CHARTS OF THE WEEK

Crypto debacle, bulls versus bears and the US election cycle

NOVEMBER 18, 2022

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This week's charts cover the crypto crash and FTX meltdown, the dearth of positive days for stocks this year, and a sentiment measure that suggests an end to the bear market may be near. In the wake of the US interims, we examine the election cycle's relationship with equities, unemployment and inflation. In China, we track the renewed spike in Covid-19 cases and analyse the disconnect between different measures of inflation.

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Cryptocurrencies look like other bubbles deflated by the Fed

Cryptocurrencies are suffering across the board after the FTX debacle. As the Federal Reserve and other central banks tighten monetary policy, the sector resembles other deflated asset classes.

Bitcoin is now well below USD 20,000, down from more than USD 60.000 about a year ago. As our table shows, most other cryptocurrencies have seen similar drawdowns. Total crypto market value is now well below USD 1 trillion, less than half its level a year earlier.

Cryptocurrencies are suffering substantial losses

Drawdown

	Price (USD)	Z-score	5/2022 Perf. %	6/2022	7/2022	8/2022	9/2022	10/2022	11/2022
BTC (Bitcoin)	16687.52	-1.33	-15.7	-37.8	18.0	-14.1	-3.1	5.5	-18.6
ETH (Ethereum)	1200.81	-1.16	-28.9	-45.1	57.5	-7.6	-14.5	18.4	-23.6
Tether	1.00	-0.97	-0.1	-0.1	0.2	0.0	0.0	0.0	-0.1
BNB (Binance Coin)	267.91	-0.90	-15.2	-31.6	29.3	-1.5	1.8	14.8	-17.9
USD Coin	1.00	0.63	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Cardano	0.32	-1.20	-17.4	-26.6	12.7	-13.6	-2.7	-6.5	-20.1
Solana	13.64	-1.19	-46.2	-26.6	26.2	-25.8	5.5	-1.8	-58.2
XRP (Ripple)	0.38	-0.91	-28.1	-21.4	14.8	-13.8	46.3	-2.9	-17.9
Terra	0.00	-0.90	-100.0	-1.9	-13.0	130.0	34.6	-20.3	-28.6
Dogecoin	0.08	-0.56	-32.7	-23.1	3.3	-10.2	0.7	105.8	-33.2
Polkadot	5.67	-1.02	-28.6	-32.1	22.8	-18.7	-10.1	5.0	-14.5
Avalanche	12.89	-1.11	-53.7	-35.8	40.3	-19.5	-10.1	12.3	-33.2
Binance	1.00	0.14	0.1	0.1	-0.2	0.1	0.0	0.1	0.0
SHIBA INU	0.00	-1.06	-41.9	-12.0	13.5	3.3	-6.4	10.2	-27.3
Polygon	0.87	-0.62	-36.5	-27.3	93.8	-10.8	-6.0	15.4	-3.3
TerraUSD (UST)	0.02	-1.00	-98.0	150.0	-40.0	0.0	0.0	33.3	-50.0
Cosmos	9.91	-0.98	-42.4	-26.8	37.8	13.9	10.2	10.0	-30.8
Wrapped Bitcoin	16616.64	-1.34	-15.6	-38.0	18.5	-14.2	-3.0	5.5	-18.9
Dai	1.00	0.23	0.1	0.0	-0.1	0.1	0.0	0.0	0.0
Crypto.com Coin	0.07	-1.17	-46.0	-39.4	19.6	-11.0	-10.1	4.7	-39.0
LTC (Litecoin)	62.48	-0.70	-28.9	-21.6	11.7	-10.1	-0.9	3.1	13.4
Chainlink	6.23	-0.96	-31.0	-17.7	22.7	-13.6	14.3	3.7	-20.7
NEAR Protocol	1.83	-1.32	-42.6	-43.9	27.3	3.1	-18.5	-12.6	-41.2
Uniswap	5.74	-0.81	-15.8	-12.6	68.1	-26.6	5.0	8.1	-17.6
Algorand	0.27	-0.93	-28.1	-24.4	9.7	-14.7	20.7	2.9	-25.0
TRON	0.05	-1.79	34.1	-23.1	6.5	-8.0	-3.8	3.8	-20.9
Fantom	0.18	-0.95	-41.2	-37.5	32.0	-18.2	-14.8	4.3	-25.0
BCH (Bitcoin Cash)	103.76	-1.04	-26.9	-49.6	36.3	-17.6	4.1	-4.1	-9.9
FTX Token	1.56	-3.13	-23.8	-15.3	24.0	-12.3	-9.1	7.7	-94.0
Stellar	0.09	-1.19	-11.3	-25.5	5.2	-11.5	9.7	-2.6	-18.9

