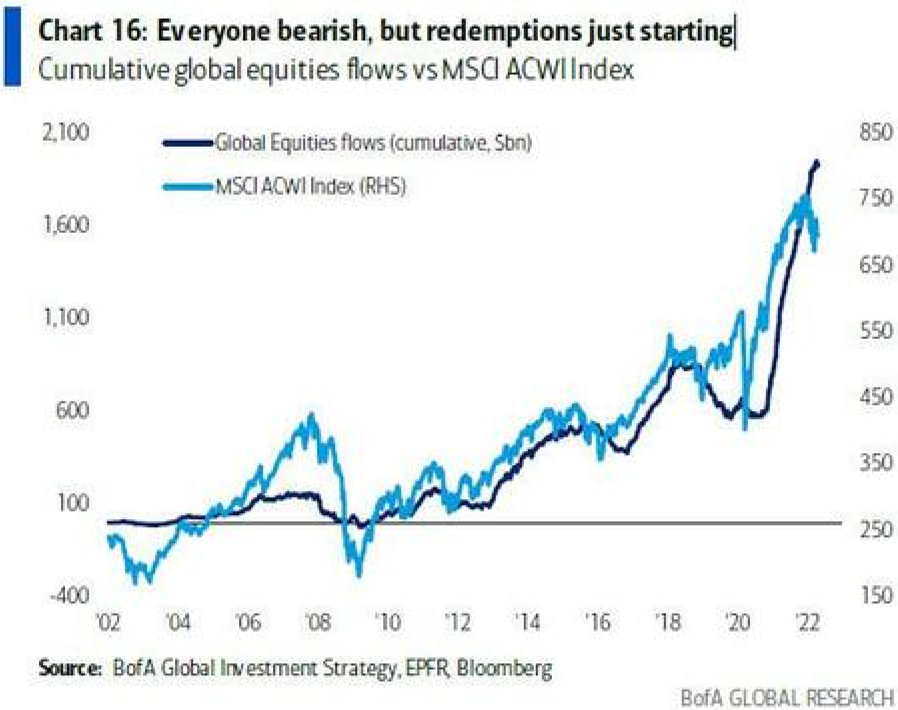
Wall Street’s Most Accurate Analyst: “Today’s Bear Market Ends In October With The S&P At 3,000”

