

Sevens Report Alpha Webinar – Bull Case vs. Bear Case (And Which One I Think Is More Compelling)

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The Bull Case:

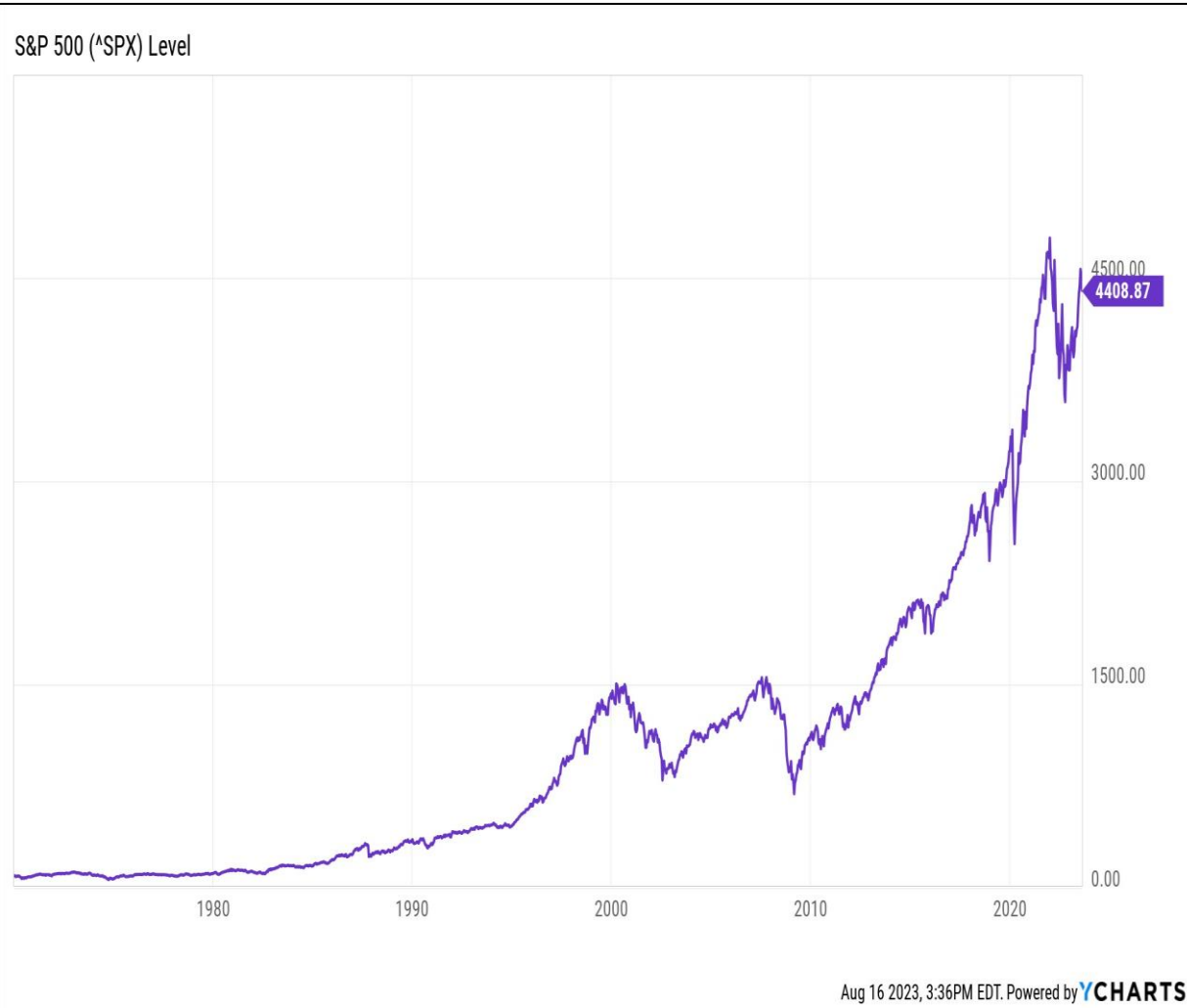
- **The Fed's going to stick the soft landing**
- **The U.S. economy and U.S. consumer are more resilient than we thought**
- **U.S. corporations remain money making machines**
- **Geo-political risks will recede.**

Bull Case: History.

How often does the market decline numerous years in a row?

