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Six Charts On The Bear Market Story and What's Next

After the worst start for markets since the Great Depression, here's what investors should consider.

Insight from sub-adviser Schroders Investment Management

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Like a bear with a sore head, many investors probably wish they had stayed in hibernation in 2022. It's been a brutal year so far, the worst since the Great Depression nearly a century ago.

Capital destruction—the amount of money wiped off the value of investments—stands at more than $9 trillion globally, exceeding the financial crisis of 2008.

Most major stock markets are in bear-market territory. A bear market typically describes a condition in which prices of investments fall 20% or more from their recent high.

Cryptocurrency investors have suffered even more. The global value of all cryptocurrencies currently stands at just over $900 billion, down from $2.9 trillion at its peak in late 2021.

The trigger: increasing concerns the economy is barreling toward stagflation (in which slowing economic growth combines with accelerating inflation) or a global recession as central banks raise interest rates and rein in money supply in an effort to tame spiraling inflation. The result has been carnage in financial markets.

In these six charts, we tell the story of the 2022 bear market so far and what investors might do next.

Key Points

Markets have struggled in 2022 due to concerns that central banks' efforts to tame inflation will trigger a period of slow economic growth and high inflation.

Commodities are one of the few sectors experiencing positive growth, while global equities and cryptocurrencies have declined.

Defensive stocks may benefit if the economy heads into recession: Share prices of defensive stocks tend to hold up better than cyclical stocks when the economy slows.

The Battle to Tame Inflation

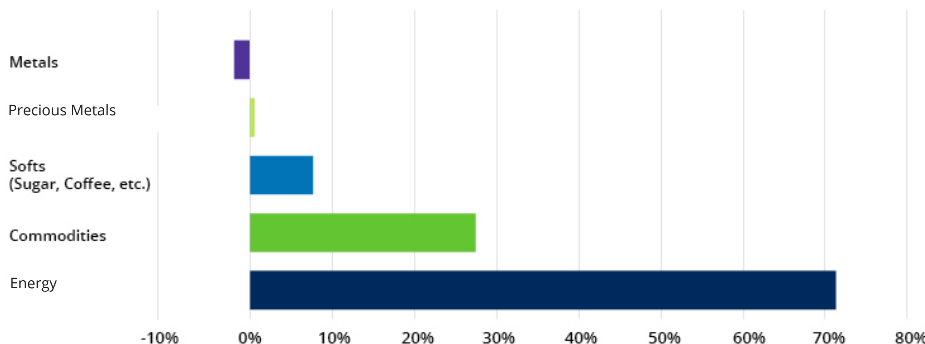
Central banks have been forced into action as inflation in most major economies has already hit 40-year highs and continues to rise. It's brought about stark reminders of the dark days of the 1970s and early 1980s, often called the Great Inflation.

This time it's been exacerbated by pent-up demand following the end of COVID-19 lockdowns in most major economies, combined with supply constraints caused by COVID-19-related lags in Asia and the war in Ukraine.

The result has been surging inflation near double-digits around the world. The main problem is the rising cost of energy, up 70% in 2022, which affects everything from production to consumption. But across the board, commodities are up nearly 30% (**FIGURE 1**).

FIGURE 1

The Rise in Commodity Prices
Commodities



Past performance does not guarantee future results. Year to date as of 6/20/22. For informational purposes only. Sources: Schroders, Refinitiv Datastream

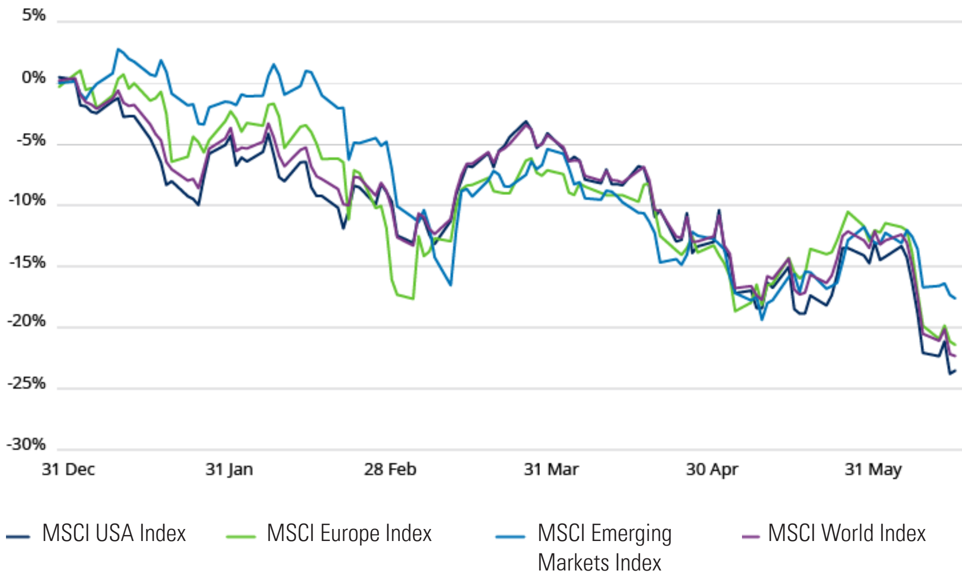
No Major Stock Market Left Unscathed

The worry for investors in stocks is that the more persistent inflation becomes, the more central banks will need to take drastic measures to contain it. If central banks don't manage the process properly, it could lead to stagflation or even a recession—which would spell bad news for consumers and company profits.

