

OCTOBER 31, 2008 — BRIEFING PAPER

GAINING PERSPECTIVE ON BEAR MARKETS

SIGNIFICANT MARKET DOWNTURNS AND THE ACCOMPANYING LOSS OF PORTFOLIO VALUE CAN DISRUPT AN INVESTOR'S CAREFULLY CONSIDERED INVESTMENT PLANS.

Given the recent market declines and the accompanying discussions in the media, many investors are asking:

- What *is* a bear market?
- How long do they last?
- How severe can a bear market be?
- How long does it take to return to pre-bear market levels?
- What can be learned from previous bear markets?

This paper provides information related to these questions to help investors and their financial advisors gain a long-term perspective on bear markets.

WHAT IS A BEAR MARKET?

A bear market can be defined in a number of ways. Unlike recessions whose beginning and end is identified by an official body, there is no official definition of a bear market. Two frequently used definitions are:

*A downturn of 20% or more in multiple broad market indexes, such as the Dow Jones Industrial Average or Standard & Poor's 500 Index over at least a two-month period.*¹

*A peak-to-trough decline of at least 20% of the S&P 500 Index.*²

The discussion in this paper will use the “peak-to-trough” definition and consider bear markets since World War II.

HOW LONG DO THEY LAST?

Including the current bear market, there have been eleven bear markets since World War II.

Chart 1: Post World War II Bear Markets

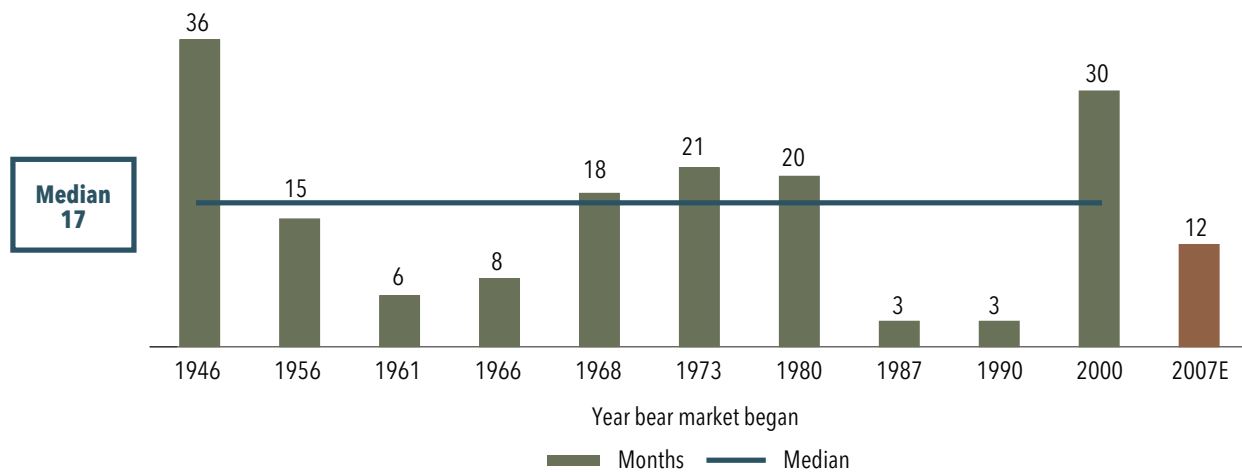
Start (Peak)	End (Trough)
May 29, 1946	June 13, 1949
August 2, 1956	October 22, 1957
December 12, 1961	June 26, 1962
February 9, 1966	October 7, 1966
November 29, 1968	May 26, 1970
January 11, 1973	October 3, 1974
November 28, 1980	August 12, 1982
August 25, 1987	December 4, 1987
July 16, 1990	October 11, 1990
March 27, 2000	October 9, 2002
October 9, 2007	Undetermined

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While the median (the midpoint of the range) length of a bear market is 17 months, as Chart 2 below shows, bear markets vary considerably in their length:

- The longest bear market began on May 29, 1946 and ended on June 13, 1949 – a duration of 36 months.
- There were two short bear markets of three months each: August 25, 1987 through December 4, 1987 and July 16, 1990 through October 11, 1990.
- As of October 31, 2008, the most recent bear market began on October 9, 2007 and reached its lowest point (trough to date) on October 27, 2008. As of this date, the length of this most recent bear market is 12 months, less than the median level of 17 months.

