November 6, 2022

Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Bitcoin	Gold	Crude Oil
32,403	3,771	10,475	1,800	4.16%	21,135	$1,686	$92.60

Investment Strategy Report

While October Looks To Be The Bear Killer, Powell Is Set To Be The Bull Killer

After a brutal month of September for stocks, October once again showed why it has gotten the reputation of being the bear killer. Stocks hit bottom at the end of September and continued to struggle for the first 2 weeks of October. But then, as if on cue, stocks took off for the rest of the month, ending October with solid gains. Throughout this year, there were several other times when it seemed that the market had bottomed and had begun a recovery: in March, May, and June through the end of July. However, each time, the recovery proved short lived and the market decline continued to reach new lows.

Market watchers know that historically, bear markets in the past have often bottomed in October, even after sometimes sustaining significant damage before the turnaround occurred. Not only that, but 2022 has something else going for it: this year is a mid term election year, and stocks have outperformed during these years compared to non mid term years, by a wide margin. Looking back from 1962 to the present, stock performance from November 1st of a mid term election year going forward was on average 7.3% (3 months), 15.1% (6 months) and 16.3% (12 months). Compare those results with non mid term election years of 2.9% (3 months), 4.2% (6 months) and 6.4% (12 months). All things being equal, you can see why now is a time that you want to be invested.

Of course, all things are not equal. Opposing this tail wind of favorable seasonality, we have a significant head wind: the Federal Reserve and Fed Chairman Jerome Powell. As most of you know, the Fed has been aggressively raising interest rates this year in an attempt to slow inflation. At their most recent meeting last week (Nov. 2nd), they raised rates another 75 basis points, to approximately 3.85% (from about 0.15% at the beginning of the year). The fear is that the Fed is acting too aggressively (despite signs of a slowing economy which I have written about in my previous letters) and will throw the economy into a recession. Investors were hoping that at this past meeting, the Fed would accompany the rate hike with some less aggressive comments about future rate hikes. And in their written statement, released at 2 pm, they did seem to suggest a more cautious pace of rate hikes. And stocks took off to the upside. This bullish move in stocks apparently upset Powell, who, in his 2:30 pm press conference made an about face and stated that “We still have a ways to go” and that “the ultimate level of interest rates will be higher than previously expected”. After Powell did his about face, stocks did the same, reversing course and plummeting lower.

Market sentiment has gotten extremely negative, as most of you can attest to, as we get that sickening feeling that accompanies the extreme market volatility we’ve been experiencing. By one metric, investor pessimism is at its highest level since March 5, 2009 (and we all know how well stocks did from this bear market bottom of the financial crisis). The American Association of Individual Investors (AAII) sentiment survey recently showed that 61% of investors were bearish. This astoundingly high figure is a powerful contrarian signal. And according to Stansberry Research (10/20), stocks typically return 13.1% in the 6 months following a reading as high as this.

When we combine the favorable seasonality with the negative sentiment readings, we can see that there is plenty of impetus to move stocks higher. I am expecting that as the economy shows more signs of slowing, we will get less aggressiveness from the Fed, which will be the positive signal that stocks are waiting for.

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