The result has been a rout in stock markets that's been brutal, broad-based, and unremitting. From the US to China, developed economies to emerging, most stock markets are down more than 15% so far in 2022, and many have exceeded the 20% bear-market threshold (**FIGURE 2**).

FIGURE 2

The Bear Market for Stocks in 2022



Past performance does not guarantee future results. As of 6/20/22. Investors cannot invest directly in an index. Sources: Schroders, Refinitiv Datastream. See last page for representative index definitions.

Cryptocurrency in Crisis?

In environments such as these, the riskier the investment, the harder it falls. And the cryptocurrency market has fallen further than most (**FIGURE 3**).

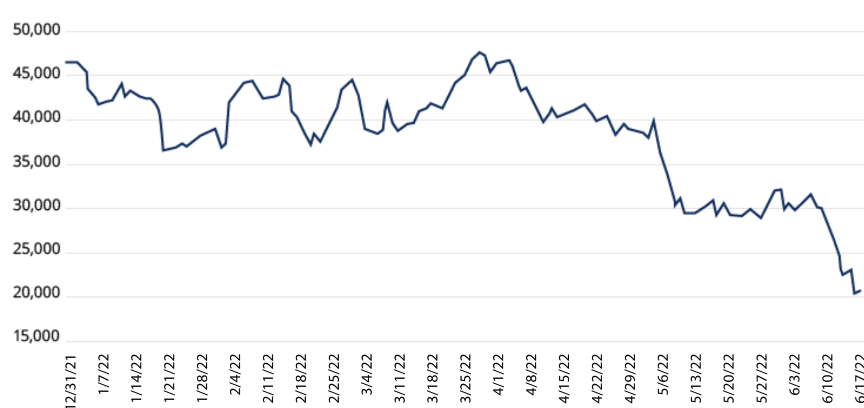
The global cryptocurrency market has lost more than two-thirds of its value since November 2021. But most of the losses were sustained after March 2022 following the collapse of one of its supposed stable coins, terraUSD.

Terra was supposed to maintain a $1 peg, but a run on the coin broke the pegging mechanism and investors' confidence. It is now worth one cent.

Terra's tribulations have had a ripple effect across the cryptocurrency markets. Bitcoin, the leading light of cryptocurrency, is now worth around $20,000, down from its all-time high of nearly $69,000.

FIGURE 3

The Fall of Bitcoin



Past performance does not guarantee future results. As of 6/20/22. Source: Schroders, Refinitiv Datastream

Does a Bear Market Signal a Recession?

The big question, however, is this: Just because investors are panicking, does it mean the economy will enter a recession? Let's take a look at the world's biggest economy, the US, for a possible answer.

While Schroders' economists are not currently forecasting a recession in the US, the risks are skewed toward one. Investors can take some comfort that recessions don't necessarily follow a bear market. That said, the odds are not favorable looking back at history (**FIGURE 4**).

Since the 1900s, the US economy has only managed to avoid a recession 30% of the time when a bear market has occurred.

Looking ahead, the longer the sell-off lasts and the deeper the fall in prices, particularly against a backdrop in which the Federal Reserve is hiking interest rates, then the higher the risk of a recession.

FIGURE 4

Do Bear Markets Signal Recession?

Bear markets and recessions 1900–2022

Bear market dates		Length (months)	Decline (%)	Recession (yes or no)	Recession dates
Start	End				
Sep 1902	Oct 1903	13	-29	Yes	Sep 1902 to Aug 1904
Sep 1906	Nov 1907	14	-38	Yes	May 1907 to Jun 1908
Dec 1909	Dec 1914	60	-29	Yes	Jan 1910 to Jan 1912 and Jan 1913 and Dec 1914
Nov 1916	Dec 1917	13	-33	No	–
Jul 1919	Aug 1921	25	-32	Yes	Jan 1920 to Jul 1921
Sep 1929	Jun 1932	33	-86	Yes	Aug 1929 to Mar 1933
Mar 1937	Apr 1942	62	-60	Yes	May 1937 to Jun 1938
May 1946	May 1947	12	-28	No	–
Aug 1956	Oct 1957	15	-21	Yes	Aug 1957 to Apr 1958
Dec 1961	Jun 1962	6	-28	No	–
Feb 1966	Oct 1966	8	-22	No	–
Nov 1968	May 1970	18	-36	Yes	Dec 1969 to Nov 1970
Jan 1973	Oct 1974	21	-48	Yes	Nov 1973 to Mar 1975
Nov 1980	Aug 1982	21	-27	Yes	Jul 1981 to Nov 1982
Aug 1987	Dec 1987	4	-34	No	–
Jul 1990	Oct 1990	3	-20	Yes	Jul 1990 to Mar 1991
Mar 2000	Oct 2002	30	-49	Yes	Mar 2001 to Nov 2001
Oct 2007	Mar 2009	17	-57	Yes	Dec 2007 to Jun 2009
Feb 2020	Mar 2020	1	-34	Yes	Feb 2020 to Apr 2020
Sep 2018	Dec 2018	3	-20	No	–
Jan 2022	?	5*	-24*	?	?
Averages		**19**	**-37**		
Averages: bear market with recession		**24**	**-40**		
Averages: bear market without recession		**8**	**-28**		