Chart 2: Length of Bear Markets in Months



E = Estimate as of October 31, 2008.

Data source: Standard and Poor's Corporation. Past performance is no guarantee of future results. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. Please see endnotes for a complete description of this index.

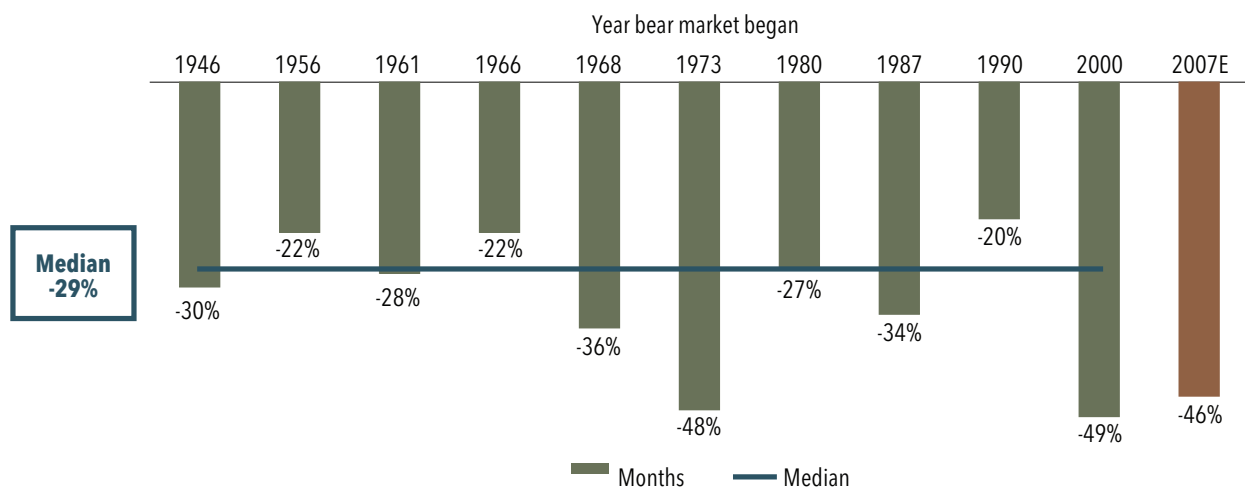
HOW SEVERE CAN A BEAR MARKET BE?

Just as bear markets vary in length, they also vary in how severe (as measured by return) they are. The average return of the bear markets, as measured by the S&P 500, shown in Chart 3 is -32% with a median return of -29%.

As Chart 3 shows:

- The largest decline of the S&P 500, 49%, was from March 27, 2000 through October 9, 2002, an average *monthly* decline of 1.6%.
- The smallest decline of 20% corresponds to one of the shortest periods of decline; from July 16, 1990 through October 11, 1990 with an average *monthly* decline of 6.6%.
- As of October 31, 2008, the most recent bear market experienced the third largest decline of all bear markets since World War II, a decline in the S&P 500 of 45.8%, an average *monthly* decline of 3.8%.

Chart 3: Severity of Bear Markets



E = Estimate as of October 31, 2008.

