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Delta Insights
a weekly commentary on investing

March 24, 2023

Rolling Bear

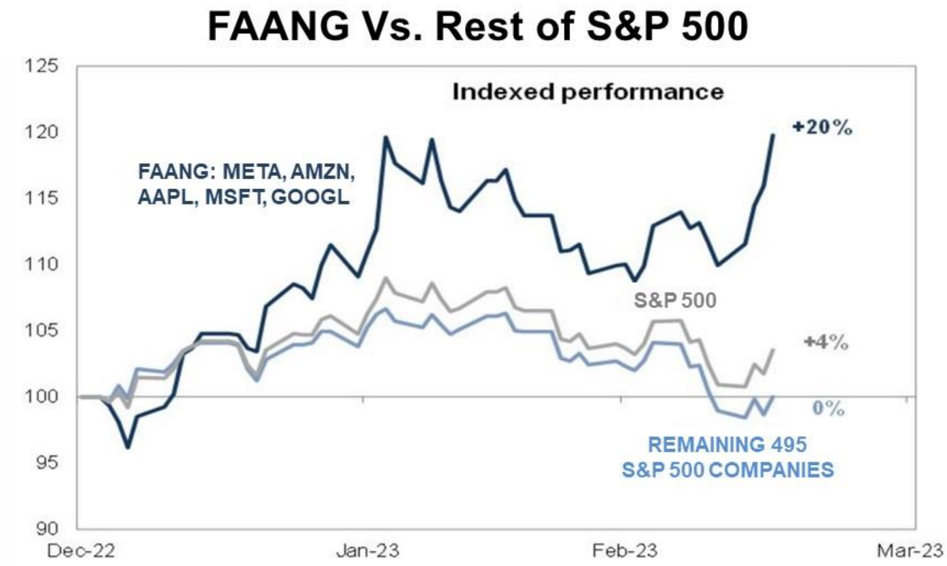
The 2020 35% S&P 500 Covid crash is best described as the Everything Everywhere All at Once bear. It was roughly equitable in its distribution of stock price depreciation in a matter of about a month.

The bear market that began on January 4, 2022 is a rolling bear. Although the S&P 500 declined by about 25% from high to low (so far), the damage has been very uneven. The S&P 500 Value sector (IVE) was down by 5.4% 2022. Leading innovative stocks measured by the ARK ETF (ARKK) were down by 67%. Measured by depreciation, the value sector did not suffer a bear market in 2022 while innovation suffered a depression.

It is characteristic of almost all bear markets that eventually pain is felt in all sectors before a durable bottom is reached. If some sectors avoided the bear in 2022, it is likely the bear will come rolling on over in 2023.

The Bear has begun to roll. It has rolled away from ARKK, up 25% year-to-date, and onto important value sector elements of energy, commodities and banks. Commodities (BCD) are down 7%, energy (XLE) is down 10% and region banks (KRE) are down 27% year-to-date. As a result, the S&P 500 Value sector (IVE) is struggling to stay positive for the year.

As the bear rolls, be prepared to roll investment exposures into market sectors the bear has already mauled and away from what was safe in 2022. Current stock market winners are comprised of large-capitalization, high-cash generating, secular growth technology companies. In a nutshell, the FAANG stocks are back. The NASDAQ 100 is up by about 16% year-to-date (after being down 33% in 2022) and FAANG is up 20%.



Steadily rising interest rates are creating pressure points on economic sectors at different times. In 2022, rising rates compressed high Price/Earnings (P/E) multiples disproportionately impacting high-flying technology stocks and companies without earnings. Low P/E value stocks performed relatively well as their P/E multiples were already compressed and investors believed earnings might hold up with China reopening, recession-light and a Fed pivot.

The regional bank crises which became explicitly evident in the past couple of weeks is the prod that is causing this bear to roll. Lending conditions are likely to tighten. This suggests:

- Cash is king. Cash rich companies with strong cash flow will likely perform better than companies dependent on debt financing and early growth companies with negative profits.
- Real estate is particularly vulnerable in a tight lending market. Banks with under $250bn of assets make up 80% of commercial real estate lending.
    - An U.S. average office vacancy rate of 18.7% as of 4Q22.
    - $1 trillion of Commercial Real Estate (CRE) mortgages are coming due by 2024, 33% of which were originated since the beginning of 2020.
    - There is an additional $1.5 trillion that will mature by 2027.
    - The net effect of the above may be material write-downs in commercial real-estate asset values.
- Higher borrowing rates and standards makes recession more likely.