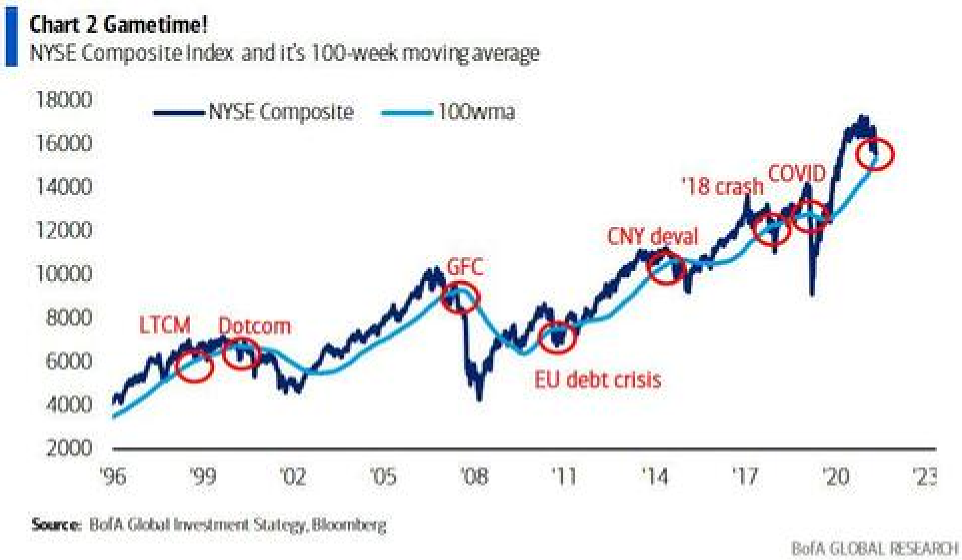
Description

Two weeks ago, just when everyone thought that he couldn’t turn any more bearish, BofA’s chief investment strategist Michael Hartnett, Wall Street’s biggest bear who is by implication has also emerged as the most accurate sellside analyst (the average S&P price target of his peers is still around 4,700), stunned everyone when he told readers that while the mood on the street was already dismal, relaying the the Heard on the Street line was *“I’m so bearish, and even I’m miserable*“, he warned that even though **everyone** was bearish, redemptions were just starting, and the real selling was only just beginning.



One week later – and much to the embarrassment of JPM's in house permabull who at the same time said to take the other side of the trade and to buy stocks – Hartnett was again been proven right, with the S&P tumbling and the Nasdaq suffering its worst month since the Lehman bankruptcy. Hartnett also correctly warned that the closer we got to the 4,000 "strange attractor" level, the more aggressive the selling would become (as we discussed in "Hartnett Turns Apocalyptic, Says Carnage To Accelerate With "Max Pain" And "Exit" Waiting Below 4,000")

Since then it's gotten ***even*** worse, providing the biggest bear on Wall Street with even more ammo for his latest weekly Flow Show note (available to pro subscribers in the usual place), and he wastes no time to terrify his readers of the hell that is coming, warning that with the NYSE Composite (US stocks + ADR's + bond ETFs) down -9% YTD to 100-week moving average, **"recession/crises in past 25 years have always seen our fave Wall St barometer break decisively below this level (15350 today)…at 100wma;"** And in case that's not enough, he also warns that **"every crisis/recession sees meaningful dip below 100wma…game time!"**



Extending this analogy to all bear markets – because the only ones who still don't realize that the S&P is in a brutal bear market are JPMorgan's strategists – Hartnett compiles the following useful information:

- 9 bear markets in the past 140 years
- Average price decline = 37.3%
- Average duration is 289 days

Table 1: Bear markets are quicker than bull markets
History of US equity bear markets (S&P 500)

Peak	Trough	Decline	Recovery	Event (s)
09/1929	06/1932	86.2%	03/1937	Crash of 1929, 1st part of Great Depression
03/1937	04/1942	60.0%	05/1946	2nd part of Great Depression, WWII
10/2007	03/2009	56.8%	02/2020	Global Financial Crisis
06/1911	12/1920	51.0%	12/1924	WWI, Post-War Auto Bubble Burst
03/2000	10/2002	49.1%	10/2007	Dot-com bubble burst
01/1973	10/1974	48.2%	08/1987	Inflationary Bear Market, Vietnam, Watergate
11/1968	05/1970	36.1%	01/1973	Start of Inflationary Bear Market
01/1906	10/1907	34.2%	08/1908	Panic of 1907
02/2020	03/2020	33.9%	03/2020	COVID-19 Crash of 2020
08/1987	10/1987	33.2%	07/1990	Black Monday
4/1899	06/1900	30.4%	03/1901	Cornering of Northern Pacific Stock
05/1946	06/1949	29.6%	08/1956	Post-war Bear Market
12/1961	06/1962	28.0%	02/1966	Height of Cold War, Cuban Missile Crisis
10/1892	07/1893	27.3%	03/1894	Silver Agitation
11/1886	03/1888	22.0%	05/1889	Depression, Railroad strikes
04/1903	09/1903	21.7%	11/1904	Rich Man's Panic
8/1897	03/1898	21.1%	08/1898	Outbreak of Boer War
09/1909	07/1910	20.6%	02/1911	Enforcement of the Sherman Anti-Trust Act
5/1890	07/1891	20.1%	02/1892	Barings Brothers Crisis

