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MID-YEAR REVIEW & COMMENTARY

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Growling Bear Market

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"Much of the "excess" has been wrung out of U.S. equity markets this year."

Forgive us our dentist friends but sometimes "bear" stock markets remind me of trips to the dentist. They are necessary, they are sometimes painful, and one is generally glad when they are over. Unlike dentist visits, bear markets fortunately don't come every six months but only once or twice per decade.

Such was the case in the first half of 2022. We entered "bear" market territory in mid-June when the S&P 500 Index ('S&P 500') officially fell 20% from its January 2022 high. This was the second bear market of the 2020's – the first, of course, was the March 2020 bear market that occurred as Covid spread world-wide. It was the shortest bear market in post-World War II starting on Feb. 19, 2020 and ending on March 19th, 2020.

No telling how long this one will last, but painful it has been so far.

If you don't know by now, equity markets in the U.S. had their worst start to the year in decades.

The S&P 500 fell 16.1% in the second quarter and is down 20.0% year-to-date. Other indices fared badly as well: The Dow Jones Industrial Average is now down 14.4% for the year while the tech-heavy NASDAQ Composite is down 29.2%. Size didn't make much difference with the S&P 600 small-cap index down 18.9% and the S&P 400 mid-cap index down 19.5%. The only factor that mattered in year-to-date performance was style. Value stocks outperformed growth stocks by a wide margin with the Russell 1000® Value index down "only" 12.9% versus the 28.1% drop for the Russell 1000® Growth Index.

Unlike earlier in the year, there were no positive sectors in the second quarter. The weakest sectors were consumer discretionary (-25.5%), communications services (-20.9%) and technology (-19.7%) while the strongest sectors were consumer staples (-4.0%), utilities (-5.1%) and energy (-5.3%). Energy remains the only sector with positive year-to-date returns. Defensive sectors such as consumer staples and utilities gained strength in the quarter while economically sensitive stocks weakened.

Bonds provided little help to performance with the S&P U.S. Aggregate Bond index down 10.0% year to date. Gold fell 1.2% from December 31st. Bitcoin fell 59.2%. Oil was the winner with a gain of 40.6%.

The key reasons for the weak markets are well-known but their consequences are harder to gauge:

In the U.S., Fed bankers are raising interest rates to stem inflation. Fears abound that they will overshoot and cause a recession even though other economic indicators such as unemployment rates still suggest a strong economy. Meanwhile, rising rates make many stocks less attractive and make bonds a reasonable investment alternative compared to stocks, something not seen in years.

Similar situations are occurring outside the U.S. High inflation is prevalent in many countries and bankers there are raising rates to (over)

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control it, leading to fears of a global slowdown.

The Russia-Ukraine conflict, a large part of the reason for the high inflation, shows no sign of ending soon and the economic damage it is causing in Europe is significant. Germany is warning of gas service interruptions soon and is warning citizens on the need to conserve fuel for the upcoming winter.

There is some good news in this year's bad news.

Much of the "excess" has been wrung out of U.S. equity markets this year. The S&P 500 is now expected to "earn" about $228 per share in 2022. With today's valuation of 3822.6, its p/e ratio is now 16.8x earnings, much more reasonable than its p/e ratio of 21.4x at the beginning of the year. There is, however, a caveat worth thinking about. There is now a more than reasonable chance earnings will not live up to current expectations once results start being released in mid-July. According to Factset, of the 238 S&P 500 companies that have issued 2022 earnings guidance through June 30, 132 have issued "negative" guidance and 106 have issued "positive" guidance. Thus, it is likely that earnings estimates fall a bit over the summer, pushing p/e estimates up.

There are already some signs that inflation is moderating. Crude oil prices have slipped from $120 per barrel to $100 on July 5, a 20% drop. Lumber prices have fallen by more than 30% while copper prices are 20% below their earlier highs. Consumers' latest estimates of future inflation are now slightly below the May figures.

In addition, in most cases, bear markets don't last forever, and markets recover after them, often spectacularly. The accompanying charts from LPL Research illustrate this.

Bear Market Recoveries

S&P 500 Index Length To Recover From A Bear Or Near Bear Market

Month of Peak	Month of Low	Length of Bear (Months)	% Decline	Length of Recovery (Months)
8/2/1956	10/22/1957	15	-21.6%	11
12/12/1961	6/26/1962	6	-28.0%	14
2/9/1966	10/7/1966	8	-22.2%	7
11/29/1968	5/26/1970	18	-36.1%	21
1/11/1973	10/3/1974	21	-48.2%	69
9/21/1976	3/6/1978	17	-19.4%	17
11/28/1980	8/12/1982	20	-27.1%	3
8/25/1987	12/4/1987	3	-33.5%	20
7/16/1990	10/11/1990	3	-19.9%	4
7/17/1998	8/31/1998	1	-19.3%	3
3/24/2000	10/9/2002	31	-49.1%	56
10/9/2007	3/9/2009	17	-56.8%	49
4/29/2011	10/3/2011	5	-19.4%	4
9/20/2018	12/24/2018	3	-19.8%	4
2/19/2020	3/23/2020	1	-33.9%	5
All Bear Markets		11	-30.3%	19
If Bear Is Worse Than -22%		14	-37.2%	27
If Bear Is Better Than -22%		7	-19.9%	7

Source: LPL Research, CFRA FactSet 05/20/22

All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

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Stocks Do Well After They Go Into A Bear Market

S&P 500 Index Performance After Going Into A Bear Market (1950 - Current)

Date Bear Market Starts	Trading Days To Enter Bear Market	S&P 500 Index Returns		
		3 Months	6 Months	12 Months
10/21/1957	305	5.2%	9.3%	31.0%
5/28/1962	115	7.3%	11.2%	26.1%
8/29/1966	139	7.9%	17.6%	24.6%
1/29/1970	288	-4.9%	-8.9%	10.7%
11/27/1973	221	0.7%	-9.2%	-28.1%
2/22/1982	310	3.0%	1.3%	32.1%
10/19/1987	38	10.9%	14.7%	22.9%
3/12/2001	242	6.3%	-7.4%	-1.2%
7/9/2008	188	-20.0%	-27.2%	-29.1%
3/12/2020	16	21.0%	34.6%	59.0%
Average		3.8%	3.6%	14.8%
Median		5.8%	5.3%	23.8%
Higher		8	6	7
Count		10	10	10
% Higher		80.0%	60.0%	70.0%

Source: LPL Research, FactSet 05/20/22
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future
Performance back to 1950 incorporates the performance of predecessor index, the S&P 90.

The second half of 2022 should be challenging. As always, we are happy to help with whatever investment question you might have.