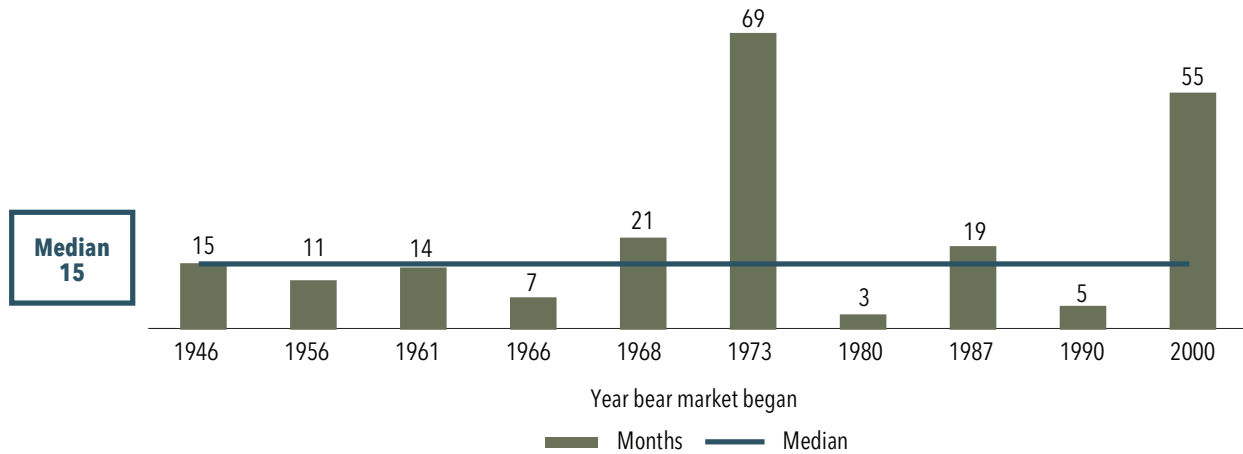
Data source: Standard and Poor's Corporation. Returns represent price returns of the S&P 500 from each peak to trough period. Past performance is no guarantee of future results. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. Please see endnotes for a complete description of this index.

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HOW LONG DOES IT TAKE TO RETURN TO PRE-BEAR MARKET LEVELS?

Chart 4 illustrates the number of months it took for the S&P 500 to regain its price level before the bear market began (the recovery period). Recall that for this discussion, the bear market is defined as the period from the peak of the S&P 500 to the trough, or the low point. The recovery period is the period between the trough, or low point, and the point at which it returns to its previous peak.

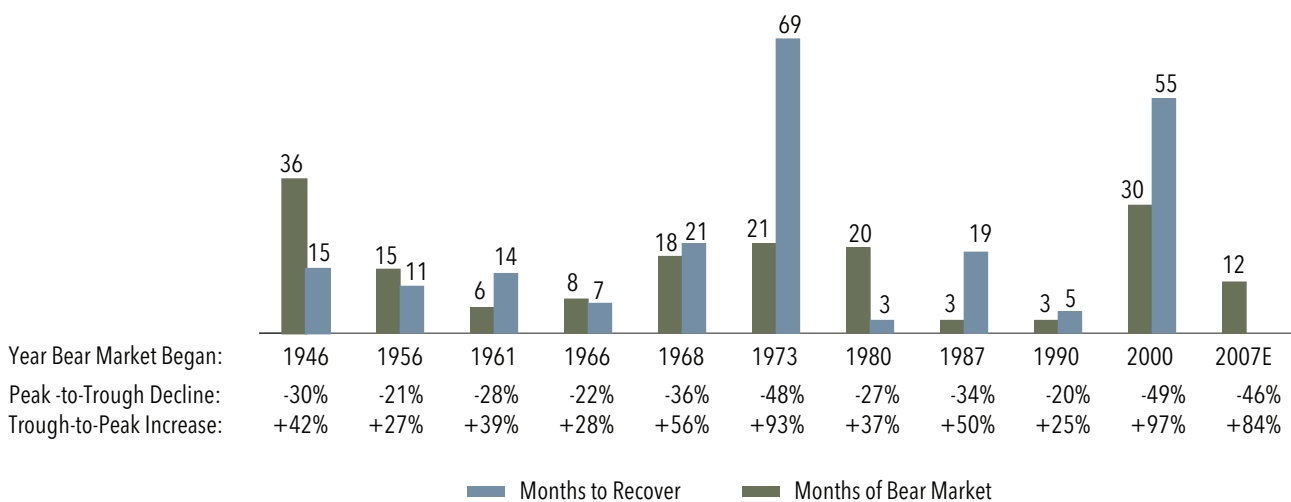
Chart 4: Months to Recover



Data source: Standard and Poor's Corporation. Past performance is no guarantee of future results. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. Please see endnotes for a complete description of this index.

