Neox Capital

Rebounding from Recession

A short historical view of markets’ path out of recession

Table of contents

Recession and correction recoveries

In this article we are taking a brief look at recessions and recoveries over time.

Throughout history, the stock market has demonstrated an incredible ability to recover from periods of volatility and downturns. While there will always be periods of uncertainty and volatility – Mr. Market is quite manic depressive - the stock market has shown that it is resilient and that recoveries are always possible.

Currently the mood is starting to shift towards expectations of lower-than-expected inflation and thereby a possible slower pace of interest hikes.

The first page (Graph 1) show the duration of bull and bear markets as well as the recovery pace. Duration of recessions are shown as grey columns in the graph. We are using US data as that is the only available market data with such a long history.

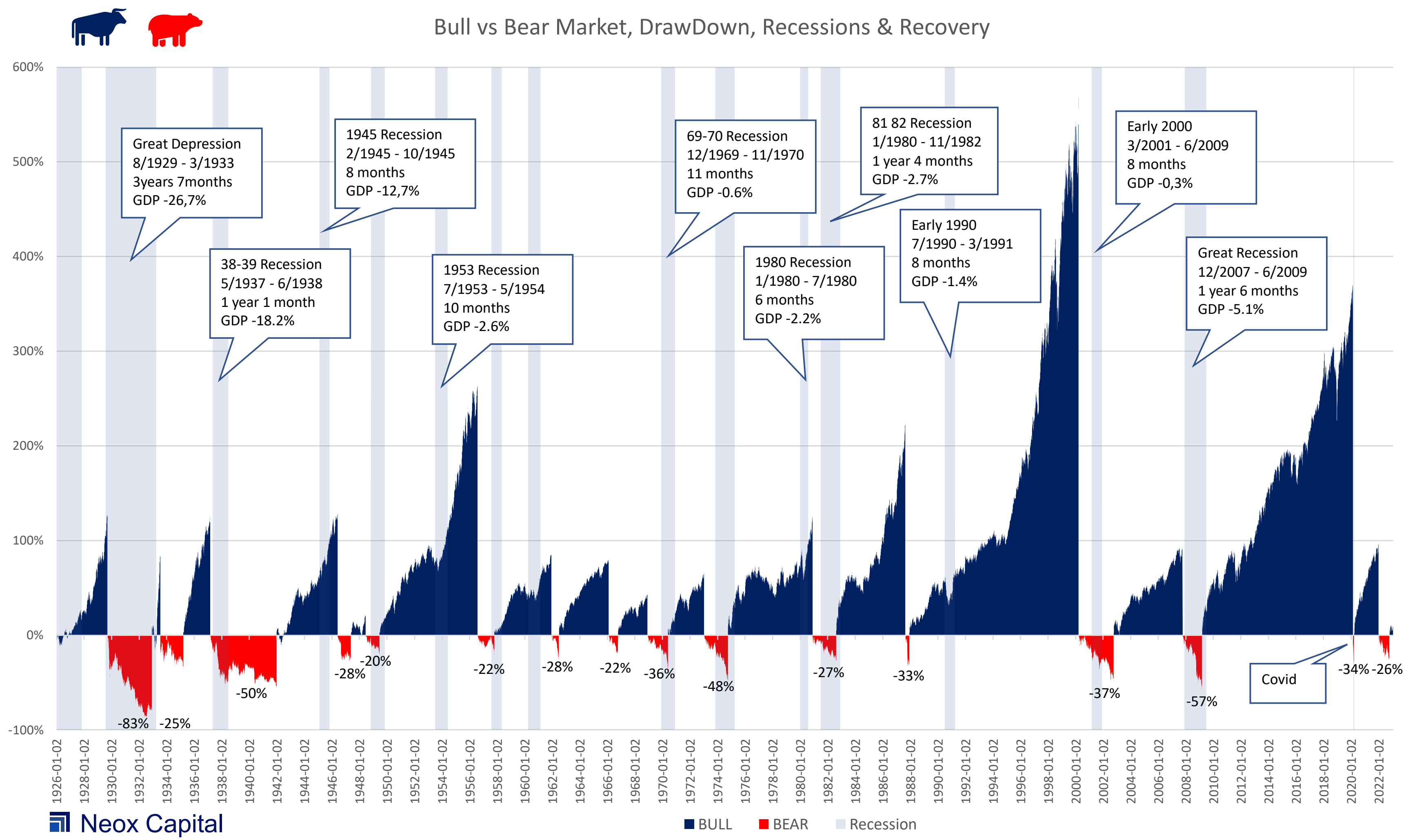
The recovery after severe drawdowns and recessions have historically been swift.

