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COVID-19 and Sector Performance: Lessons from Past Crises

Daniel Ung
CFA, CAIA, FRM, Head of Quantitative Research & Analysis, SPDR ETF Model Portfolio Solutions, State Street Global Advisors

Anthi Tsouvali
State Street Global Markets

Shankar Abburu
Quantitative Research & Analysis, SPDR ETF Model Portfolio Solutions, State Street Global Advisors

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Global equity markets faltered in March but have recovered most of their losses since. In spite of this, institutional investors remain doubtful about the strength and the durability of the rally and have so far shown a lack of conviction.

The scepticism had already started at the beginning of the year when investors questioned where in the business cycle the global economy was. A variety of other factors exacerbated the scepticism, including the trade dispute between the US and China, the uncertainty over the upcoming US elections and the COVID-19 pandemic. For this reason, investors mostly stayed on the sidelines, which explains why the State

Street Global Markets proprietary indicator shows that investor allocation to cash has remained at remarkably high levels.

All bear markets have different catalysts and no two crises are ever the same. Nevertheless, it is worthwhile to examine whether any lessons can be drawn from previous crises to inform the trajectory of the present (see Figure 1). To do this, we examined the four worst equity bear markets and performance turning points (peaks and troughs) and identified both the outperformers and underperformers, from the perspective of both performance and fundamentals.

Figure 1: Last four severe bear markets

	Crisis Start Date	Trough Date	Peak After Trough	Crisis End Date
Crisis 1 (Iranian Revolution)	Nov 80	Jun 82	Sep 82	Aug 82
Black Monday	Aug 87	Oct 87	Apr 89	Dec 87
Dot Com	Mar 00	Aug 02	Sep 06	Oct 02
GFC	Oct 07	Jan 09	Mar 11	Mar 09

Source: State Street Global Markets, Bloomberg Finance L.P. Excluded 1990s bear market. Due to the brevity of that bear market, we were unable to draw any meaningful conclusions. Past performance is not a reliable indicator of future returns.

Analysis of Past Crises

The main findings are:

- Before market peak: Before reaching market peak, **the Industrials sector demonstrated consistent outperformance during three out of four previous crises, up to 12 months before the peak** (see Figure 2). This is somewhat surprising as conventional wisdom suggests that economically sensitive sectors, such as Industrials, have often rallied in anticipation of economic recovery.
- Peak to trough: Once the market started floundering after the peak, **Consumer Staples trumped all other sectors and delivered a consistent level of outperformance in all crises except for Black Monday.**
- Trough to previous market peak: Immediately after the trough, **Consumer Discretionary appears to be a winner across all four crises,** as earnings improved quickly.

Share

Figure 2: Performance in the run-up to market peak before the trough

	Avg. Returns (%)				Avg (%)	Avg. EPS % change				Avg (%)
	Crisis 1	Black Monday	Dot Com	GFC		Crisis 1	Black Monday	Dot Com	GFC	
Communication	5	7	-4	-4	1	0	-17	2	-1	-4
Cons. Discr.	3	-3	3	0	1	-9	-5	7	5	0
Cons. Staples	7	0	5	8	5	1	0	-11	3	-2
Energy	-7	-7	-1	-2	-4	12	-38	63	13	13
Financials	-1	0	-3	-3	-2	5	18	37	1	15
HealthCare	8	1	11	6	6	8	20	4	-3	7
Industrials	10	3	6	0	5	-35	-2	-5	-4	-11
Info Tech	2	-1	-4	-5	-2	-3	4	30	7	10
Materials	1	2	-4	-2	-1	17	112	3	-2	32
Utilities	4	1	6	3	4	5	-8	-2	-5	-3

Source: State Street Global Markets, Bloomberg Finance L.P., FactSet, as of 20 July 2020. Past performance is not a reliable indicator of future returns.