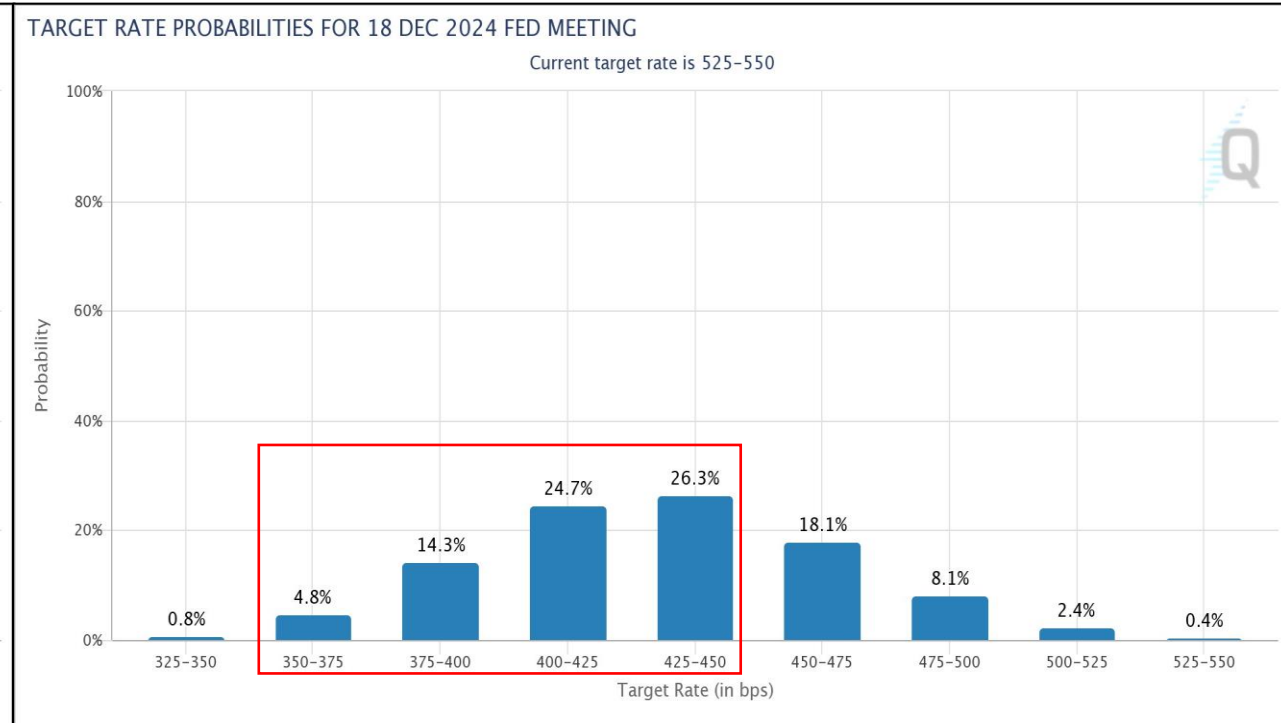
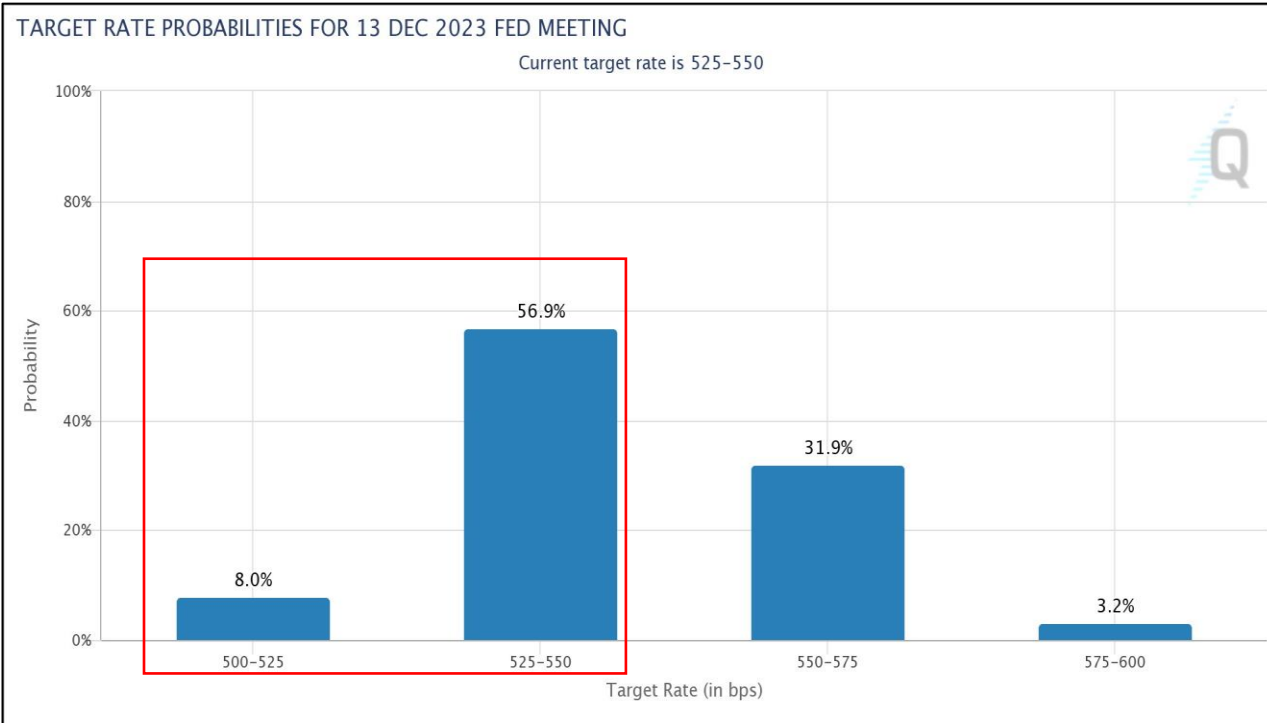
| Year | S&P 500 Yearly Return | Year | S&P 500 Yearly Return | Year | S&P 500 Yearly Return | Year | S&P 500 Yearly Return |
|------|-----------------------|------|-----------------------|------|-----------------------|------|-----------------------|
| 1970 | 4.01% | 1984 | 6.27% | 1998 | 28.58% | 2012 | 16.00% |
| 1971 | 14.31% | 1985 | 31.73% | 1999 | 21.04% | 2013 | 32.39% |
| 1972 | 18.98% | 1986 | 18.67% | 2000 | -9.10% | 2014 | 13.69% |
| 1973 | -14.66% | 1987 | 5.25% | 2001 | -11.89% | 2015 | 1.38% |
| 1974 | -26.47% | 1988 | 16.61% | 2002 | -22.10% | 2016 | 11.96% |
| 1975 | 37.20% | 1989 | 31.69% | 2003 | 28.68% | 2017 | 21.83% |
| 1976 | 23.84% | 1990 | -3.10% | 2004 | 10.88% | 2018 | -4.38% |
| 1977 | -7.18% | 1991 | 30.47% | 2005 | 4.91% | 2019 | 31.49% |
| 1978 | 6.56% | 1992 | 7.62% | 2006 | 15.79% | 2020 | 18.40% |
| 1979 | 18.44% | 1993 | 10.08% | 2007 | 5.49% | 2021 | 28.71% |
| 1980 | 32.42% | 1994 | 1.32% | 2008 | -37.00% | 2022 | -18.11% |
| 1981 | -4.91% | 1995 | 37.58% | 2009 | 26.46% | | |
| 1982 | 21.55% | 1996 | 22.96% | 2010 | 15.06% | | |
| 1983 | 22.56% | 1997 | 33.36% | 2011 | 2.11% | | |

Bull Case: History.