Covid 19 is the shortest recession in history. The drop in market prices ended less than a month after start. Market participants quickly realised that the collapse in economic activity was self-imposed and expected a swift rebound in growth.

Stock markets are not always down during a recession. Stock markets can rise or fall during a recession depending on the state of the economy. Factors such as the availability of capital, consumer confidence, and the performance of specific companies or sectors can have an impact on stock prices. Additionally, governments can intervene in the markets by enacting policies that affect the markets, such as increasing or decreasing interest rates.

If history repeats itself, recoveries have followed declines, and long-term investors may benefit from the recovery.

Copyright © Neox Capital, 2023

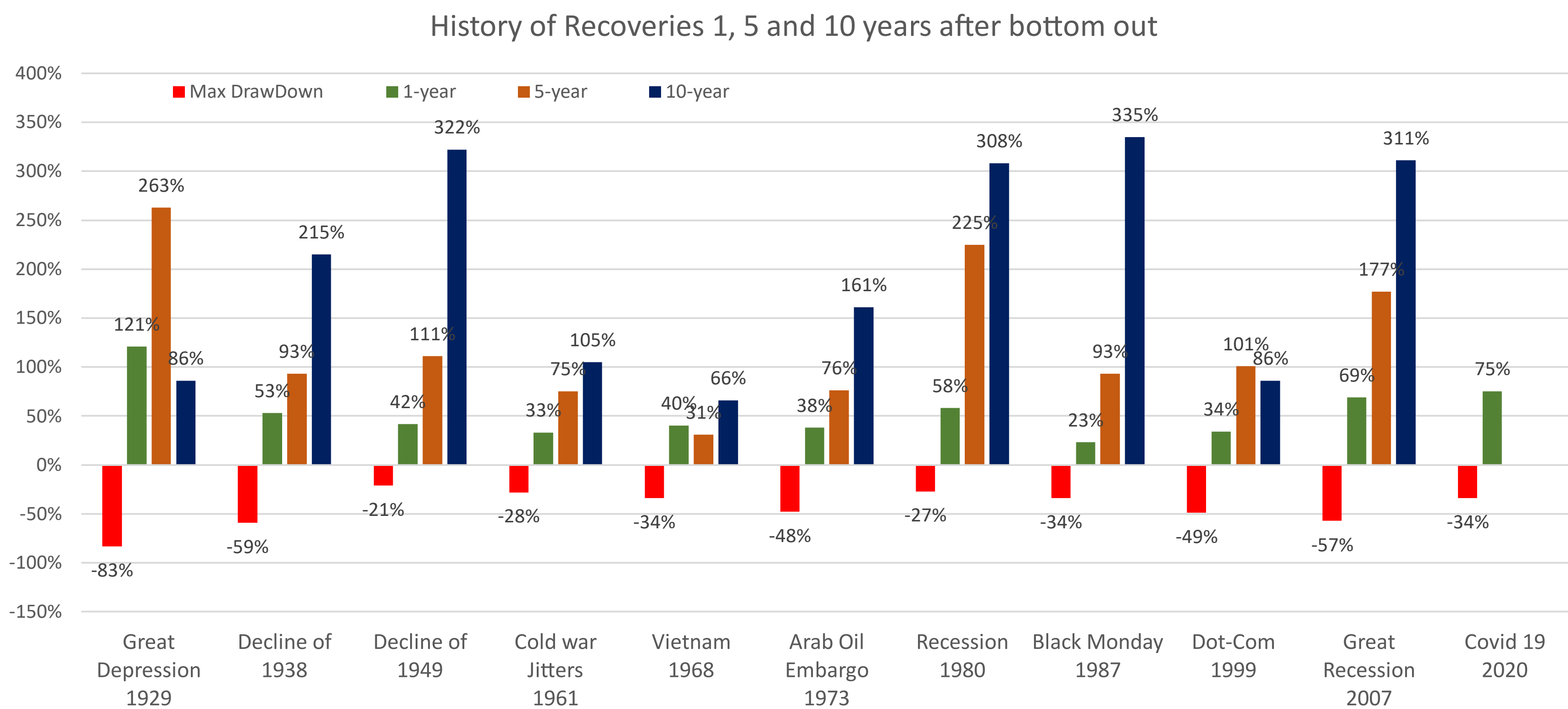


Graph 1

Source: FactSet. Daily data from 3 January 1928 through 30 January 2023. Bear market is defined as the period from a peak to trough, with at least a 20% decline in the S&P 500 index price. Data in USD. Past performance is no guarantee of future results. Max drawdown is the largest drawdown (peak-to-trough) within each calendar year. Benchmark S&P 500.

Copyright © Neox Capital, 2023

The graph below show selected market drawdowns and subsequent recoveries 1, 5 and 10 years after the market bottomed out. Interesting to note is the Dot-Com bubble recovery that increased 86% after 10 years even though the great recession between 2007 and 2009 was within those 10 years.



Graph 2

Source: FactSet. Daily data from 3 January 1928 through 30 January 2023. Bear market is defined as the period from a peak to trough, with at least a 20% decline in the S&P 500 index price. Data in USD. Past performance is no guarantee of future results. Max drawdown is the largest drawdown (peak-to-trough) within each calendar year. Benchmark S&P 500

Copyright © Neox Capital, 2023

The table below lists the 15 recessions recorded during the last 100 years or so. The average length of recessions in modern times after WW2 is about 10 months.