Source: BofA Global Investment Strategy, Ibbotson, SBBI Yearbook, Bloomberg
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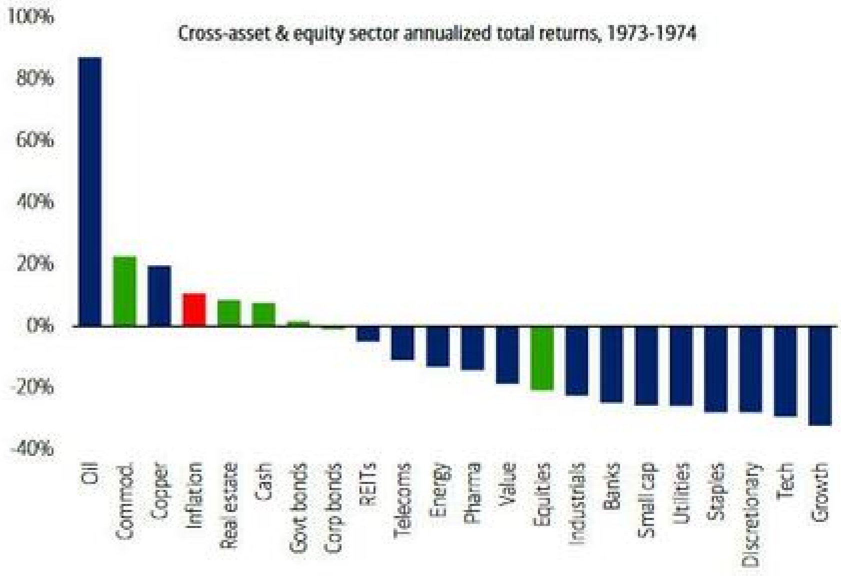
And while past performance no guide to future performance, if it were, **today's bear market ends Oct 19th '22 with S&P500 at 3000, Nasdaq at 10000.** There are two silver linings here:

- first: many stocks are already there, i.e., **49% of Nasdaq >50% below their 52-week highs, 58% of Nasdaq >37.3% down, and 77% of index in bear market, i.e. down >20%;**
- second: bear markets are quicker than bull markets.

Hartnett next echoes what we said yesterday in our discussion of the BOE's shocking decision, which we said confirms the worst stagflationary case for the economy. According to the BofA strategist, the BoE projected UK CPI >10% by Oct'22, cut '23 GDP forecast 150bps to -0.25%; in other words, **10% inflation, 0% growth the living definition of stagflation.**

It's why to Hartnett, the correct relative playbook is 1973/74 and it shows that **cash and commodities beat bonds & stocks** (esp consumer & tech; note *Big Tech starting to ape Nifty 50 crash*).

Chart 3: 1973/74 relative playbook
Cross-asset & equity sector annualized total returns (1973-74)



Prior to 1990 Energy = Oil, Gas & Consumable Fuels; Telecoms = Integrated Telecoms
Source: BofA Global Investment Strategy, Bloomberg, Ibbotson, Fama-French growth/value series, Case-Shiller, Bureau of Economic Analysis, Homer & Sylla, A History of Interest Rates
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Chart 16: Stagflation quilt
Annual returns by asset class and sector

Source: BofA Global Investment Strategy, Bloomberg
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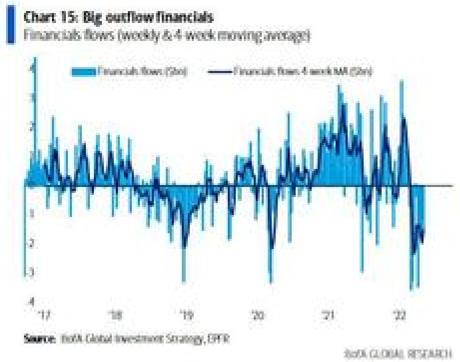
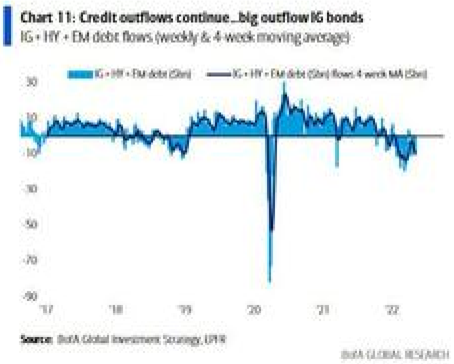
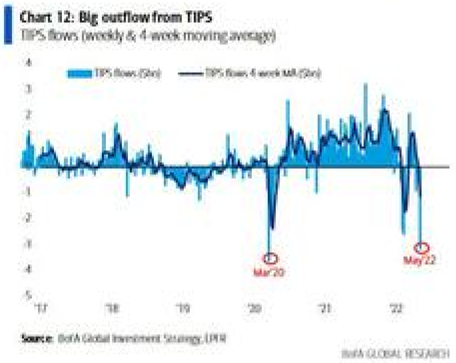
Meanwhile, flows – which are always a leading indicator for sentiment – confirm that none of this is a shock to investors, and after some huge outflows in the past month, the latest weekly flows into the

