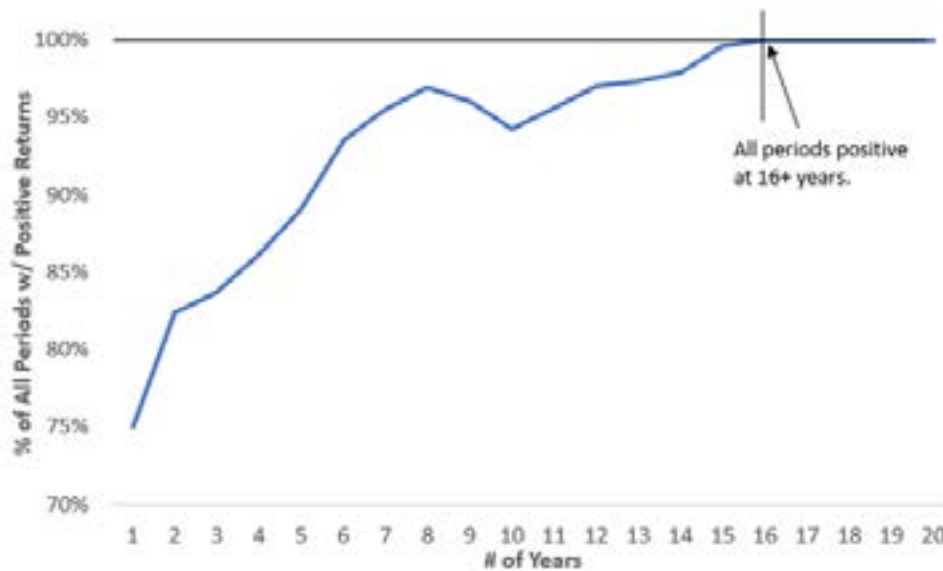
S&P 500 Price		S&P 500 Total Return	
Time Frame	% Positive	Time Frame	% Positive
1 Day	52.43%	1 Month	62.78%
1 Week	56.17%	3 Months	68.24%
1 Month	60.07%	6 Months	71.11%
3 Months	63.64%	1 Year	75.09%
6 Months	66.69%	2 Years	82.43%
1 Year	69.33%	3 Years	83.73%
2 Years	76.01%	5 Years	89.10%
3 Years	77.91%	10 Years	94.22%
5 Years	79.30%	20 Years	100.00%
10 Years	88.42%	30 Years	100.00%
20 Years	96.30%		
30 Years	100.00%		

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10. The Risk of a Negative Outcome in Stocks Decreases as the Time Frame Increases

The risk of a negative outcome declines as the timeframe increases, demonstrating how a volatile asset like the S&P 500 can produce positive outcomes over time. This is why investment advisors recommend that people with long time horizons hold a higher percentage of equities.

S&P 500 Total Return: % of Time Positive by # of Years Invested



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TL;DR

1. Bond prices and bond yields move in opposite directions.
2. When the Federal Reserve was easing, bonds hedged stock market declines. In inflationary times, bonds have not hedged stock market declines.
3. Stocks of commodity companies can be used as a hedge against inflation.

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