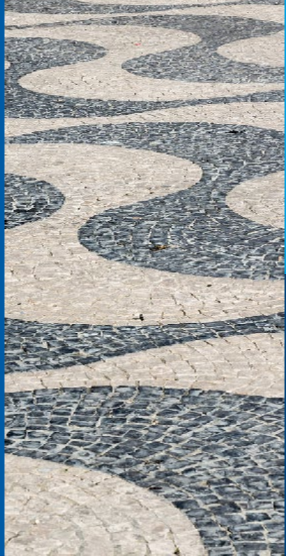

Morgan Stanley
INVESTMENT MANAGEMENT

Equity Market Commentary

SLIMMON'S TAKE | APPLIED EQUITY TEAM | April 2025

The following views and perspectives are formed by the work of the Applied Equity Team in managing assets for investors.

AUTHOR

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Without a doubt, the number 1 question Leslie and I receive is, "*what's the best way to deploy cash into the market?*"

So, is this tariff induced selloff an opportunity to be bold and add cash to equities or is it better to hunker down and wait for a better entry point?

SLIMMON'S TAKE normally serves to communicate our market views and investment positioning.

The purpose of this one, however, is to answer that first question and to assist in guiding investment timing during stock market corrections, as we are experiencing now.

1 Let me begin by saying, I have no idea how these Trump administration tariffs will be resolved.

Nor does anyone else, in my opinion, unless they are a regular in the Oval Office.

Just guesses.

2 What I do know is the stock market is down significantly due to this uncertainty.

And if the time frame is looking out **one year**, corrections have historically provided **above average equity returns.**

3 The Applied Equity Team analyzed every drawdown of the S&P 500 greater than -15% since 1950.

We believe **a more clinical, non-emotional approach** to investing during market declines enhances investors' chances of success.

The index performance is provided for illustrative purposes only and is not meant to depict the performance of a specific investment. **Past performance is no guarantee of future results.**

4 The "sticky note" on my desk currently has three key numbers on it:

5,222

4,915

4,608

Those are each of the S&P 500 levels when the peak-to-closing price is down -15%, -20% and -25%, respectively.[1]

5 Last Friday, April 4th, the S&P 500 close was below 5,222.

Historically, we believe **-15% declines** *can* be good entry points, *but not necessarily*:

A. There have been 18 declines since 1950 of -15% or more.[2]

B. The average one-year return after the correction is not much better than the average return for any year.

C. That's because about half of those 18 times led to recessions.

In the recession years, the one-year return was barely positive on average.

D. Yet if the economy avoids a recession, like it did most recently in 1998, 2011 and 2018, the odds of a good outcome are high…again historically speaking.

My conclusion? Determining whether we will have a recession is simply a guess, a coin flip. But I would not let this -15% opportunity pass.

However, I would only allocate a portion of whatever cash was on the sidelines given the economic outcome has the key determinant of the resultant return.

6 One-year returns after the correction become more attractive when the market **is down over -20%**, *regardless of whether there was a recession or not. Almost double the normal one-year average.*[3]

A. There have been 12 declines of over -20% since 1950, and 9 of them occurred with recessions.

B. But even if there was a recession, the returns one-year out were still attractive.

The exceptions were the 1974 oil crisis and the 2008 Great Financial Crisis. Two very deep recessions.

C. The unfortunate reality of the -20% declines is that most of them morph into -25% or worse. But not all.

My conclusion? Consider increasing the allocation percentage into equities if in fact the S&P closes -20% or worse. But I would still reserve some cash for the next leg lower.

7 On October 6, 2022, Leslie distributed a chart to our readers that showed the one-year return after the correction for stocks following a -25% peak-to-trough decline.

A. As of September 30th, 2022, the S&P 500 had **breached -25%**.

B. There had been eight previous instances of the same, and the one-year return was better than *double the normal average.*[4]

C. What's amazing is the actual one-year return off that September 2022 low *was exactly in line. A double*.

My conclusion? This would be my final allocation of cash into equities. My confidence of positive returns is highest at this level.

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[1] Versus the 2/19/2025 S&P 500 closing high of 6,144. Bloomberg.

[2] Measuring from the day the S&P 500 closed down -15% for the first time out the next 12 months. Total return. Bloomberg.

[3] Bloomberg.

[4] Bloomberg.

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Let me repeat what I said initially. I have no idea how this tariff thing will be resolved.

This means I am not trying to call the bottom.

It can get a whole lot more painful than just a -25% decline.

Yet unless this is a repeat of 1974 or the Global Financial Crisis, investors could be quite pleased a year from now with this non-emotional approach.

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We know that the more the market drops, the better the next one-year returns have been historically.

Yet what's perverse but consistent with human behavior is that, in my experience, the willingness to step in fades.

In essence, when the market has stopped dropping somewhere between -15% and -20%, the reason is because the recession scare turns out to be just that…a scare, not a reality.

However, as a recession looms more likely, once the market passes the -20% down level, investors halt their "buying the dip," in my experience.

Even though the one-year return on average after the correction gets even better, regardless of whether there is a recession or not.

Therefore, it does not surprise me that the current data suggests the level of retail buying has been pretty good during this decline….so far.[5]

10

Hence the importance of my sticky note.

It **forces** me to do something I increasingly will not want to do.

(Maybe I should put another sticky note *under* my desk, which is where I likely will be if the S&P is down -25% or more.)

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Now, all I am doing here is playing the historical averages and assuming they will likely work again.

That might be a faulty assumption.

And I am sure there are readers saying, "*Andrew is an idiot for investing, doesn't he understand this is much worse with far more uncertainty*?" (I am reading a lot about Mr. Smoot and Mr. Hawley.)

But *when is there ever certainty?*

As if Mr. Market is going to call you the day before "the certainty" starts and tell you to get in the market that day.

I have been in this business a long time and every decline has felt far worse than the previous one. Always.

We only learn afterwards which declines were indeed the really bad ones.

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All corrections are gut wrenching. You want to curl up and just wait for them to pass.

But I believe the markets will anticipate the end long before it's obvious.

Therefore, in our opinion, a clinical approach to investing into declines enhances the chances of investment success.

Please be sure to listen to our upcoming 1Q 2025 Portfolio Review & Equity Market Update at 1 pm ET, Wednesday, April 16.

Andrew

[5] Birinyi Associates, 4/6/2025.

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