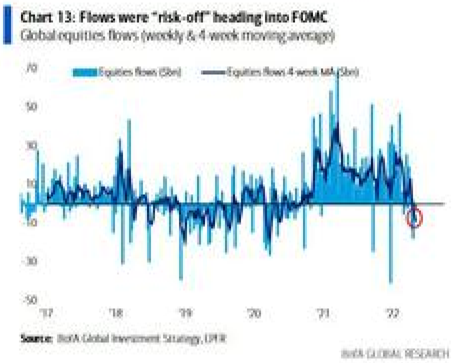
FOMC were massively “risk-off” as investors waved in the cash: $0.3bn from gold, $3.4bn from stocks, $9.1bn from bonds, $14.0bn from cash. Some more details:

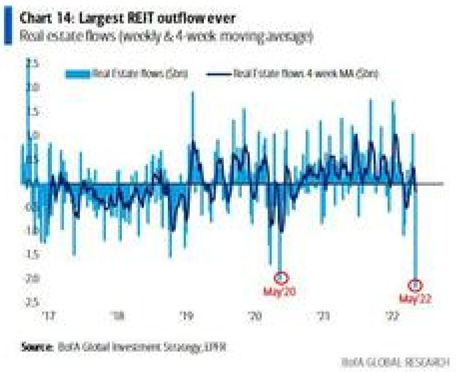
- big inflow to Treasuries ($6.0bn),
- big outflow from TIPS ($3.2bn),
- big outflow IG bonds ($7.3bn),
- largest REIT (real estate) outflow ever ($2.2bn),
- big outflow financials ($1.6bn),
- **4-week average of flows to stocks turning most negative since May’20 when the Fed had to step in to bail out the market.**











Turning from the past – both distant and recent – to the future, and Hartnett’s 2022 View, it will come as no surprise that the BofA strategist is not exactly bullish. Here’s how he see things playing out

- **Base case remains equity lows, yield highs yet to be reached**
- Wall St to spend much of ’22 working through “inflation shock”, “rates shock”, “recession shock” =

