02.11.2022 – Roller Coaster Times

With the big rise in the stock market at the end of last year, who wudda thought the stock market would close today below where it was 6 months ago (although I did predict a 7-10% Spring correction in my Nov 2021 note). As you can see by the 6-month stock chart it has been quite the up and down ride.

And, just when people were starting to feel comfortable to go back into the stock market with the lessening of Covid restrictions and the acceptance of Fed rate hikes, yesterday we got the whammy of a Fed Reserve member shouting about **intermeeting** rate hikes^ and, today, the double whammy. Our government is proclaiming the guns of war are virtually upon us in the Ukraine.* Notwithstanding the various geopolitics and horrible tragedies of a possible war, this messed up a pretty good day. It's enough to give someone the "big one." https://youtu.be/stdi-1tIUhM (JSYK - the video is probably not "politically correct")

^https://www.zerohedge.com/markets/bullard-bearard

* https://www.cnn.com/europe/live-news/ukraine-russia-news-02-11-22/index.html

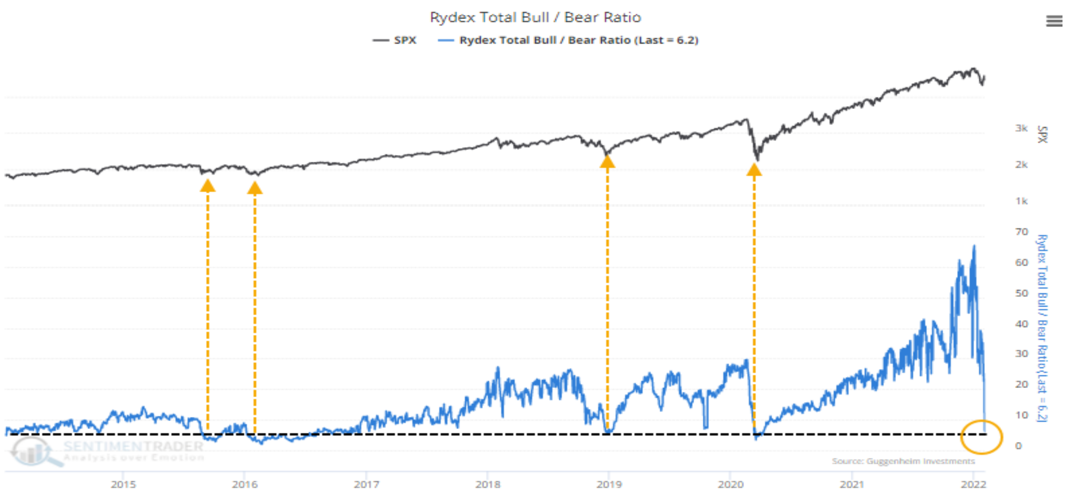
SPX Performance Around Rate Hike Cycles (Initial Hike Dates, 1982 - Current)

Hike Cycle Starts	12M Prior	6M Prior	3M Prior	1M Prior	1M After	3M After	6M After	12M After
1/31/1982	-7.06%	-8.04%	-1.22%	-1.75%	-6.05%	-3.29%	-11.05%	20.68%
1/31/1984	12.46%	0.52%	-0.09%	-0.92%	-3.89%	-2.06%	-7.80%	9.93%
6/30/1988	-10.03%	10.34%	5.98%	7.92%	-0.54%	-0.58%	1.54%	16.26%
2/4/1994	4.50%	4.74%	2.69%	0.63%	-1.08%	-3.85%	-2.43%	1.88%
6/30/1999	21.07%	11.43%	5.53%	5.44%	-3.20%	-6.56%	6.68%	5.97%
6/30/2004	17.07%	2.81%	1.23%	1.80%	-3.43%	-2.30%	6.37%	4.43%
12/17/2015	1.44%	-2.79%	2.60%	-0.42%	-7.91%	-0.06%	1.44%	10.59%
1/26/2022 ?	14.24%	-0.56%	-3.87%	-6.94%	-	-	-	-
Average	6.71%	2.31%	1.61%	0.72%	-3.73%	-2.67%	-0.75%	9.96%

