

THE AUGUST 2024 (VOLATILITY) CRASH—LESSONS FOR INVESTORS & MANAGERS

Kostas Grigorakis, CFA®, Managing Director – Investments, Senior PIM Portfolio Manager

August 20, 2024

Part 1 – The Panic

By July-end, the broader US market had shown a solid uptrend (S&P 500 up +15.78% YTD at 5522.30) [1].

In August, with many Wall Street managers on vacation and apprehensive lieutenants at the helm, concerns arose about the market's health and sustainability: Was the rally just a bubble? Could AI deliver on its promises? Were Q2 earnings merely decent instead of spectacular? And why was Warren Buffett amassing cash?

August started with some weak economic data: On August 1st, the manufacturing ISM fell into contraction, and on August 2nd, disappointing July jobs data triggered recession fears, especially after tripping a critical level known as the “Sahm rule” threshold.

The market began to worry that central banks were compounding their errors. The Fed, already pressured by the market in 2022 and mid-2023, seemed woefully slow to cut rates. Meanwhile, the Bank of Japan raised its rate, strengthening the yen and pressuring the borrowers profiting from the “yen carry trade” (borrowing at low yen rates to buy higher-yielding US assets). The need to reverse this trade became urgent, especially after news broke that Buffett had cut his massive Apple stake by 49% in Q2.

Panic erupted on Monday, August 5:

After dropping previously -8.16%, the Japanese Nikkei 225 index crashed by 12.40%—its worst drop since 1987's Black Monday—pushing the index 25% below its recent July high and under its previous peak in 1989. In the US, the “fear index” (VIX) exploded to 65.73—its third highest reading after its spikes in 2008 and the CoViD crash of 2020—driving the S&P 500 index down -3.00%—its biggest loss in three years.

What was an investor/manager to do?



Part 2 – The Post-Mortem

August 2024 started alarmingly. On Monday, August 5, the Nikkei 225 plummeted -12.40% [1], falling 25% below its recent all-time high and even under its peak from 35 years ago! The S&P 500 dropped -3.00%, marking its worst decline in three years, while the VIX (‘fear index’) surged to 65.73, its third-highest reading after 2008 and 2020. For a moment, August 5 felt like a redux of “Black Monday,” with loud calls for portfolio selling and repositioning.

But there was no follow-through—Black Monday was followed by a ‘White Tuesday.’

Investment and Insurance Products: Not FDIC Insured / No Bank Guarantee / May Lose Value

Wells Fargo Advisors is a trade name used by Wells Fargo Clearing Services, LLC, Member SIPC,
a registered broker-dealer and non-bank affiliate of Wells Fargo & Company.

On August 6, everything reversed: The Nikkei 225 rebounded by an astonishing +10.23%, the S&P 500 rose by +1.04%, and the VIX plunged to 27.71—the fastest 57.8% drop in the index’s history. This episode turned out to be more of a Volatility Crash than a Market Crash, leaving pundits perplexed.



What happened?

As chronicled in our Q2 Strategy and Market Update [2], going into this episode, our research indicated that the market was healthy and investmentworthy—both in terms of its internal functioning and the economic backdrop. Firmly in its long-run bullish regime, the market had significant resilience, providing it with substantial ‘immunity’ to large exogenous shocks as powerful as August’s convergence of bad news or even the ‘black swan’ of the CoViD outbreak in 2020.

While exogenous shocks are not systematically forecastable, we believe that strategies that can track and adapt to market regime shifts are well-positioned to absorb their impact without getting derailed from their longer-term growth trajectory.

Since regime-tracking is neither commonplace nor easy, we invite you to closely examine our strategies.

[1] All data—Source: YCharts, FactSet.

[2] <https://fa.wellsfargoadvisors.com/gnh-capital-group/mediahandler/media/653679/GNH%20Capital%20Group%20-%202024%20Q2%20Strategy%20and%20Market%20Update.pdf>

Wells Fargo Advisors is a trade name used by Wells Fargo Clearing Services, LLC, Member SIPC, a registered broker-dealer and non-bank affiliate of Wells Fargo & Company.

Wells Fargo Advisors did not assist in the preparation of this report, and its accuracy and completeness are not guaranteed. The opinions expressed in this report are those of the author(s) and are not necessarily those of Wells Fargo Advisors its affiliates. The material has been prepared or is distributed solely for information purposes and is not a solicitation or an offer to buy any security or instrument or to participate in any trading strategy. Additional information is available upon request.

[PM]-09052027-5276218