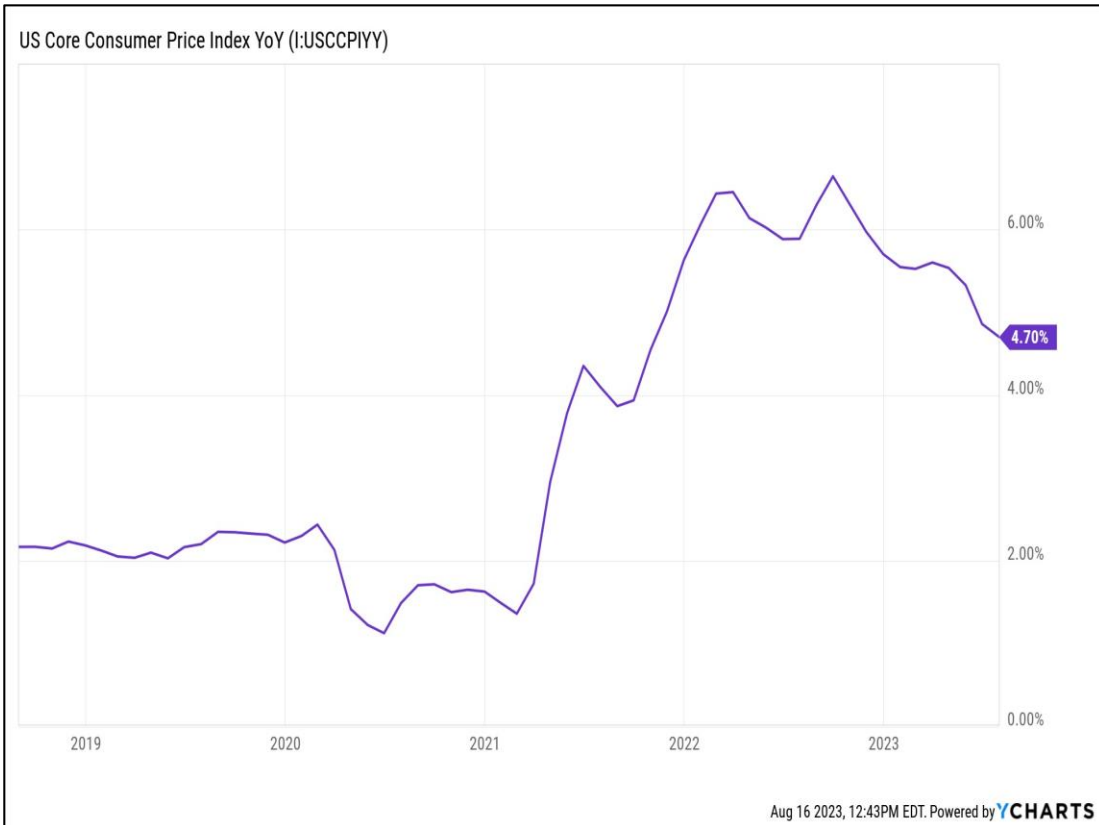


| Date | S&P 500 New Highs | Days Between | Date | S&P 500 New Highs | Days Between |
|------------|-------------------|--------------|-----------|-------------------|--------------|
| 4/27/1971 | 104.39 | | 3/24/2000 | 1527.46 | |
| 2/8/1972 | 104.74 | 287 | 5/30/2007 | 1530.23 | 2623 |
| 1/11/1973 | 120.24 | | 3/6/2013 | 1541.46 | 2107 |
| 7/17/1980 | 121.44 | 2744 | 5/19/2015 | 2127.83 | |
| 11/28/1980 | 140.52 | | 7/12/2016 | 2152.14 | 420 |
| 11/9/1982 | 143.02 | 711 | 1/24/2018 | 2837.54 | |
| 8/25/1987 | 336.77 | | 8/9/2018 | 2853.58 | 197 |
| 7/26/1989 | 338.05 | 701 | 2/19/2020 | 3386.15 | |
| 2/2/1994 | 482 | | 8/18/2020 | 3389.78 | 181 |
| 2/14/1995 | 482.55 | 377 | 1/3/2022 | 4796.56 | 503 |

Bull Case: The main drivers of the 2022 decline are being reversed.
Fed is done, or nearly done, with rate hikes. Meanwhile, rate cuts are coming next.



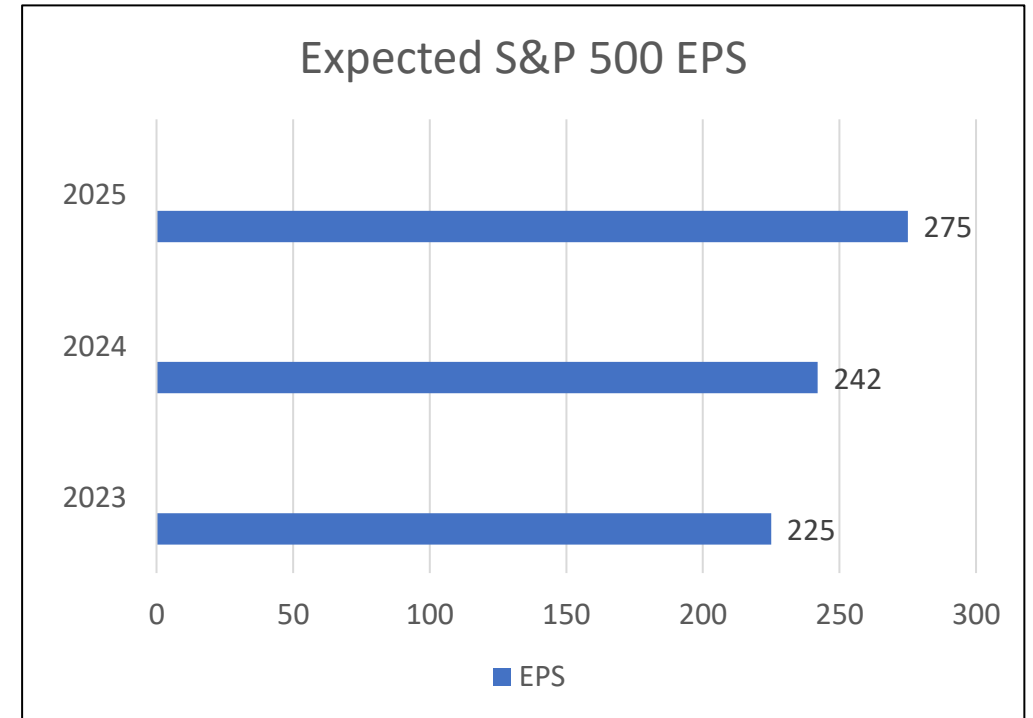
Bull Case: The main drivers of the 2022 decline are being reversed.
Inflation is receding and the coming drop in housing and shelter in CPI will finish the job.



