FUN FACTS TO PONDER

A key lesson I learned from my 13 years as a financial advisor is that human behavior really does not change. Yes, today we have more sophisticated analytics and information flow, but in the end, greed and fear generally prevail. The behavior is almost always driven by recency bias.

Case in point, how was the chase into “disruptive technology ETFs” after they were up over 100% last year any different than Tulip Mania of 1637? It was caused by greed in 1637, and it was caused by greed in 2020.

For this very reason, Applied Equity Advisors is keen to watch for historical precedents that might be applicable to the current investing environment. In effect, due to the consistency of human behavior, we can and should draw from the past.

To that end, here are a few investment factoids that have caught my eye recently and found their way into my investment notes:

1. Good things still to come for stocks?

   This is the 19th time since 1950 the S&P 500 is up over 10% through May. Of those previous 18 times, the SPX ended the year higher 15 times with a median return of an additional +9% for the rest of the year.2

2. Seems like everyone expects a 10%-15% pullback this summer - me included! However:

   The S&P 500 has spent 147 trading days without a 5% pullback, the 18th longest streak since 1928. While you may think that would increase the likelihood of bigger correction to come, it's actually just the opposite. “Buy the dip” mentality is so ingrained, it appears to have historically limited the drawdowns in the past.

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1 ARKK ETF. Factset.

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Of the 17 previous periods of even longer streaks than the current one, there was not a single drawdown of 10% or more over the next three months.3

3. “Tapering” might not be the death knell for stocks:

At a Congressional testimony on May 21, 2013, then Fed Chair Ben Bernanke hinted that the Fed could begin to taper sometime in the future. From then until June 24, 2013, the S&P 500 dropped a paltry -5.6%. From that low until the Fed actually commenced tapering in December 2013, the S&P 500 rallied 16%.4

4. It might not be too late to buy energy stocks:

While energy is the best performing sector YTD in the S&P 500, it still has not kept up with the commodity price. Since early January 2020, WTI is 10% higher, but the XLE remains 8% lower.5

Since 1928, there have been 7 times one sector has been up over 30% in the first quarter of the year. Today, energy makes the 8th instance. The average return for such a sector for the rest of the year is +12%, and it has always generated a positive return.6

5. And yet little enthusiasm for energy:

Of the 19 Wall Street firms that publish oil price estimates, only one believes WTI will end the year above $70.7

6. If financials are dependent on rising bond yields, then why:

Quarter-to-date, 10 year bond yields are down -24 basis points, but the XLF (financial sector ETF) is up +12% absolute, +5% relative.

Over the last five years, the XLF price movement has led rates, not the other way around.8

Plus, if utilities are highly correlated to lower bond yields, then why:

Quarter-to-date, despite bond yields that are down, utilities are up only 1% and -5% relative to bonds.9

7. Speaking of two value sectors (financials and energy), it still may be early in the value cycle overall:

The average value cycle of outperformance lasts 33 months. This one is 8 months old.10

8. Meanwhile here comes a new group of value buyers:

The largest Momentum ETF performed its semi-annual rebalance in late-May. The technology sector weighting was reduced from 43% to 18%, and the financial sector was increased from 2% to 32%.11

9. Growth had better turn around soon, or else:

Equity hedge funds remain 700 basis points overweight growth to value. Through mid-May, equity hedge funds had returned -1% YTD.12
10. Is the long-term dollar / emerging markets relationship breaking down or is EM about to outperform?

From February 2002 to July 2014, the DXY (US dollar index) dropped -34%. During that time, EEM (MSCI EM Index) dramatically outperformed both the SPX and MXWO (MSCI World Index). From that 2014 low until March 20, 2020, the DXY rallied 29%. During that period, EEM was by far the worst performing of the three indices.\textsuperscript{13}

Since March 2020, the DXY is down -12% but EEM has slightly lagged the SPX and MXWO. So far.\textsuperscript{14}

And finally:

11. If you think the equity market is in a bubble....

This past Monday, June 7th, Amazon 5-year bonds were offered at a 1 basis points premium to the risk-free 5-year Treasury.\textsuperscript{15}

Andrew

\textsuperscript{13} Bloomberg. May 25\textsuperscript{th}, 2021.
\textsuperscript{14} Bloomberg. June 9\textsuperscript{th}, 2021.
\textsuperscript{15} Ice Bond Point. June 7\textsuperscript{th}, 2021.

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