

# It's so bearish out there, it makes me bullish

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**“The most common cause of low prices is pessimism—sometimes pervasive, sometimes specific to a company or industry. We want to do business in such an environment, not because we like pessimism but because we like the prices it produces. It’s optimism that is the enemy of the rational buyer.” – Warren Buffett**

There comes a time when poor economic data becomes good financial data. Let’s face it, there is no shortage of poor economic data at the moment. Just a few examples include record-high inflation numbers, the hawkish stance of central banks (globally), and the continued downward revision of global growth numbers. Couple that with dire confidence levels and you might just start to feel cautiously optimistic about the prospect of better returns going forward. Now, this might seem like a counterintuitive statement, but it is exactly what this article sets out to explain.

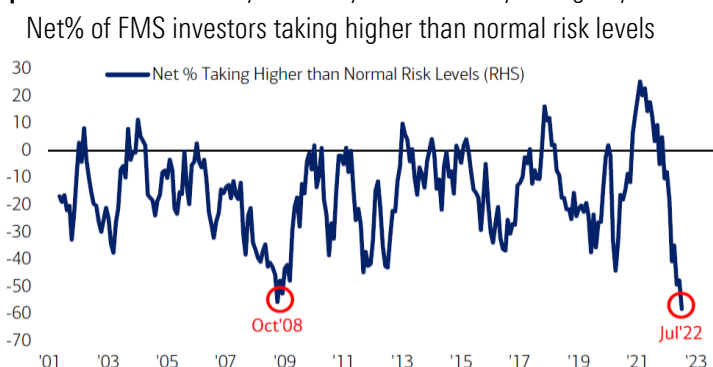
Markets could feel the brunt of more bad news in the coming months and the yo-yo effect could continue for a while longer. When markets sell off in a fashion like we have seen in 2022 (to date), it is our job to pay attention. Even though everything is not outright cheap, there is no doubt that asset prices today look a lot more attractive than this time last year.

## Painting the bear picture

According to the latest Bank of America (BofA) Fund manager survey, global growth optimism and global profit optimism are at an all-time low. Fund Managers’ cash levels are also sitting at the highest level since 2001 and equity allocations versus cash allocations have fallen to the lowest level since 2008. It is also interesting to note that within equities investors are overweight utilities, staples, healthcare (defensives) and underweight more cyclical shares like banks. The BofA survey expands further in the report, talking about deteriorating liquidity conditions and cash (specifically the US dollar) being the most crowded trade at the moment.

The below chart shows how the level of risk-taking in portfolios has decreased substantially compared to a year ago.

### Exhibit 1 | What level of risk do you think you’re currently taking in your investment?



Source: BofA Global Fund Manager Survey, BofA Global Research. Data as at 19 July 2022. For illustrative purposes only.

For Financial Advisors and their Clients

Pretty gloomy, right?

### Courageously contrarian

A simple concept when it comes to investing is contrarianism. This refers to a willingness to do the opposite of what everyone else is doing. Unfortunately, the challenge with being different is that it will be extremely uncomfortable most of the time. Bargains are available at times when there is a pervasive negative narrative around them and a great deal of pessimism. That is when things normally go on sale and risk is the lowest.

The question I get asked the most is how much pain the market can still endure before it starts to rally again. In other words, "please help me time the bottom (of the market)". The difficulty of course is that no investor (no matter what their level of skill or intelligence) can time the bottom of the market perfectly.

At Morningstar, our decades of research findings all point out that *time in the market remains superior to timing the market*. Now and then markets will give investors an opportunity to buy and right now, the market has graciously given us an opportunity like this.

### The upside of the downside – is there a silver lining?

If 2022 were to end today, it will be marked as one of the worst years on record for the US stock market. As bad as it may sound, there is a silver lining to this market low. From the table below you can see that historically the best returns were generated following periods of very large drawdowns. So, for those brave enough to deploy capital when everything seems bearish, the odds are significantly in your favour to generate great returns going forward.

### Exhibit 2 | The worst years ever for the U.S. stock market

Year	S&P 500	Reason	Next Year	3 Years	5 Years
1931	-43.8%	Great Depression	-8.6%	35.4%	162.1%
2008	-36.6%	Great Financial Crisis	25.9%	47.6%	126.1%
1937	-35.3%	1937 Crash	29.3%	14.2%	18.7%
1974	-25.9%	1973-74 Bear Market	37.0%	57.8%	99.2%
1930	-25.1%	Great Depression	-43.8%	-23.0%	11.6%
2002	-22.0%	Dot-Com Crash	28.4%	49.0%	81.7%
1973	-14.3%	1973-74 Bear Market	-25.9%	25.7%	24.5%
1941	-12.8%	WWII	19.2%	77.4%	120.6%
2001	-11.9%	Dot-Com Crash	-22.0%	10.9%	34.4%
1940	-10.7%	WWII	-12.8%	30.0%	110.2%
1957	-10.5%	1957-58 Recession	43.7%	61.6%	86.6%

Source: A Wealth of Common Sense, "[The worst years ever in the stock market](#)". Data as at 22 May 2022. Past performance is not a reliable guide to future performance. For illustrative purposes only and not indicative of any investment.

## How does this impact our portfolio positioning?

We continue to look for opportunities and actively manage portfolios to take advantage of opportunities that arise. While pockets of SA Equities are still looking attractive and we have a healthy exposure to SA Equities, earlier this year we marginally trimmed our SA Equity exposure to take profits from some of the strong returns realized in 2021. We have also used this window to increase our offshore equity holdings in our more equity-centric portfolios where we believe clients will be rewarded for the added risk. Given the attractiveness of current yields, we have maintained our overweight position on SA Government bonds while having limited exposure to SA credit and SA listed Property.

## In closing

The economy is backwards-looking, and the market is forward-looking. Sometimes when it feels like market conditions are at their worst, it is because the worst has already been priced in.

So, how can the current bearish outlook make me feel bullish? Because where others might be caught up in the negativity and gloom of these negative figures, we see opportunity. Broad-based market losses in 2022 have opened opportunities for investors to scoop up investments in high-quality companies at discount prices.

When you have a combination of low prices and lower earnings, coupled with poor sentiment, that's when you should consider turning your bearish view to bullish. ■■■

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### Risk Warnings

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