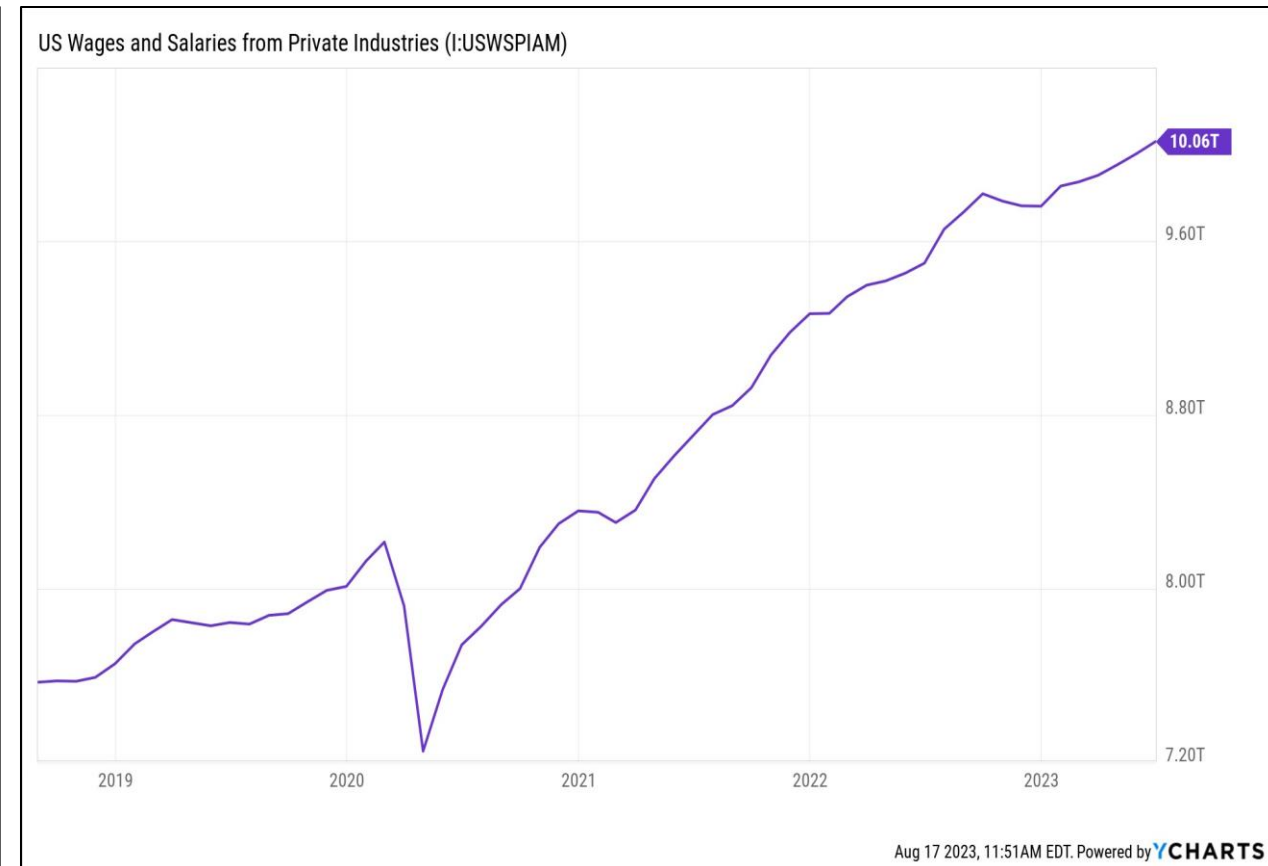
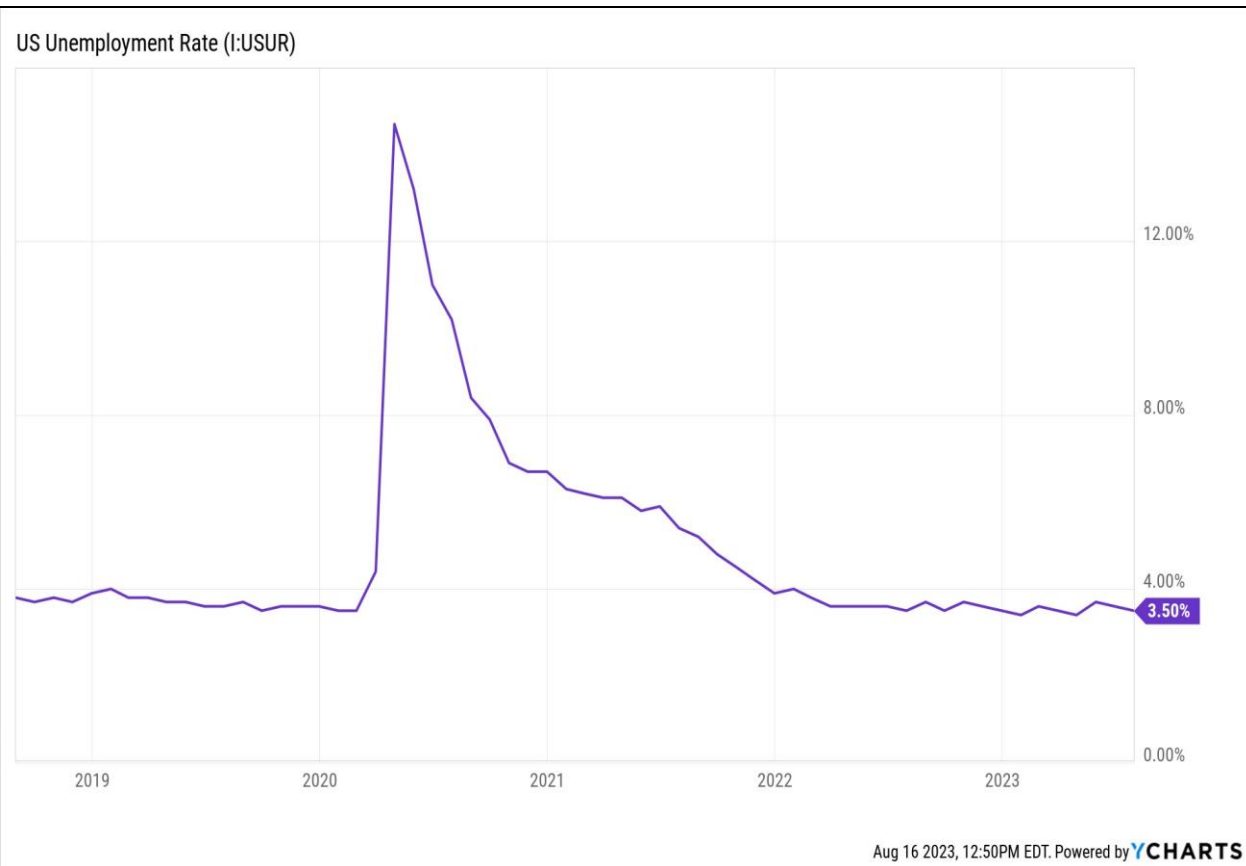
Bull Case: The main drivers of the 2022 decline are being reversed.