Because of the increased probability of recession, the probability of Fed rate cuts in the second half of 2023 has risen. The bond market is pricing in 0.75% of rate cuts by the December Fed meeting. This suggests:

- The bond market suffered its worst bear market in modern history last year and its first ever two sequential years of negative performance in 2021 and 2022. Bonds rise when interest rates fall. 2023 should be a recovery year for bonds, especially if default rates remain in the expected range.
- The large cap technology growth stocks are interest rate sensitive as their multi-year forward profit projections are discounted back to a present value. They are unlike cyclical stocks where profits rise and fall dramatically with the economic cycle so P/E multiples are constrained by the assumption that profits are unstable and only a short-period of profit forecasts should be used to determine value today – think short-duration bond. By contrast, the profits of Google, Microsoft, Amazon and other market leading technology companies are considered durable through the full economic cycle – think long duration bonds. The double-digit positive performance of the NASDAQ 100 this year is partly driven by the decline in the 10-year treasury rate from 4% to 3.4%.

Buy-and-hold is a top performing investment approach in a bull market. Buy-and-hold in a rolling bear market may prove to be exceptionally financially painful. The investment landscape is shifting at unprecedented speed causing the dance with the bear to look more like disco than a waltz. Like dance, investment strategies should move in-sync with the music.

Let Us Help You Position Your Portfolio – Give Us a Call Today

We have unique and sophisticated investment methods that seek to capture the stock market's gains while minimizing drawdowns in bear markets. If you would like to learn more about how we manage money, we invite you to give us a call at **(415) 249-6337**, visit www.deltaim.com or email us at info@deltaim.com.

"We located the hissing noise, Mr. Watkins. Your wife's mother is in the back seat."

Delta Stock Market Dashboard

MARKET SENTIMENT IS

BEARISH

THIS WEEK'S NUMBER IS

26.0

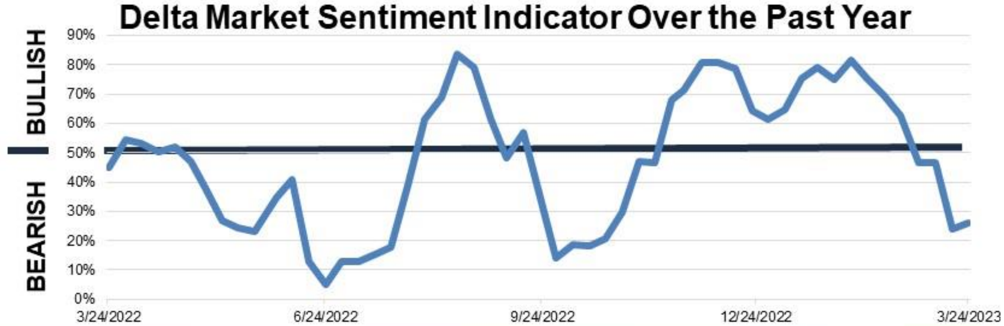
Our technical indicator increased from 23.9 to 26.0 this week