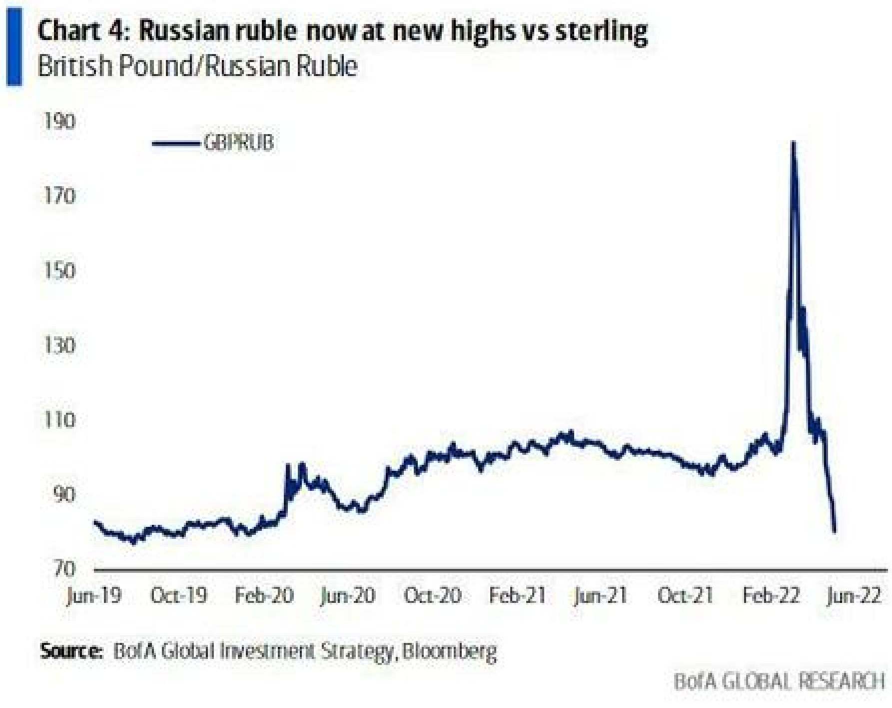
negative, volatile returns in absolute terms

- Relative calls defensive…cash/volatility/commodities>stocks/bonds, IG>HY, defensives>cyclicals
- Meantime as recession risks next move up in commodities should be tactically sold,
- Lead indicators of bear market were trough in yields & US$ + peak in EM, crypto, speculative tech (e.g. biotech) in Q1'21; **only once yields & US$ peak, and floor in EM, crypto, speculative tech follow, should risk be added,** first and foremost in corporate bonds – we are not there yet (and note speculative tech will remain in bear market for next 2 years, **a floor does not = new bull market)**

Finally, Harnett turns to his favorite topic – the *three types of shocks that define the transition from 2020 to 2022*. According to the BofA strategist, **in past 9 months "inflation shock" was priced-in slowly, "rates shock" was priced-in slowly, but "recession shock" was priced-in too quickly;** this is a problem as stronger-than-expected economic data in H1'22 is causing market to price-in longer/bigger inflation/rates shock.

Inflation shock: inflation set to "peak" but lower inflation likely to be "transitory" given biggest macro story of '22…a lack of supply of energy, food, housing, labor relative to demand showing scant signs of improvement…

Energy…natural gas prices at highest since '08 as world scrambles to reconfigure energy supplies (note explosive upside of Russian ruble now at new highs vs sterling, euro, US dollar),



Food…fertilizer prices @ all-time highs = cost of food production up = supply of food down = price of food up, note corn prices @ new highs & food prices seriously vulnerable to super-spike on poor harvests,

Chart 5: Fertilizer prices at all-time highs
Global fertilizer prices

Source: BofA Global Investment Strategy, Bloomberg

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Houses…mortgage rate surging but 93% of US mortgages are fixed and supply of existing homes near record low, as evidenced by housing permits highest since '74

Chart 6: Supply of existing homes near record low
Existing home sales inventory vs Home permits