Earnings declines are over.

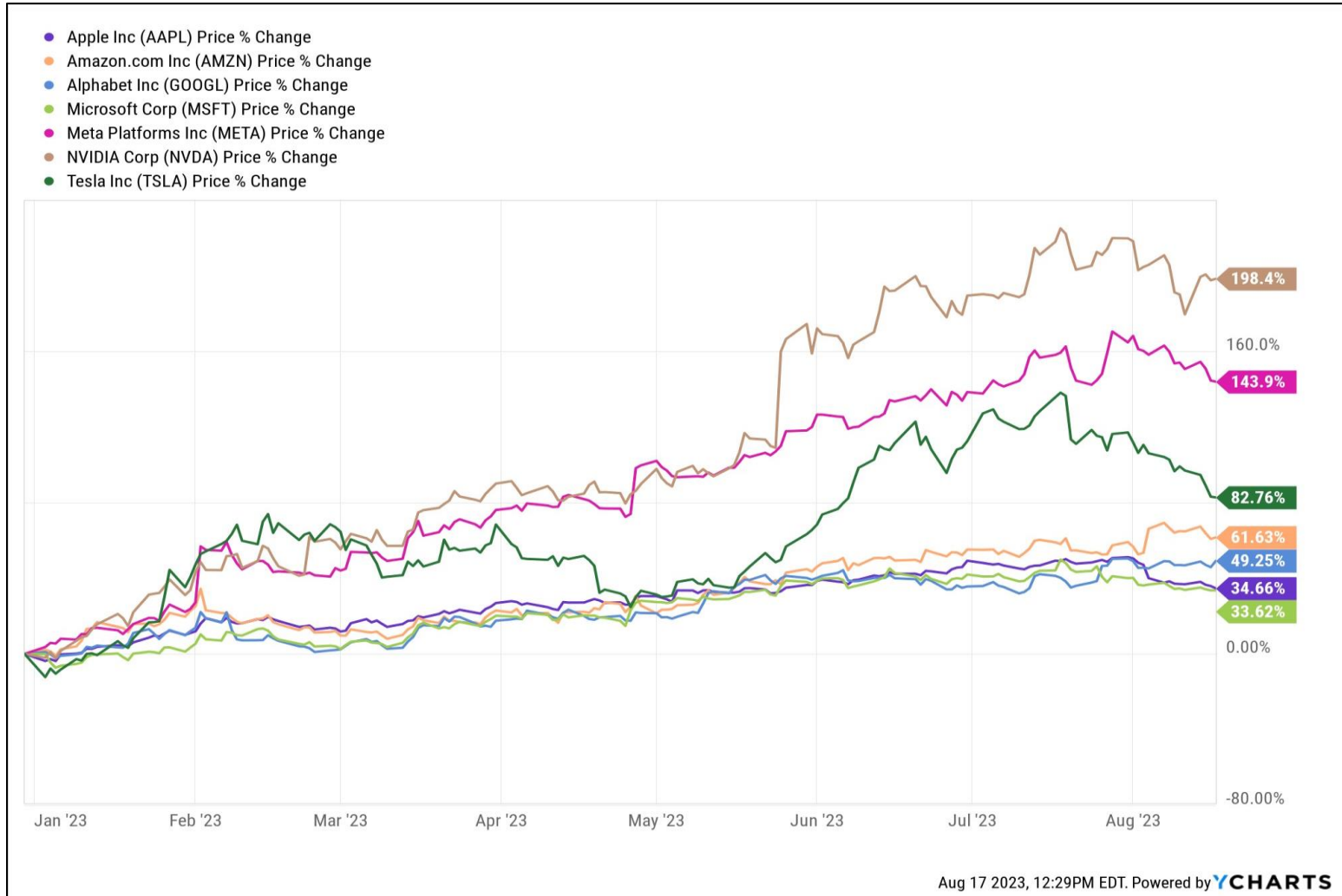
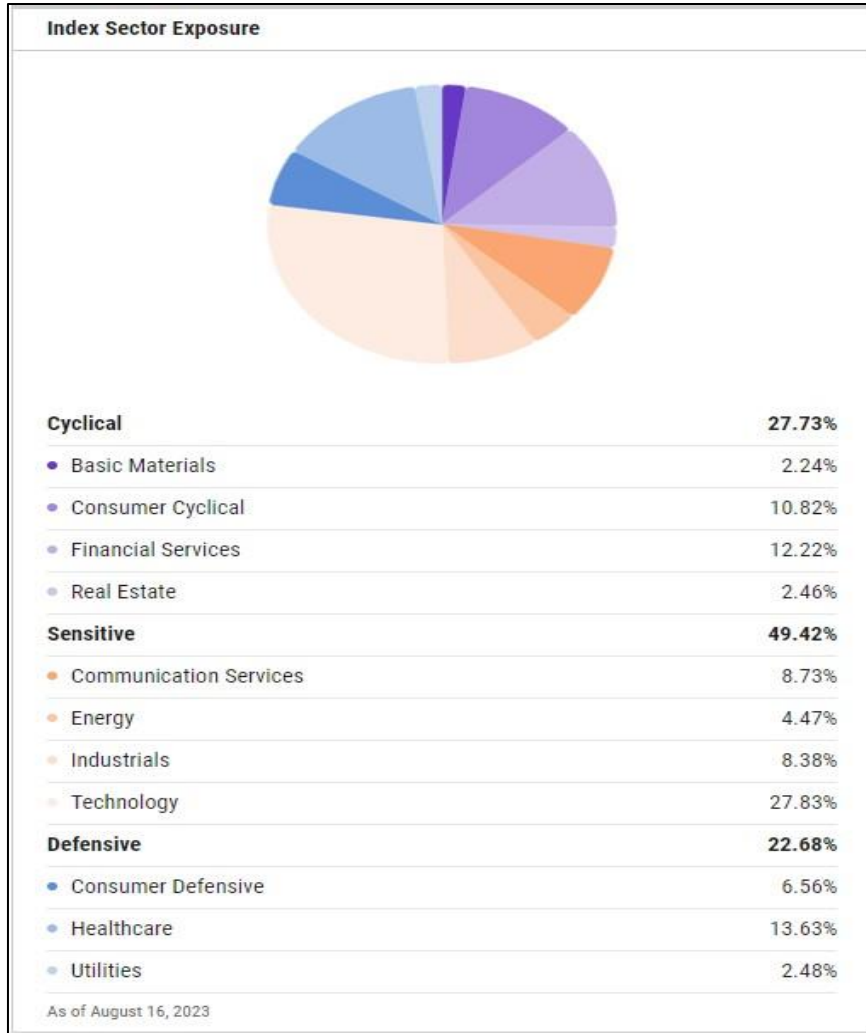
| Expected S&P 500 EPS For: | Expected EPS |
|---------------------------|--------------|
| 2023 | \$225 |
| 2024 | \$242 |
| 2025 | \$275 |



