Wealth Management
Dominion Securities

RBC Dominion Securities Inc.
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Global Insight Weekly Report
The Perfect Storm – May 19, 2022

Bearish Investor Sentiment and What This Means Going Forward

Dear clients,

As equity markets continue to digest a combination of concerns (high levels of inflation; global supply chain issues; war in Ukraine; slowing economic growth; higher interest rates), we thought it would be helpful to highlight how markets tend to perform when investors reach a very high level of negative sentiment.

At the current time, the S&P 500 is down nearly 20% from its recent high in early January, and everywhere you look there are headlines and discussions about recessions and bear markets. This makes sense of course, as there are seemingly lots of reasons for investors to be fearful right now, as mentioned above. However, there is also an important consideration when it comes to long-term success as an investor: Often when it seems like there is no positive news on the horizon, and sentiment has turned extremely bearish on the stock market, that can be a contrarian indicator of a recovery in the near future which leads to positive returns. It is precisely the wrong time to be considering selling and going to cash, and then hoping you will be able to pick the right time to get back into the market. In the past few years, we've seen similar dynamics in December 2018 and during the beginning of the COVID crisis in March 2020. Both times, exiting the market during the height of fear would have led to missing out on a return to new all-time highs several months later.

This is not to say that it's impossible for equity markets to go down a little more before there is a recovery. However, by looking at past market cycles, we can see that these negative market conditions are more likely to improve over the near to medium term. Remaining disciplined in your investment strategy during these times is often hard, but is one of the keys to long term success.

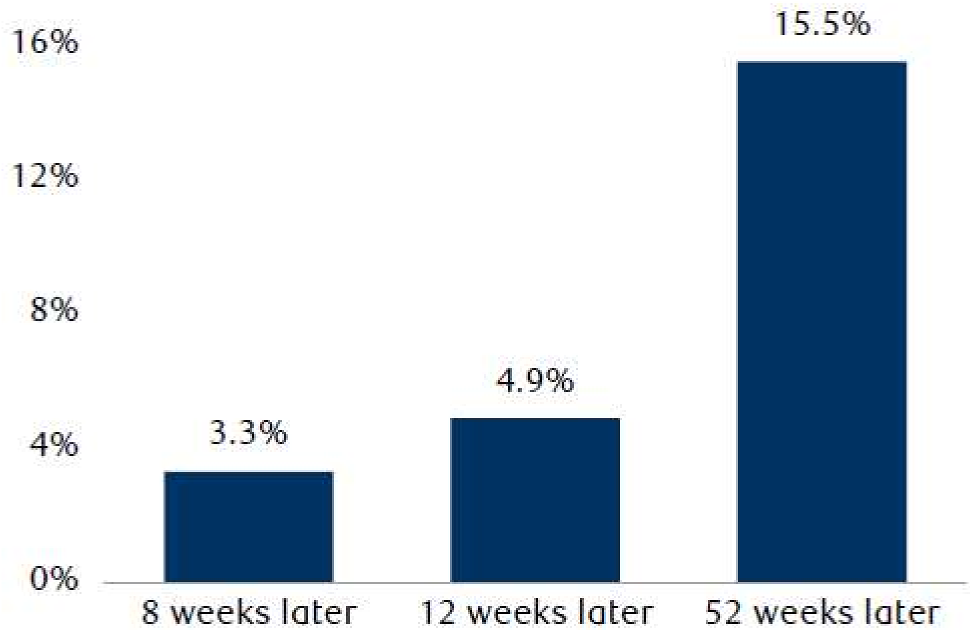
Please see the attached Global Insight Weekly article, which discusses some of the recent weakness in markets, and also provides some historical context for periods of extreme investor bearishness. They use the American Association of Individual Investors (AAII) "bull-bear spread" to show how we've reached the point where there are 31.7% more investors considered bears (negative view of market) than bulls (positive view). This level is more negative than at any time in the past decade, even more than during the height of COVID. In the past, investing in the market at these levels would have worked out quite well over the next year.

From the article:

"An RBC Capital Markets study found that when the AAII bull-bear spread falls below -10, it is typically a short-term buy signal, whereas when the reading rises above +30, it is usually a short-term sell signal... Specifically, the study reveals that since 1987 when the bull-bear spread fell below the -10 threshold, the market bounced soon thereafter and rose 15.5 percent 52 weeks later, on average."

The market tends to rise after sentiment becomes very bearish

Average S&P 500 return after the bull-bear spread is below -10*



* Data represents forward returns when the 4-week moving average of percentage of bulls minus percentage of bears in survey results from the American Association of Individual Investors (AAII) is below -10; survey measures weekly sentiment data from 8/13/87 to 5/19/22.

Source - RBC Capital Markets U.S. Equity Strategy, RBC Wealth Management, AAII, Bloomberg

Please take some time to review the attached report. Also, if you happened to miss the recent conversation with Jim Allworth about inflation and the growth outlook for the economy, you can find that here. It is worth your time.

As always, please reach out to us directly if you have any questions or concerns related to your portfolio.

Best regards,

Ord Private Wealth Management
John, Tim, Liam & Kristen