Chart 5 illustrates the percentage return required during the recovery period, shown as the "Trough to Peak Increase," to get back to the previous peak level. Recovery periods vary for bear markets. Since World War II, six recovery periods were longer than the bear market, four were shorter.

Chart 5: Return Required to Get Back to Peak

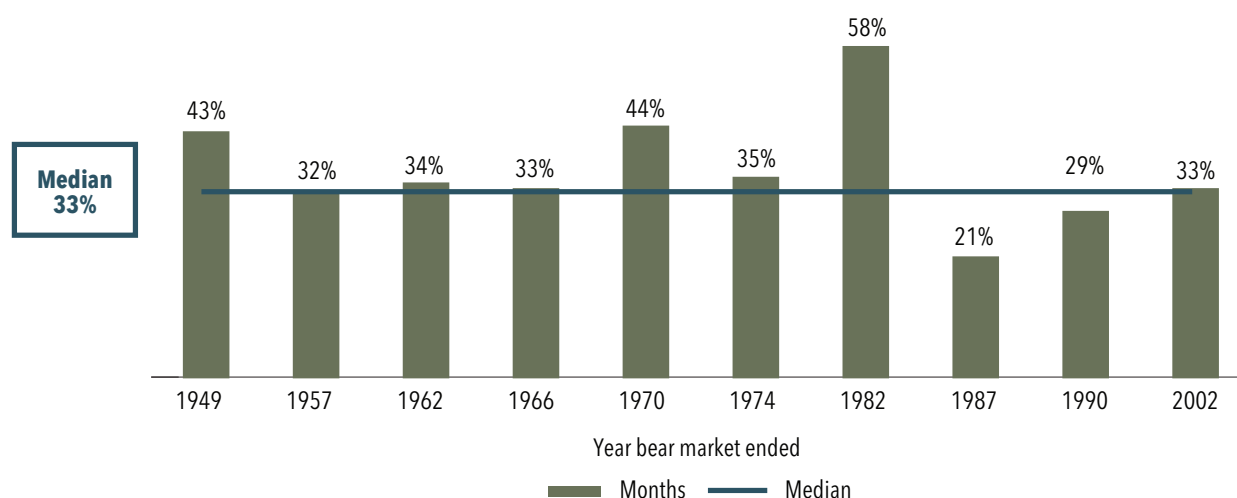


E = Estimate as of October 31, 2008.

Data source: Standard and Poor's Corporation. Peak-to-Trough Decline and Trough-to-Peak Increase represents price returns of the S&P 500. Past performance is no guarantee of future results. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. Please see endnotes for a complete description of this index.

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Chart 6: One Year After Bear Market



Data source: Standard and Poor's Corporation. Returns represent price returns of the S&P 500. Past performance is no guarantee of future results. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. Please see endnotes for a complete description of this index.

WHAT CAN BE LEARNED FROM PREVIOUS BEAR MARKETS?

TIMING THE MARKET MAY REDUCE RETURNS

It is not possible to identify a completed bear market until after it has passed. Therefore, trying to “time the market” may result in an investor missing the beginning of the upswing and the accompanying, potentially significant, returns.

Chart 6 illustrates the returns of the S&P 500 one year after the end of the bear market ranging from the smallest, 21%, to the largest, 58%, with an average of 36% and a median of 33%.

The impact of first year returns after a bear market can be significant. Chart 7 compares the annualized 1, 3 and 5 year returns of the S&P 500 for a hypothetical investor who participated in the market performance of the first year after the end of the bear market to one who did not.