Past performance does not guarantee future results. As of 6/20/22. Source: Schroders, Refinitiv Datastream

Which Stocks Might Perform Best (and Worst)?

Unfortunately, recession isn't the only thing investors are worried about. There's the increasing risk of stagflation—stagnant growth combined with high inflation.

Stagflation tends to favor defensive companies, whose products and services are essential to people's everyday lives, over cyclical companies, whose products aren't. In other words, consumers ignore the new iPhone because they need to pay the electricity bill.

This means the share prices of defensive stocks have tended to hold up better than cyclical stocks when the economy slows, as shown in **FIGURE 5**. The only exception has been energy stocks. This makes sense as the revenues of energy stocks are naturally tied to energy prices, a key component of inflation indices. By definition they should perform well when inflation rises.

In technical terms, defensive sectors have a market beta[1] of less than 1, meaning they've historically outperformed when the index falls, whereas cyclical sectors have a market beta of greater than 1, meaning they've historically underperformed when the index falls.

This is illustrated in **FIGURE 5**, which displays the average historical return of 11 global economic sectors versus the MSCI World Index in stagflation environments.

FIGURE 5

How Stock Sectors Have Performed During Stagflation

Sector	Beta	Cyclical/defensive	Stagflation
Utilities	0.4	Defensive	16.0
Cons stap	0.7	Defensive	14.2
Real estate	0.8	Defensive	11.8
Energy	1.4	Cyclical	8.4
Health care	0.8	Defensive	6.7
Cons disc	1.2	Cyclical	1.0
Materials	1.1	Cyclical	0.4
Financials	1.1	Cyclical	-0.5
Industrials	1.2	Cyclical	-3.3
Comms Svcs	1.0	Neutral	-3.9
IT	1.1	Cyclical	-6.7

Past performance does not guarantee future results. Monthly data from January 1995 to December 2021. [1]Beta is a measure of risk that indicates the price sensitivity of a security or a portfolio relative to a specified market index. Stagflation is calculated as the months in which US CPI inflation was above its 10-year average and our global-business-cycle indicator is in the slowdown phase. CPI, or the Consumer Price Index, is defined by the Bureau of Labor Statistics as a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services. Source: Schroders Economics and Strategic Research Unit.

When Might Stock Markets Recover?

Again, we look to the US for a potential answer (**FIGURE 6**). There have been 11 occasions in the 148 years between 1871 and 2019 when stocks (as measured by the S&P 500 Index) have destroyed at least 25% of value for investors. In the 2001 and 2008 downturns, losses exceeded 40%.

In the worst case, the Great Depression of the 1930s, investors lost more than 80% of their money. It took more than 15 years for them to make their money back—if they remained invested.

Other stock-market falls were not quite so calamitous. In seven of the 11 episodes, investors would have recouped all losses in two years or less if invested in the S&P 500 Index. In the other four—1893, 2001 and 2008—the period to break-even was four to five years.

FIGURE 6

How Long Did US Stocks Take To Recover Losses From a 25% Crash?

Market crash	Maximum loss	Years to breakeven from -25% point
1877	-33%	1.8
1893	-25%	4.0
1903	-26%	1.1
1907	-34%	1.2
1917	-28%	1.5
1929	-82%	15.2
1970	-25%	0.8
1974	-39%	2.0
1987	-26%	1.5
2001	-42%	4.1
2008	-49%	4.8
Median	-33%	1.8

Past performance does not gaurantee future results. Monthly data 1871-2020. Data is for S&P 500 Index and assumes investors retained their exposure to the stock market. Sources: Robert Shiller, Schroders.

To help prepare your portfolio for bear markets and volatility, talk to your financial professional.

MSCI Emerging Markets Index is a free float-adjusted market capitalization-weighted index that is designed to measure equity market performance in the global emerging markets. **MSCI Europe Index** is a free-float adjusted market-capitalization-weighted index designed to measure the equity market performance of the developed markets in Europe. **MSCI USA Index** is a free float-adjusted market cap Indices are unmanaged and not available for direct investment.italization index that is designed to measure the performance of the large and mid cap segments of the US market. **MSCI World Index** is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. **S&P 500 Index** is a market capitalization-weighted price index composed of 500 widely held common stocks.

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