Bull Case: The consumer is much, much stronger than anyone appreciated.



Bull Case: AI is a unique phenomenon, that pushes multiples higher based on the composition of the S&P 500.



Bull Case: De-globalization is ending.

U.S./China relations set to improve:

- Biden Says US-China Relations Set to Improve ‘Very Shortly’ – Bloomberg, 5/21/2023.
- Xi, Blinken agree to stabilize US-China relations in Beijing talks – Reuters, 6/19/2023.
- Yellen’s latest trip helps set a new normal for the U.S.-China relationship – CNBC, 7/10/2023.

Russia’s disastrous Ukraine invasion underscores just how costly conflict is for economies:

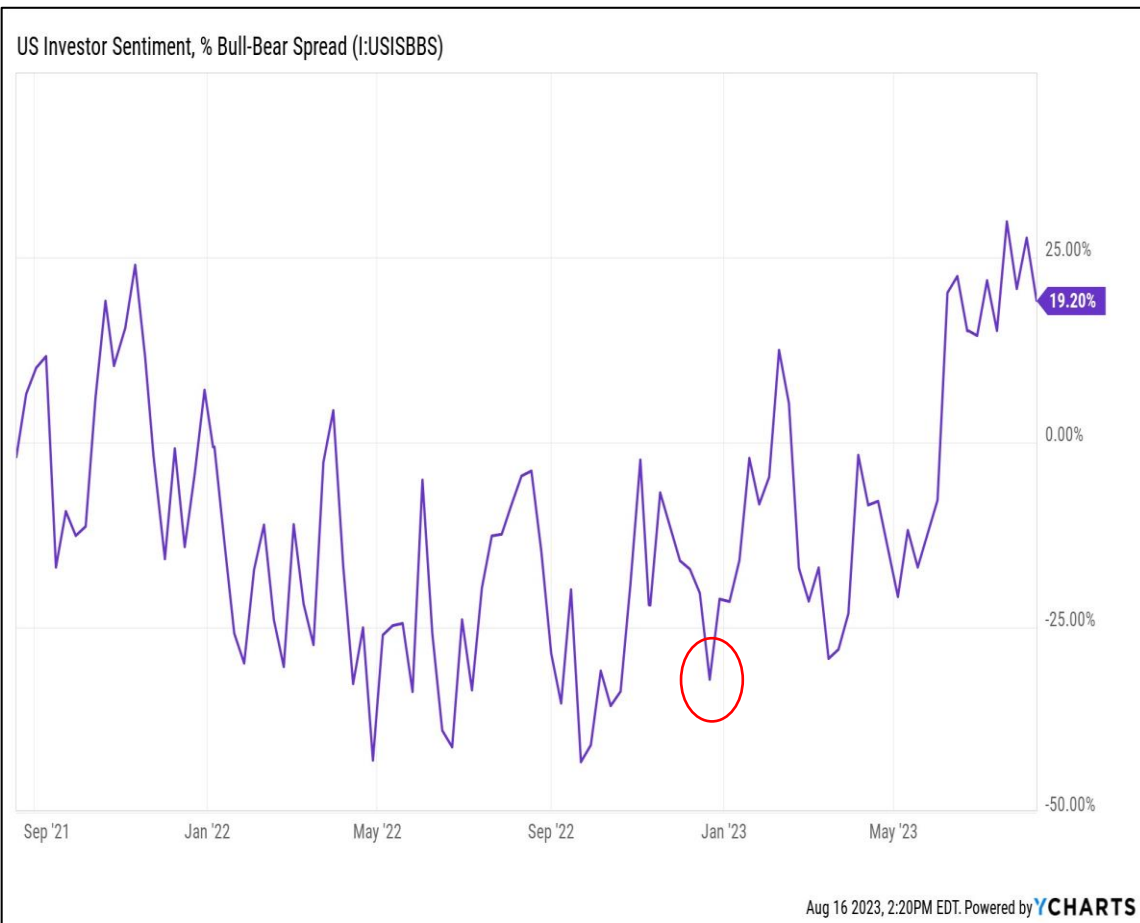
Russia’s Invasion of Ukraine and Cost-of-Living Crisis Dim Growth Prospects in Emerging Europe and Central Asia – The World Bank, 4/06/2023.