Chart 7: The Difference the First Year Can Make

	Annualized Returns of the S&P 500, for one, three and five year periods after the S&P 500 troughed				A hypothetical investor experience showing the impact of waiting to invest until one year after the S&P 500 trough					
	1-Yr	3-Yrs	5-Yrs	Cumulative 5 Year Returns	1-Yr	3-Yrs	5-Yrs	Cumulative 5 Year Returns	Difference in 5 Year Annualized Returns	Difference in 5 Year Cumulative Returns
Average returns after Bear Markets	36%	16%	13%	89%	0%	4%	6%	38%	-7%	-51%
Median returns after Bear Markets	33%	16%	13%	84%	0%	5%	7%	41%	-6%	-43%
Highest returns after Bear Markets	58%	23%	27%	225%	0%	8%	16%	106%	-11%	-119%
Lowest returns after Bear Markets	21%	8%	6%	31%	0%	-1%	-2%	-9%	-8%	-40%

Past performance is no guarantee of future results. The example shown is hypothetical and designed to illustrate the potentially negative effects of market timing. It is not intended to predict or represent the results of an actual investment. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. An individual investor's experience will vary and there is no assurance that an investment will provide positive performance over time. Data source: Standard and Poor's Corporation. Returns represent price returns of the S&P 500.

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HAVE A CLEAR POINT OF REFERENCE

Those who study investor behavior often speak of the tendency for investors to “anchor” or use an incorrect number or fact as a point of reference. In discussions about bear markets, including this one, the focus is usually on the decline of a broad market index of stocks such as the S&P 500. Upon hearing that the market is down a certain percentage, it’s easy to use that number as the reference point for the decline of an entire portfolio. However, if an investor has a diversified portfolio, the relative amount of their portfolio decline is likely to be less. “Anchoring” on an incorrect point of reference can cause investors to potentially make short-term decisions that may be hazardous to their long-term financial goals.

Consider the following hypothetical portfolio examples in Chart 8 and their percentage returns during the months of selected bear markets. (Note that returns are based on monthly data for this illustration; data used in the previous charts was S&P 500 daily returns.)

While past performance is no guarantee of future results, in each case shown below, the return of the diversified portfolio was more favorable than that of the portfolio of 100% stocks (“the market”). (For the results of other portfolio mixes of stocks, bonds and cash, see Appendix A.)

“Far more money has been lost by investors in preparing for corrections or anticipating corrections than has been lost in the corrections themselves.”

Peter Lynch (as quoted in “Learning to Love This Bear Market”, Larry Swedroe, Money, October, 2008)

SEEK AN OUTSIDE OPINION

In bear markets it can be tempting for investors to react to every up and down in the market, potentially moving their carefully crafted financial plans off course. The danger lies in ignoring the “big picture” (i.e., the historic perspective), and

Chart 8: Hypothetical Portfolio Examples During Months of Selected Bear Markets

	100% Stocks/ 0% Bonds/ 0% Cash	60% Stocks/ 30% Bonds/ 10% Cash	40% Stocks/ 50% Bonds/ 10% Cash
May, 1946 – June, 1949	-9.5%	-4.0%	-1.0%
August, 1956 – October, 1957	-12.8%	-7.1%	-4.3%
December, 1961 – June, 1962	-21.9%	-12.2%	-7.3%
February, 1966 – October, 1966	-11.5%	-5.9%	-3.2%
November, 1968 – May, 1970	-21.9%	-11.5%	-6.8%
January, 1973 – October, 1974	-33.0%	-16.6%	-8.8%
November, 1980 – August, 1982*	3.6%	13.6%	18.7%
August, 1987 – December 1987	-21.4%	-11.7%	-6.9%
July, 1990 – October, 1990	-14.1%	-7.2%	-3.6%
March, 2000 – October, 2002	-32.8%	-8.1%	5.5%

Past performance is no guarantee of future results. The example portfolio allocations shown are hypothetical and designed to illustrate the potential advantages of diversification. It is not intended to predict or represent the results of an actual investment. Different benchmarks and economic periods will produce different results. All indices are unmanaged and unavailable for direct investment. An individual investor’s experience will vary and there is no assurance that any investment will provide positive performance over time. Diversification does not ensure against market loss.

* The return shown is positive because it considers the entire month; the bear market began on November 28, 1990. This data is based on monthly total returns data. Source: Ibbotson Associates. Stocks are represented by the S&P 500; Bonds are represented by One-bond Intermediate-Term Government Bonds portfolio; Cash is represented by One-bill U.S. Treasury Bills portfolio.