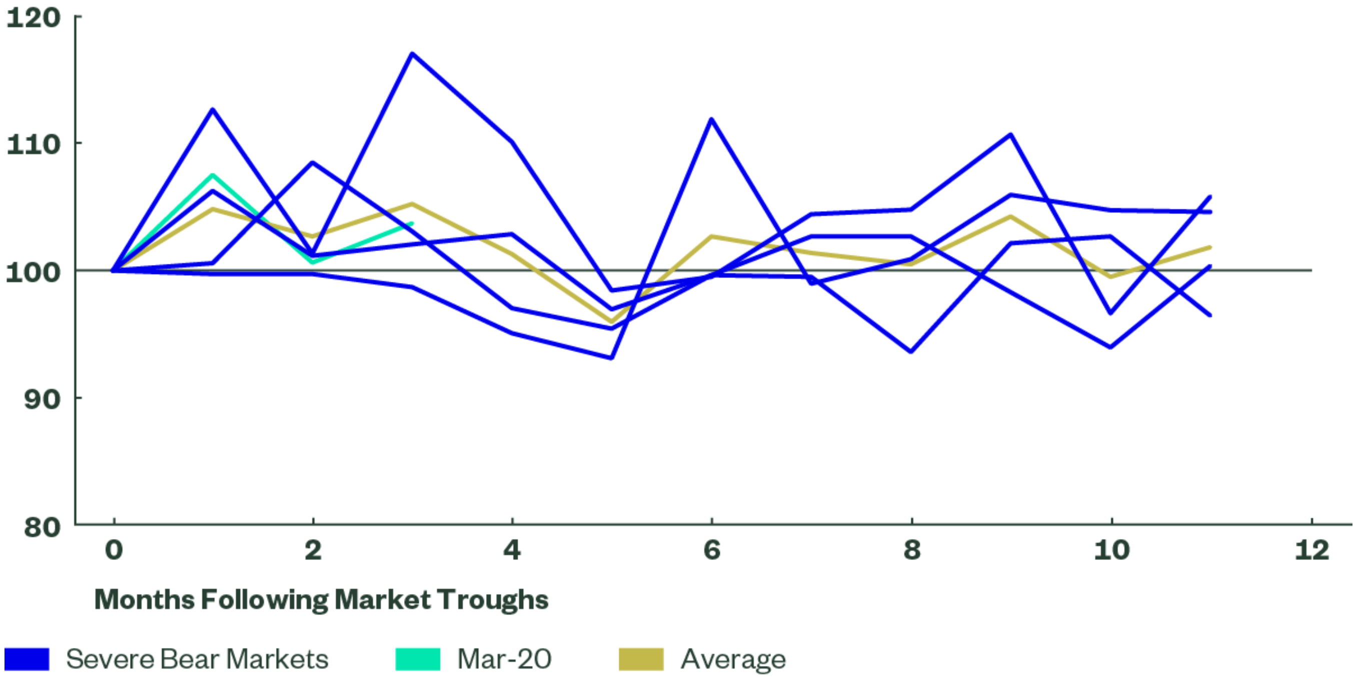
What has worked so far?

In terms of sector performance, during the current sell-off, Information Technology, Health Care and Consumer Staples have outperformed the wider US market. At the same time, Financials, Energy and Industrials have been hit the hardest.

In this current crisis, Consumer Staples did not hold up as well it did in months following the peak, compared to past bear markets. **On the other hand, Consumer Discretionary is one of the best performing sectors so far this year** (see Figure 3). This may suggest that the market believes the worst is behind us because, in previous crises, it was Consumer Discretionary that outperformed most during the recovery period.

If history and past bear markets are any guide, investors who believe recovery is imminent should look more closely at Consumer Discretionary (despite the recent rally) and avoid defensive sectors. On the other hand, those investors who still feel that the worst is yet to come may want to consider Consumer Staples and Utilities.

Figure 3: Consumer Discretionary is trading in line with history



Source: State Street Global Markets, Bloomberg Finance L.P., as of 20 July 2020. Past performance is not a reliable indicator of future returns.

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