Consequences of the War in Ukraine: The Economic Fallout – Rand Corporation, 3/07/2023.

The Bear Case:

- **We aren't wrong, we're just early!**
- **The Fed rate hikes will cause a recession, just later than initially expected.**
- **The factors that have driven the rally, namely sentiment and valuation, are now liabilities.**
- **Personal spending has supported the economy, but we're already seeing signs of "downshifting."**
- **It isn't different this time, and a looming recession will hurt the economy broadly and corporate earnings more specifically.**

Bear Case: Sentiment and valuation were keys to 2023 rally, but both removed.



S&P 500 PE Ratio



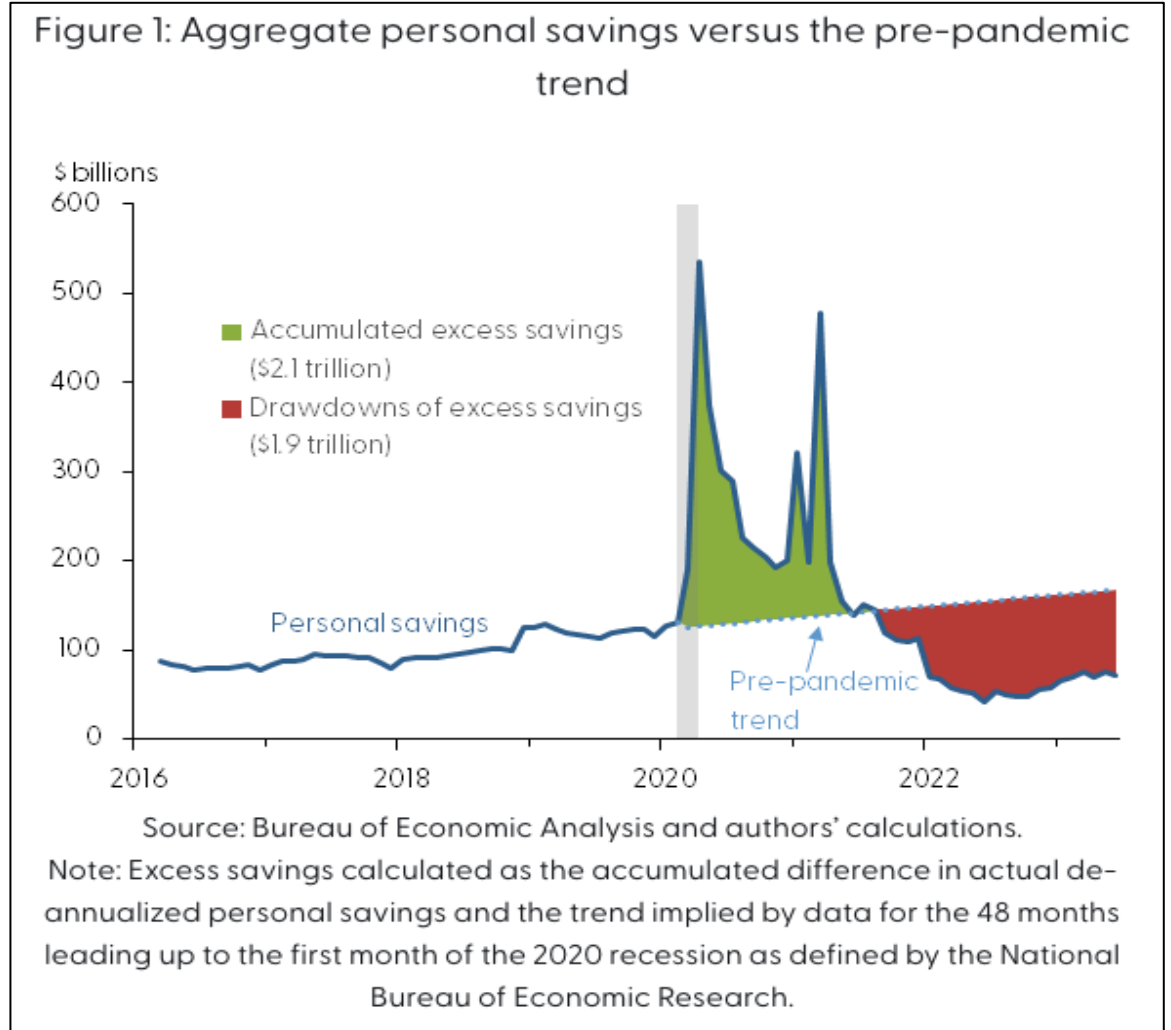
Bear Case: Fed rate hikes now starting to matter.



Bear Case: COVID stimulus provided a strong buffer to slowdown, but it's quickly eroding.

The San Francisco Federal Reserve estimates U.S. excess savings have fallen to around \$500 billion as of March 2023, from around \$2.1 trillion in August 2021.

Updated estimates suggest that households held less than \$190 billion of aggregate excess savings by June, and they estimate that these excess savings are likely to be depleted during the third quarter of 2023.