There is a lot of confusion about what makes up an official recession and how long they typically last. A common definition is: "significant decline in economic activity that is spread across the economy and lasts more than a few months“. It interprets this definition using three criteria -- depth, diffusion, and duration -- in a somewhat interchangeable manner. While a recession needs to meet each factor to some degree, there are extreme cases where the severity of one component can partially offset the lack of another.

An example is the economic decline in early 2020 due to Covid-19 that was so severe and widely dispersed that it was classified it as a recession despite a very short duration.

Name	Period	Duration months	GDP Decline
Great Depression (Banking panic, collapse in money supply)	1929 08 - 1933 03	43	-26.70%
Recession 37 - 38 (Tight monetary policy, declining business profits)	1937 05 - 1938 06	13	-18.20%
Recession of 1945 (Decline in gov. spending)	1945 02 - 1945 10	8	-12.70%
Recession of 1949 (Monetary tightening)	1948 11 - 1949 10	11	-1.70%
Recession of 1953 (Post Korean War inflation)	1953 07 - 1954 05	10	-2.60%
Recession of 1958 (Monetary policy tightening)	1957 08 - 1958 04	8	-3.70%
Recession of 1960 - 1961 (FED raising interest rates)	1960 04 - 1961 02	10	-1.60%
Recession of 1969 - 1970 (Fiscal tightening)	1969 12 - 1970 11	11	-0.60%
Oil Crises recession (OPEC quadrupling prices)	1973 11 - 1975 03	16	-3.20%
1980 recession (FED raising interest rates dramatically)	1980 01 - 1980 07	6	-2.20%
1981 - 82 recession (Tight monetary policy to control inflation)	1981 07 - 1982 11	16	-2.70%
Early 1990s recession (Inflation, 1990 oil price shock, consumer pessimism)	1990 07 - 1991 03	8	-1.40%
2001 recession (Dot-com and 9/11 attack)	2001 03 - 2001 11	8	-0.30%
Great recession (Subprime mortage crises - global financial crises)	2007 12 - 2009 07	18	-5.10%
Covid-19 recession	2020-02 - 2020 04	2	-19.20%

Table 1

Copyright © Neox Capital, 2023

The graph below depict development since 1926 showing downturns, recovery and price increases. The data is shown in logarithmic scale. The original data is super imposed in Original Data graph.