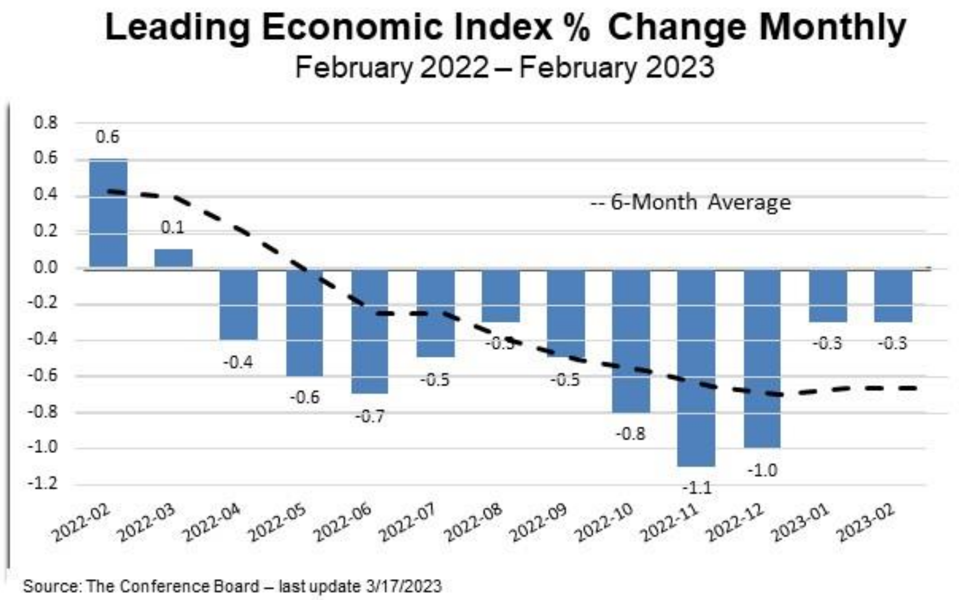
INDICATOR STATISTICS

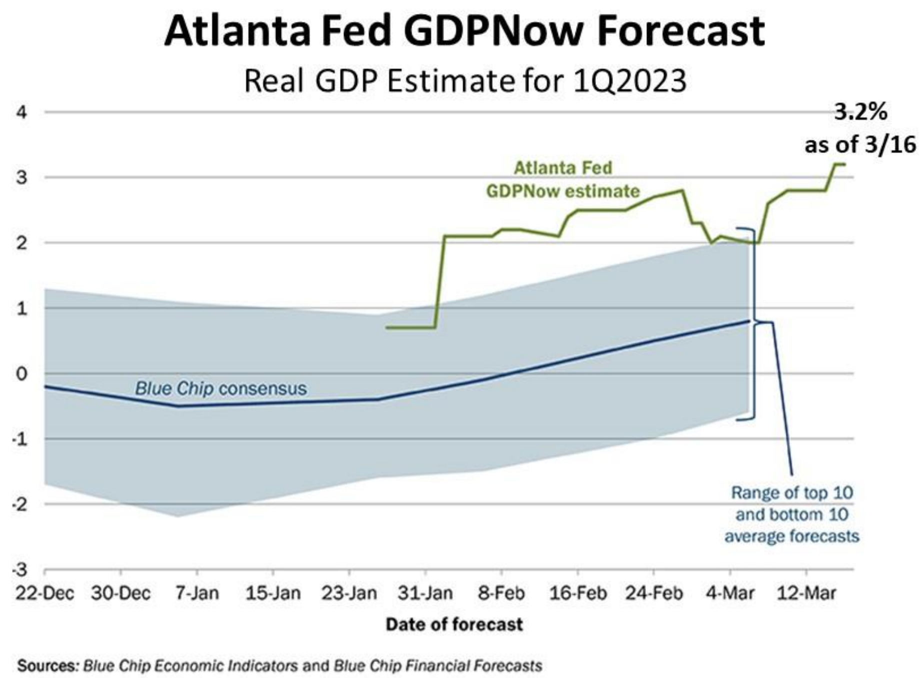
Consecutive Bearish Weeks:	4
Cycle Inception Date:	3/2/2023
Range:	23.9 - 46.7
Mean:	35.8
Bullish Weeks YTD:	8
Bearish Weeks YTD:	4
*S&P 500	0.3%
*DJIA	-1.9%
*NASDAQ	4.4%

** Percentage change during current cycle*

Delta Market Sentiment Indicator Over the Past Year




Leading Economic Index % Change Monthly
February 2022 – February 2023
-- 6-Month Average
0.6
0.1
-0.4
-0.6
-0.7
-0.5
-0.3
-0.5
-0.8
-1.1
-1.0
-0.3
-0.3
2022-02
2022-03
2022-04
2022-05
2022-06
2022-07
2022-08
2022-09
2022-10
2022-11
2022-12
2023-01
2023-02
Source: The Conference Board – last update 3/17/2023


Atlanta Fed GDPNow Forecast
Real GDP Estimate for 1Q2023
3.2%
as of 3/16
Atlanta Fed
GDPNow estimate
Blue Chip consensus
Range of top 10
and bottom 10
average forecasts
22-Dec
30-Dec
7-Jan
15-Jan
23-Jan
31-Jan
8-Feb
16-Feb
24-Feb
4-Mar
12-Mar
Date of forecast
Sources: Blue Chip Economic Indicators and Blue Chip Financial Forecasts