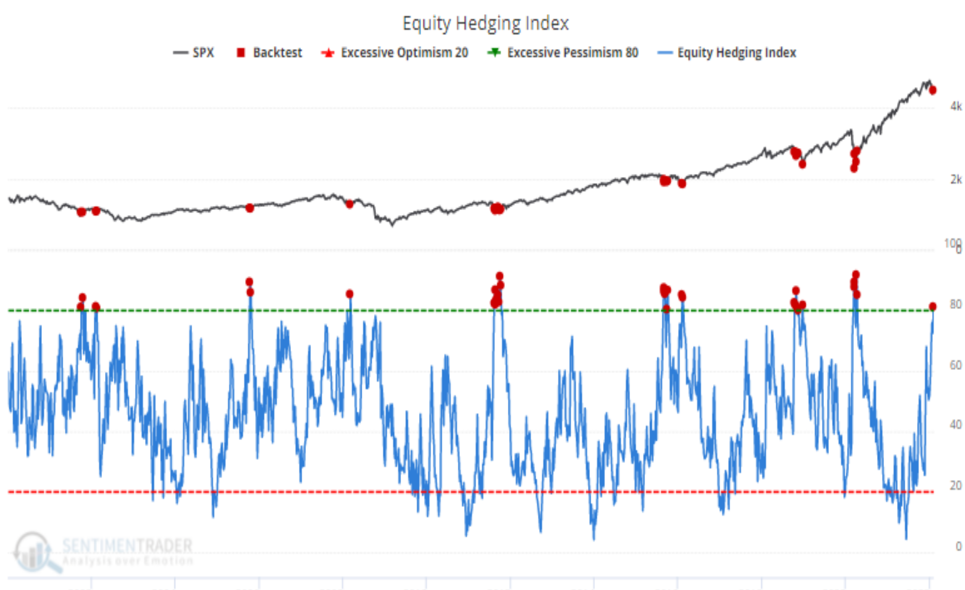
The question, as always, is where do we go from here? Of course, most everything I write about the markets is my opinion and it could be wrong. If history is any guide, we are in for some continued volatility with lots of churning until the new regime takes hold. Here's a table from Goldman Sachs (I know it's blurry. Sorry about that) showing stock market performance before and after rate hikes begin. While it's all iffy going as far as 6 months afterwards, the 1 year returns for the last 7 rate hike cycles show average returns that are in line with my "predictions" from my Nov 2021 newsletter, "6000 or Bust." https://tacticaladvisoryservices.com/market-updates

Most any time the Fed starts to increase interest rates, it's been due to some sort of inflationary impulse/stock bubble forming and I don't believe today is any exception. In most of the previous cases, there has been a transformation of the investment cycle from growth to value or something similar. I believe that's what's going on here. Today was a perfect example. The growth fund "QQQ" was down about 3% while the value fund "VTV" only declined about 1%. The "real stuff" components of the value index, of which we are significantly overweight, were up hugely with the energy fund "XLE" up almost 3%, gold up a bit less than 2%, and commodities up about 1.5%. (source: Yahoo Finance). Obviously, it won't be this way every day. I do believe the transition has begun and over the course of time, we will grind our way higher.

While history doesn't necessarily predict the future, I thought these two additional graphs* may help to calm some nerves. The first one shows the ratio of "bulls" (people who think markets are going up) to "bears" (people who think markets are going down). When there's lots of bulls the jagged blue line goes up and when the bears rule, the blue line goes down. As you can see by the orange circle, we are about at the lows in the ratio for the last 8 years, which also happen to coincide with other lows in the stock markets (see the orange arrows pointing upwards). This gives me hope that lots of people have sold their weak hands allowing the market to move back up.



This 20 year stock index chart is a bit more complicated but it shows something similar to the "bull/bear" ratio. The red dots indicate times when there is lots of "hedging" in the stock markets. Hedging generally means buying "insurance" to protect one's portfolio in the event stocks go down. Most of the time people don't want to buy insurance because it costs money and hurts returns. Also, most of the time, people/funds only buy insurance after the fire has started costing them even more money. If you look at the table below the graph, you'll see the index's average returns between 1 week and 1 year after the hedging crossed into the "excessive pessimism" stage. The average returns are quite good. I stress those are "average" returns. No indicator is perfect and this one isn't either. It missed a doozy when there was lots of hedging in late 2007. So, there's that.



	1 Week Later (%)	2 Weeks Later (%)	1 Month Later (%)	2 Months Later (%)	3 Months Later (%)	6 Months Later (%)	1 Year Later (%)
Average Returns	0.74%	1.88%	4.39%	5.95%	6.75%	12.06%	16.27%
Median Returns	1.04%	1.68%	4.06%	7.11%	6.66%	11.11%	16.76%
Win Rate	58%	70%	79%	82%	79%	88%	85%

As mentioned earlier, we have been moving into "value" and "real stuff" at our Nationwide Advisory Services accounts over the past few months. My belief is the cycle continues and the companies that flew to the sky with no or little positive cash flow will continue to see a rerating of their prices downward while companies with reasonable valuations that can produce needed stuff that actually makes a profit will be rewarded. Seems like that should be common sense for all the times but, as I've learned and we've seen the past couple of years, stock markets aren't ruled by common sense. They are ruled by sentiment. (https://www.elliottwavetrader.net/market-update)

As always, thank you for allowing me to be of service. Please let us know if you have any questions or need anything.

Enjoy,

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