Graph 3

As this graph is displaying nearly 100 years of data, we are using **logarithmic scale** as it is a way of displaying numerical data over a very wide range of values in a compact way—typically the largest numbers in the data can be hundreds or even thousands of times larger than the smallest numbers.

Copyright © Neox Capital, 2023

Who are the likely post-recession winners?

The post-recession winners can be broadly categorized into three groups:

1**. Large multinational companies**: These large companies have been able to take advantage of globalization and the digital revolution to create new opportunities for growth and profitability. They have also been able to benefit from the low-interest rate environment which has allowed them to borrow money cheaply. After 2009 bottom out until 2015 large caps outperformed with 35%-units.
2**. Technology companies**: Major technology companies have seen tremendous success over the past decade as the digital revolution has taken hold. These companies have been able to take advantage of new technologies to create innovative products and services that have changed the way we live. After 2009 bottom out until 2015 large caps outperformed with 135%-units.
3. **Small businesses**: Small businesses have been able to take advantage of the post-recession economic environment to launch and grow quickly. The low-interest rate environment has allowed smaller businesses to borrow money more easily and the digital revolution has helped them access new markets. After 2009 bottom out until 2015 large caps outperformed with 50%-units.

Companies that master the subtle balance between cutting costs to survive today and investing to grow tomorrow seem to prosper after a recession. A subset of this group that deploys a specific combination of defensive and offensive moves has the highest probability of standing apart from the crowd. These companies reduce costs selectively by focusing more on operational efficiency than their competitors do, even as they invest relatively expansively in the future by spending on marketing, R&D, and new assets.

The challenge this time is that the inflation is primarily supply driven. This means that it is quite difficult to curb with higher interest rates, as this will mainly affect the demand side. It will be a rare feat if Central Banks can pull off a soft landing, and the jury is still out on that.

Interestingly, this coming slowdown in economic growth is very well understood by investors and therefore, to a large extent already priced into the market. This can for example be seen in increased cash positions. So given that there will be no serious policy error by the major central banks, there is plenty of dry powder waiting to be used if the soft landing actually happens.

So, what lies ahead? In 2023, the stock market is expected to remain strong, with economies continuing to recover, and corporate profits and dividends increasing. However, there are some concerns over inflation and rising interest rates. This could put a damper on stock prices, but the market should remain relatively healthy, and the interesting question is where we are a few years ahead. If history repeats itself there could be some interesting years coming up.

Peter Sjoeholm, CEO

Copyright © Neox Capital, 2023

Disclaimer

This document is intended as general information only.
This document has been prepared without taking into account your objectives, financial situation or needs. Local taxes, withholding taxes, VAT, transaction fees, custodian fees and double tax treaties have not been taken into account. You should consider these matters before acting on any information. If investors are unsure if this product is suitable for them, they should seek advice from a financial adviser. Persons into whose possession this document may come are required to inform themselves about and to comply with any relevant restrictions. This does not constitute an offer or solicitation by anyone in any jurisdiction in which such an offer is not authorized or to any person to whom it is unlawful to make such an offer or solicitation. Persons interested in any of Neox Capital's products or services should inform themselves as to (i) the legal requirements in the countries of their nationality, residence, ordinary residence or domicile; (ii) any foreign exchange controls and (iii) any relevant tax consequences. The Neox Capital's services are available only in jurisdictions where its promotion and sale is permitted. Where securities are mentioned in this document, they do not necessarily represent a specific portfolio holding and do not constitute a recommendation to purchase, hold or sell. No responsibility or liability is accepted for any errors or omissions or misstatements however caused.

Please note that past performance is no guarantee of future results.

Data provided by FactSet.

© Neox Capital, 2023