TD Wealth

The Bear Returns

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A newsletter from William Barlow, CFA, CIM®, B.Sc., Portfolio Manager, Senior Investment Advisor, TD Wealth Private Investment Advice

"In bear markets, stocks return to their rightful owners."
-J.P. Morgan

Moving the Markets:

Inflation continues to be a key focus from a market and economic perspective. In the U.S., there was hope that inflation could be easing, however this was dashed when the latest CPI print came in above expectations. This has some thinking central banks are too far behind the curve.

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Not seen since the challenging months of early 2020, the proverbial Wall Street bear has returned with a vengeance. A traditional bear market is defined as a decline of 20% or more from prior peaks, and the S&P 500, which tracks many of the world's largest U.S. based companies, has recently stooped below this level. Declines of this magnitude are extremely challenging: portfolio values cascade lower, talking heads adamantly suggest that the sky is falling, and the urge to 'stop the bleeding' moves from being the cardinal investing sin, to a compelling idea. Given that emotions can get the best of us and lead to poor decision-making, it might be helpful to look at past periods of panic to set expectations. How often do bear markets occur? How long do they last? What should one do from a portfolio standpoint during such declines? These are all important questions that I'll try to address in this note.

It was only last year that economists were talking about a Goldilocks economy and the potential for a raging 20's style recovery. Fast forward to this year, and we're hearing the very same economists warning of stagflation and a lost decade! It's no wonder economics is known as the dismal science amongst skeptics. The reality is that markets are cyclical, trees don't grow to the moon, and though the timing of the current bear has been surprising to many, bear markets will likely be a feature for decades to come. In fact, this is the 23rd bear market since 1929, ranging from the short and shallow variety like the 2018 bear (a 20% decline over three months), to the long and deep variety we saw in 2008 (a 58% decline lasting 17 months) (https://compoundadvisors.com/2022/every-bear-market-is-different). For more colour, bear markets have lasted 12 months on average, and took 21 months to recover. If one were to rebalance, the recovery would be quicker, although the fortitude to buy in the face of relentless selling isn't always easy.

Another way to splice the data is to look at the average decline during such markets, in addition to the days to form a bottom after the bear arrives. On this front, we know that the average decline is a troubling 32.7%, and it took 131 days to bottom after the ominous 20% level was breached. Given that the average stock has been declining on some metrics since last year, we can be hopeful that we are closer to bottoming than average, but this data wouldn't have one swinging for the fences just yet.

We now know that bear markets happen every 4 years on average, that the declines last about 12 months (including extreme cases of 1929 and 2008), and perhaps most importantly, that all previous bear markets have recovered. This leads to the next most important question: what action should be taken from a portfolio standpoint? The answer is going to depend on one's personal circumstances and mindset, but we can draw some general conclusions. The first and most attractive option is to increase savings, and prepare to invest at lower levels. This acknowledges that buying low has been a consistently strong strategy since the beginning of time. The second option is to prepare to rebalance, by shifting assets between cash, fixed income, and equities, which is another way to buy while assets are on sale. The least favourable option would be to bail out on one's plan by giving into short-term fear. This could be an egregious error, and likely prolongs recovery.

I find the statistics above helpful as a historical guide, but they also exclude a very important point: markets have returned roughly 10% annually, despite the occasional bear rearing its head. The implications are critical and twofold: This too shall pass, and our behavior during a decline, likely trumps the decline itself.

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What I'm Reading: *What can Sherlock Holmes Teach Investors?* By Joe Wiggins. An article rather than a book, but I think an important one because it focuses on how the drumbeat of negative noise tends to increase during bear markets. The summary quote is useful given the current environment: "*As investors, we not only need to ensure that we are able to focus on what matters and why, we must be constantly on guard against the often-irresistible specter of noise.*"

Who I'm Following: Marko Kolanovic, JP Morgan's Chief Global Strategist, is on record suggesting that the market will stage a near full rebound starting sometime in the second half of the year. The award-winning strategist posits that yields have gone too far, and that the market is pricing in an extremely hard landing which might be avoided. As a result, beaten up technology companies, energy companies, and Chinese listed American Depository Receipts (ADR's) are looking attractive.

Market Folly: Non-fungible tokens, which can be defined as unique digital assets (pictures), might be remembered as the poster child for COVID-era irrational exuberance. The most talked about are JPEG-like images of primates, collectively known as bored apes (literally pictures of bored monkeys). The 'cultural phenomenon' has run into tough times, with the average bored ape NFT falling by as much as 95% from an average of $188K USD. Worse still, a raft of bored apes have been stolen by hackers, no doubt adding insult to injury.

Reason to be Optimistic: Corporate insiders, arguably those who know their companies most intimately, are buying their companies' stock more than they are selling, for the first time since 2020. According to Bloomberg, this has historically been a bullish signal looking forward, and could suggest that corporate executives are not as anxious as the market in general. This data is consistent with that of Argus Research, who have noted the same findings in their Vickers's Insider Sentiment segment (https://www.bloomberg.com/news/articles/2022-05-23/insiders-put-recession-angst-aside-to-binge-on-their-own-stocks).

Outside the Office: The biggest news on our end is that my family and I are moving from our townhouse this summer. We figured it made sense to wait for the housing market to explode and the stock market to roll over before making the biggest purchase of our lives! Kidding aside, it will be great to have a yard for our boys after being without one during the pandemic.

Select Benchmark Returns – June 30, 2022

Asset Class	YTD	1 Year	5 Years	Asset Class	YTD	1 Year	5 Years
S&P/TSX Composite (Canada)	-11.13%	-6.47%	4.44%	**CDN Bond Index**	-12.23	-11.39	0.18
S&P 500 (US)	-20.58%	-11.92%	9.33%	**CDN Short Term Bond Index**	-4.39	-4.79	0.90
MSCI Europe	-22.3%	-19.74%	-0.45%	**CDN Long Term Bond Index**	-22.13	-19.74	-1.04
MSCI Emerging Markets	-18.78%	-27.2%	-0.2%	**US$/CDN$**	-1.62	-3.82	0.14
MSCI Far East	-19.4%	-21.17%	0.49%	**S&P TSX Energy**	39.79%	63.49%	5.88%
MSCI World	-21.21%	-15.51%	5.85%	**S&P TSX Materials**	-9.05%	-5.72%	5.33%

Source: TD PAIR Price Return, TD Securities

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