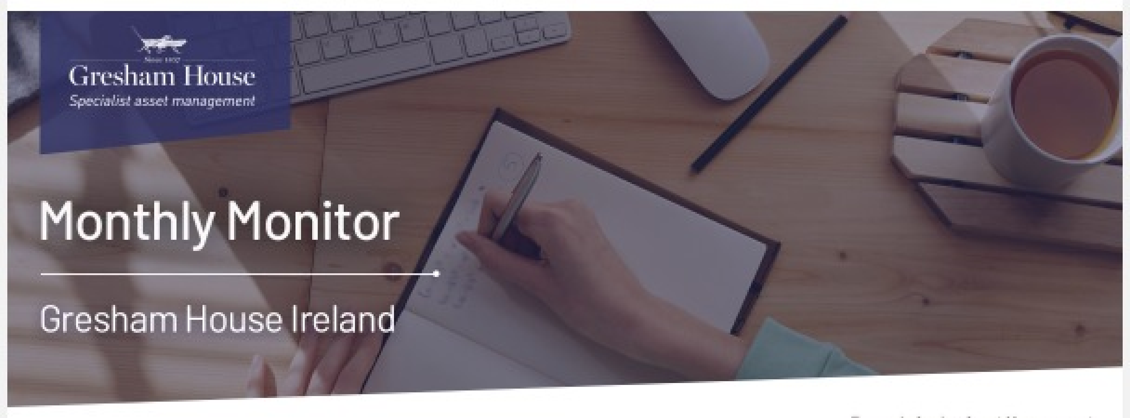


Formerly Appian Asset Management

**Monthly Monitor** | July 2022

## Uncertainty has caused the third greatest derating of equities

**The first half of 2022 has proved an extremely negative period for global equity markets. The sell-off of the last six months has been exceptional and has only been surpassed during periods of extreme market stress, recalling events in 1974, the TMT crash of 2000, the global financial crisis (GFC) and the European sovereign crisis.**

The fall has resulted in the third largest valuation derating of global equities in the last fifty years. On a price-to-earnings basis, the global equity market has derated by 38% over the last year, a derating only outstripped by the stock market crash of the early 1970s and the GFC, where it suffered a 54% and 44% derating respectively.

### One-year percentage change in P/E multiple of the global equity market


*Source: Refinitiv Datastream, 2 July 2022*

A high level of uncertainty is the one feature of commonality with other historic periods where equity markets have derated. The 1970's brought a period of double-digit inflation in the US coupled with oil price shocks, and a devaluation of the US Dollar as the gold standard was abandoned. The GFC was different, as the bursting of a US housing bubble threatened the global financial system.

Today's environment resonates more with the inflationary bear market of the 1970s than with the GFC, which delivered a deflationary bear market. The 1970s recession also saw the financial system experience limited contagion unlike the GFC; which we believe will also be this case in this cycle.

As inflation rates continue to hit highs, central bank rhetoric continues to get more hawkish and the odds of a recession increase. Equity markets don't react well to uncertainty and that's what we are living through today.

**When will inflation moderate? How high are interest rates set to go and what type of recession may be on the horizon? These are key uncertainties roiling markets today.**

The question for investors is what to do during this uncertainty and related market decline. Looking back at the other two great deratings in history, the equity market recoveries following each of the deratings was just reward for tolerating the uncertainty.

**Global Equity returns after 1973/74 derating finished:**

- 2-year return 52%
- 5-year return 96%

**Global Equity returns after 2008/2009 derating finished:**

- 2-year return 98%
- 5-year return 135%

**The catalyst for both was a removal of uncertainty.**

The 2009 GFC recovery came as markets realised governments and central banks were going to stand behind the financial system. The 1970's low came as inflation peaked, allowing central banks to ease policy.

It's looking like today's market is in line with the 1970's and a turn in the inflation numbers is needed to bring certainty back and allow markets to recover. In previous cycles, markets recovered before economic data improved or earnings bottomed. We believe the same will be true this time.

Please visit our website for further information. The latest views and insights from the team can be found here.

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