Source: BofA Global Investment Stategy, Bloomberg, Suttle Economics

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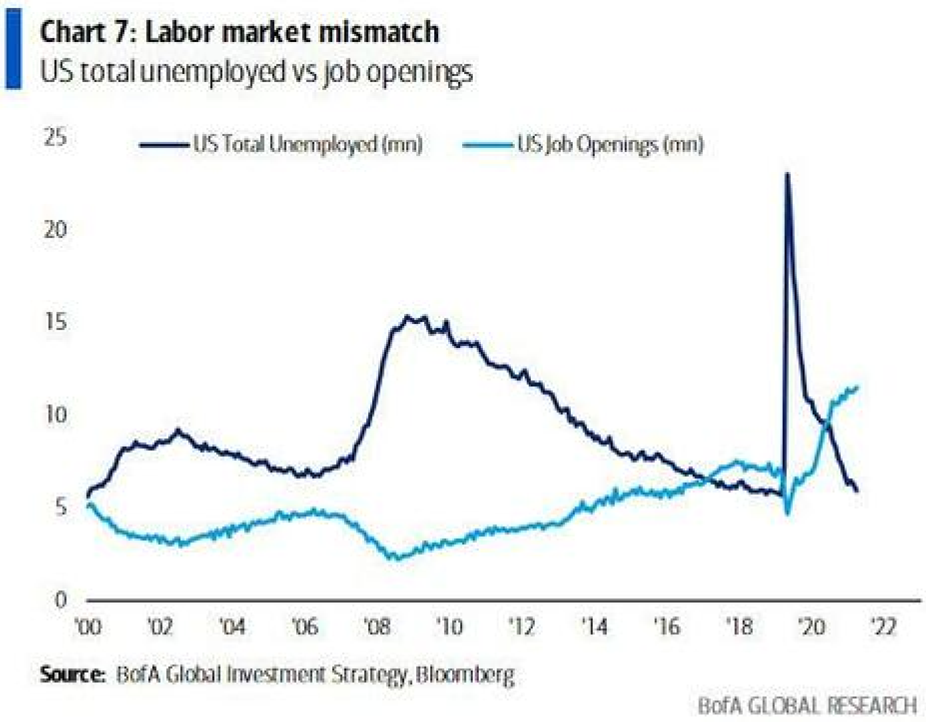
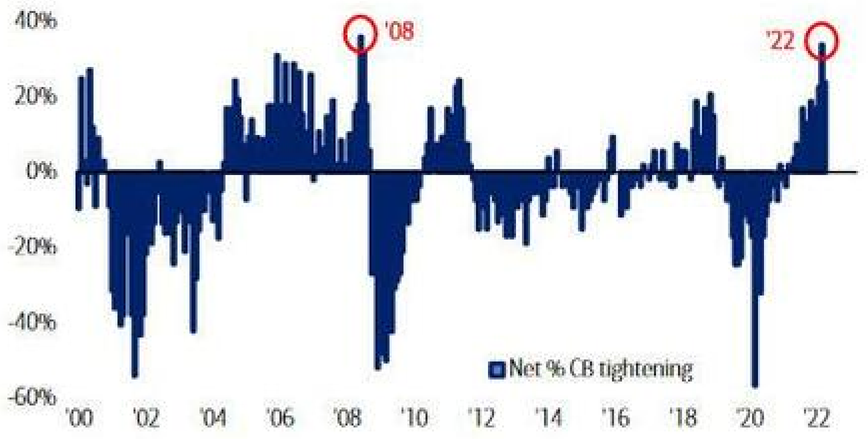
Labor…there are 12mn US job openings versus a 6mn supply of unemployed workers , you do the math.



Rates shock: yes central banks on course to hike rates 251 times in 2022, yes net 34% tightening monetary policy most since '08, yes QT starts H2'22, yes not a lot rate hikes can do about broken supply chains; but yields & volatility will rise until Fed & central banks ahead of the curve…this week they moved further behind curve; US inflation 8%, EU inflation 8%, UK inflation heading >10%, yet they are quivering at the thought of selling $1 of bonds (QT) after buying $23,000,000,000,000 since Lehman, and $11,000,000,000,000 since COVID-19; little wonder bond vigilantes back to trading "end of central bank credibility" = volatility entrenched.