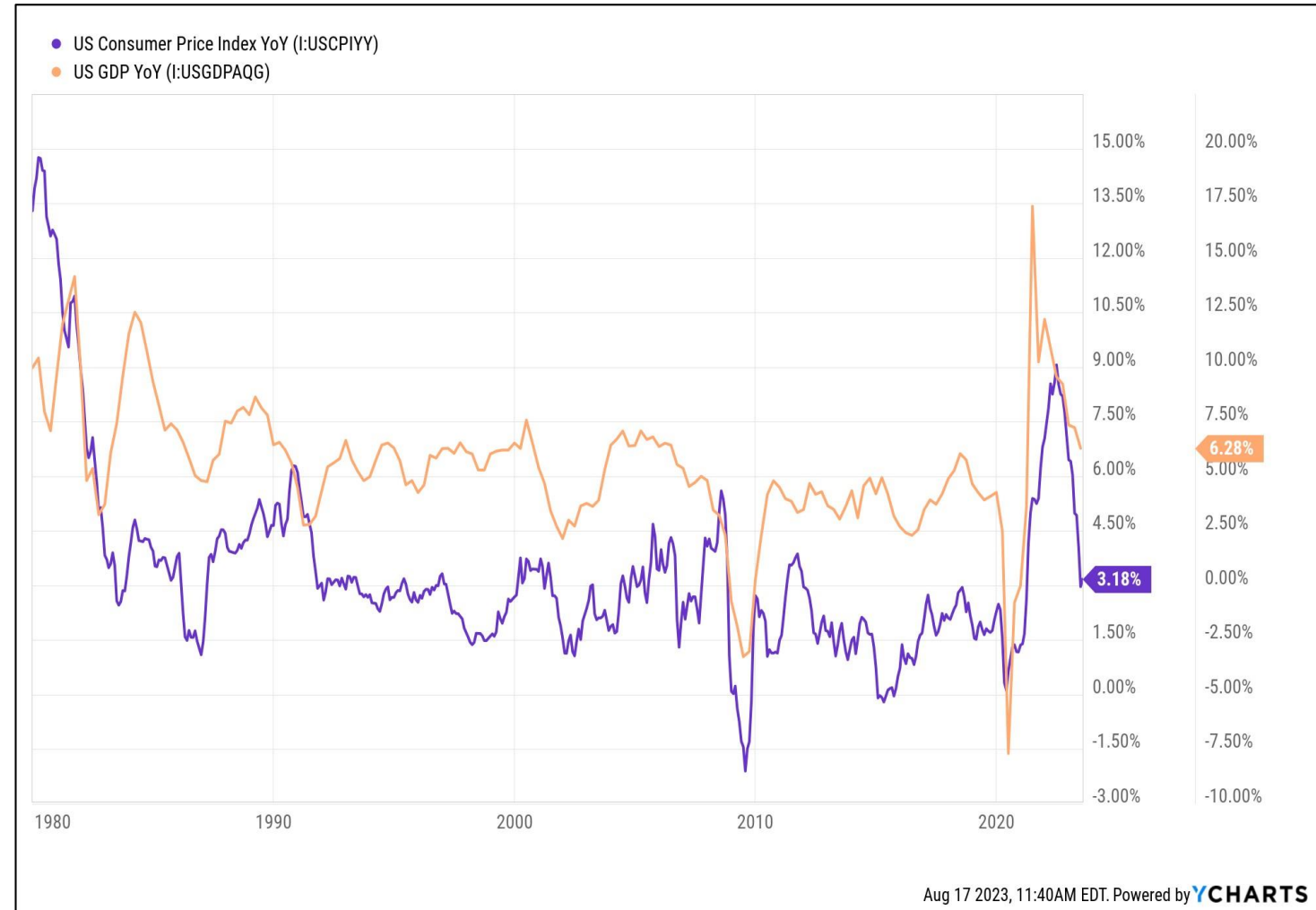


Bear Case: Bull argument really rests on Immaculate Disinflation (something that's never actually happened).

If inflation drops as growth slows, Fed will cut rates, but it'll be too late (this is a classic “too late” response from Fed).

If inflation doesn't drop, then the Fed keeps hiking or keeps rates higher for longer (which sends yields up, which is what's pressuring stocks lately). Recession eventually occurs.

Either way, the only way “out” for stocks is if inflation falls but growth doesn't – not a good habit to bet on something that's never happened before.



Which Argument Do I Think Is More Compelling?

- Over the medium and longer term, the bear case.
- Here's why:
 - Experience: The bull argument is very similar to what I heard back in '00 and '07.
 - Time: The longer rates stay high, the greater my conviction that the bear case will prove true.
 - Consumer spending: We are already seeing signs of “down shifting” and that's usually a precursor to curtailing spending all together.
 - Inflation: Damage is already done. Prices are not returning to pre-pandemic levels. Best that can be hoped for is mild price relief, but most things are much higher in price than before, and wage gains aren't keeping up.
 - Credit: 7% mortgage rates, 8% car & boat rates are an issue. For now, it's being blunted but previously low rates, but they won't last forever. Rates and prices have an inverse relationship, I don't think that changed.
 - **Now, while I find the bear argument more compelling, don't take that to mean I think the market is going to crash. I do not. But, I also do not think that new highs are coming anytime soon, and the next 10% in the market is likely lower, not higher.**
 - However, the longer-term attractiveness of stocks remains, especially at better entry points.

Alpha Strategies for Both Scenarios

If you agree with the Bull argument:

- No Landing Scenario. 7/25/23
 - JPMorgan Active Value ETF (JAVA), Avantis U.S. Small Cap Value ETF (AVUV), iShares Broad USD High Yield Corporate Bond ETF (USHY)
- AI Primer Part Two. 6/13/23
 - Global X Artificial Intelligence & Technology ETF (AIQ), First Trust Cloud Computing ETF (SKYY), Defiance Quantum ETF (QTUM), TrueShares Technology, AI, and Deep Learning ETF (LRNZ), WisdomTree Artificial Intelligence and Innovation Fund (WTAI)
- What Would Outperform If Markets Turn Around? 2/23/22
 - SPDR FactSet Innovative Technology ETF (XITK), Vanguard Consumer Discretionary ETF (VCR), iShares Broad USD High Yield Corporate Bond ETF (USHY), SPDR Blackstone Senior Loan ETF (SRLN)

If you agree with the Bear argument:

- Utilizing High Returns on Cash. 5/31/23
 - iShares 0-3 Month Treasury Bond ETF (SGOV), SPDR Bloomberg 1-3 Month T-Bill ETF (BIL), Invesco Treasury Collateral ETF (CLTL), SPDR Bloomberg 3-12 Month T-Bill ETF (BILS), PGIM Ultra Short Bond ETF (PULS).
- Opportunity in Long Bonds. 1/24/23
 - SPDR Portfolio Long Term Treasury ETF (SPTL), PIMCO Long-Term Credit Bond Fund (PTCIX), VanEck Long Muni ETF (MLN).
- Sectors that Outperformed During Recent Recessions. 7/12/22
 - Vanguard Health Care ETF (VHT), iShares U.S. Healthcare Providers ETF (IHF), Vanguard Consumer Staples ETF (VDC), Invesco Dynamic Food and Beverage ETF (PBJ).