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projecting short-term information into long-term trends. While past performance is certainly no guarantee of future results, there is benefit to taking a long-term view in evaluating a specific event. Investors may be well served by working with a financial advisor who can help them remain focused on their long-term goals and objectives.

IMPORTANT DISCLOSURES

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INDEX DESCRIPTIONS

The Dow Jones Industrial Average is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq. The DJIA was invented by Charles Dow in 1896.

The S&P 500® Index is a readily available, carefully constructed, market-value-weighted benchmark of common stock performance. Currently, the S&P includes 500 of the largest stocks (in terms of stock market value) in the United States; prior to March 1957 it consisted of 90 of the largest stocks. Returns assume no taxes or transaction costs. Price return does not include income or reinvestment of dividends.

Stocks – Large Company Stocks Total Return are based upon the S&P Composite Index. The S&P Composite Index includes 500 of the largest stocks (in terms of stock market value) in the United States; prior to March 1957 it consisted of 90 of the largest stocks. Returns assume no taxes or transaction costs.

Bonds – Intermediate-Term Government Bonds Total Return consist of a one-bond portfolio* with an approximate maturity of five years. The bond chosen each year is the shortest noncallable bond with a maturity not less than five years, and it is held for the calendar year. Returns are formed assuming no taxes or transaction costs. *Ibbotson Associates uses this portfolio to compare bond returns over time.

Cash – U.S. Treasury Bills Total Return consist of a one-bill portfolio with an approximate maturity of 30 days. Each month a one-bill portfolio containing the shortest-term bill having not less than one month to maturity is constructed. Returns are formed assuming no taxes or transaction costs.

¹ Investopedia.com

² Standard and Poor's Corporation

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Appendix A: Asset Allocation - Model Portfolios During Months of Bear Markets Since World War II

%Stocks/%Bonds/%Cash	100/0/0	90/0/10	80/10/10	70/20/10	60/30/10	50/40/10	40/50/10	30/60/10	20/70/10	10/80/10	0/90/10	0/100/0
May, 1946-June, 1949	-9.5%	-8.3%	-6.9%	-5.4%	-4.0%	-2.5%	-1.0%	0.4%	1.9%	3.4%	4.8%	5.1%
August, 1956 - October, 1957	-12.8%	-11.2%	-9.8%	-8.4%	-7.1%	-5.7%	-4.3%	-3.0%	-1.6%	-0.2%	1.1%	0.9%
December, 1961 - June, 1962	-21.9%	-19.6%	-17.1%	-14.7%	-12.2%	-9.8%	-7.3%	-4.8%	-2.4%	0.1%	2.5%	2.6%
February, 1966 - October, 1966	-11.5%	-10.0%	-8.6%	-7.3%	-5.9%	-4.5%	-3.2%	-1.8%	-0.5%	0.9%	2.2%	2.1%
November, 1968 - May, 1970	-21.9%	-18.7%	-16.3%	-13.9%	-11.5%	-9.2%	-6.8%	-4.4%	-2.0%	0.4%	2.7%	1.9%
January, 1973 - October, 1974	-33.0%	-28.3%	-24.4%	-20.5%	-16.6%	-12.7%	-8.8%	-4.9%	-1.0%	2.9%	6.8%	6.0%
November, 1980 - August, 1982*	3.6%	5.9%	8.5%	11.0%	13.6%	16.1%	18.7%	21.2%	23.8%	26.3%	28.9%	29.1%
August, 1987 - December, 1987	-21.4%	-19.0%	-16.6%	-14.2%	-11.7%	-9.3%	-6.9%	-4.4%	-2.0%	0.4%	2.9%	2.9%
July, 1990 - October, 1990	-14.1%	-12.4%	-10.7%	-8.9%	-7.2%	-5.4%	-3.6%	-1.9%	-0.1%	1.6%	3.4%	3.5%
March, 2000 - October, 2002	-32.8%	-28.5%	-21.7%	-14.9%	-8.1%	-1.3%	5.5%	12.3%	19.1%	25.9%	32.7%	35.1%

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