Chart 8: Rates shock
Net % central banks tightening



Source: BofA Global Investment Strategy, Bloomberg

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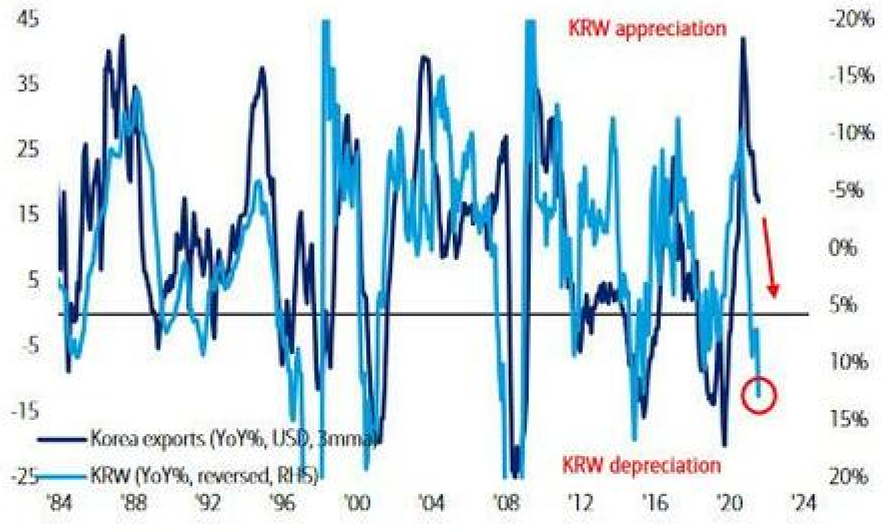
<u>Recession shock:</u> the economy today is strong, a problem; **but macro data has turned from unambiguously strong to ambiguously strong**; business confidence has stalled (see PMI's) which threatens to stall improvement in labor market in H2; Asian FX devaluation discounts weaker Asian export growth…

Chart 9: Asian FX deval discounts weaker Asian export growth
South Korean Won vs Exports



Source: BofA Global Investment Strategy, Bloomberg

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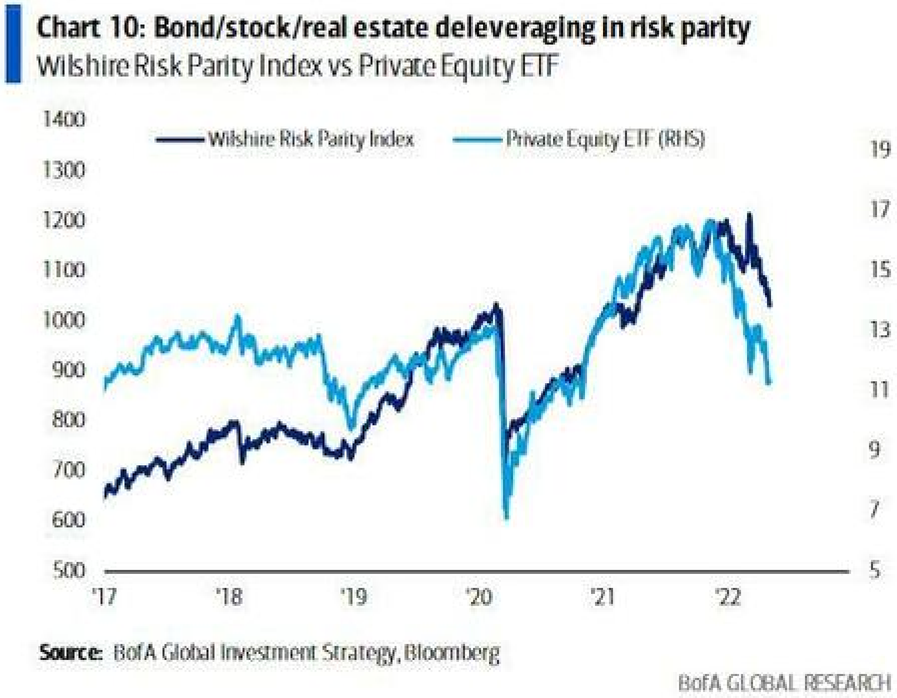
… which discounts weaker US consumer; **and quickest route to recession on Main St is via a sharp decline in asset valuations on Wall St, & risk of systemic events on bond/stock/real estate deleveraging in risk parity** (RPAR)…



… **private equity, sovereign wealth funds, credit events in speculative tech, shadow banking, US consumer buy now, pay later models, Emerging Markets, zombie corporations, goes up with every rate hike.**

by Tyler Durden

Category

1. Economy-Business-Fin/Invest
2. Main

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