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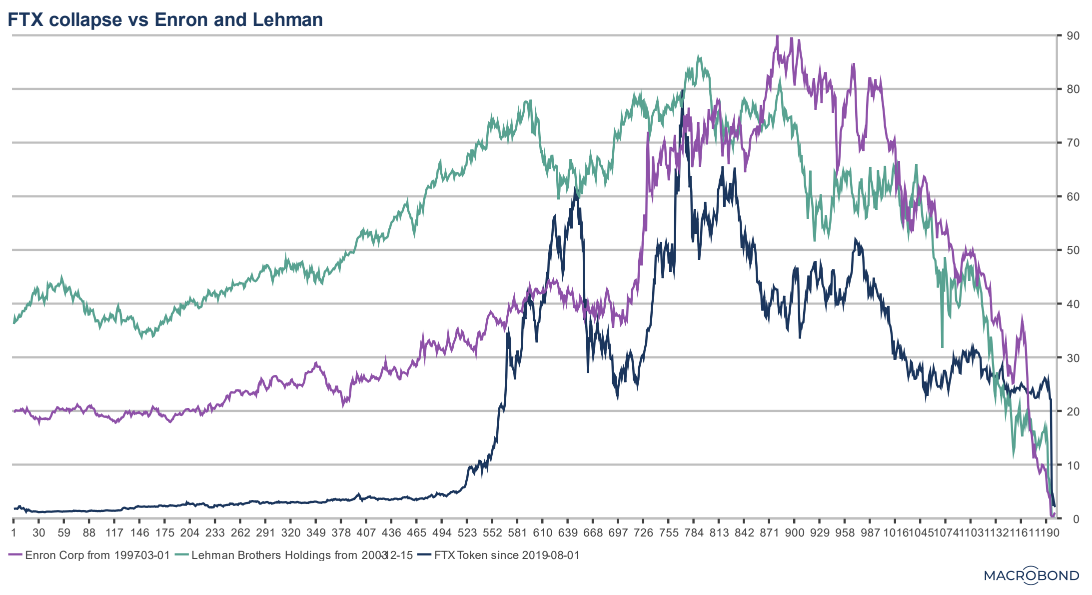
FTX and the echoes of Lehman and Enron

The crypto world has seen a high-profile collapse that will enter the history books with other financial downfalls. The following chart plots the price of the FTX token versus shares of Lehman Brothers and Enron, tracking their glory days and subsequent collapse.

As the FTX story unfolds, the bankrupt crypto exchange resembles Enron more than it does Lehman. Indeed, FTX's new CEO, lawyer John Ray, led Enron through the energy trader's own bankruptcy almost two decades ago. Enron, like FTX, had weak internal controls; FTX has been accused of fraud in Bahamian court filings.

Lehman, by contrast, was brought down by falling asset prices and investors withdrawing funds, a dynamic similar to a bank run.



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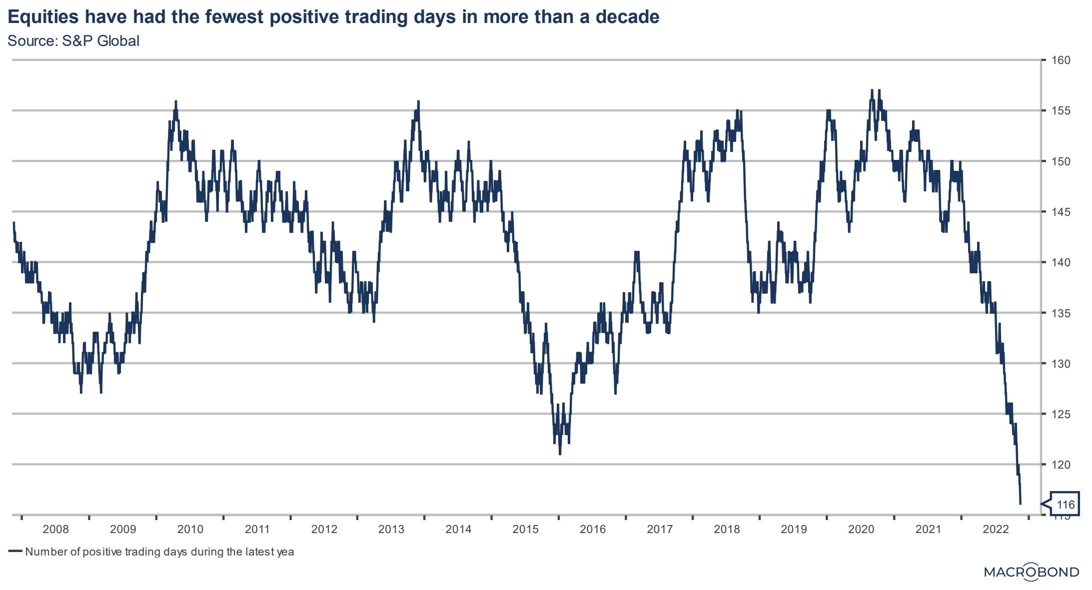
Fewer and fewer up days for stocks

The past 12 months have seen more red than green for the key US stock benchmark.

The following chart plots the number of positive trading days that the S&P 500 had over the previous year. The current bear market has pushed that figure to a two-decade trough, much lower than any moment during the 2008-09 global financial crisis.

Somewhat surprisingly, a period in 2015-16, the Fed's first tightening cycle since the GFC, also stands out as an era that saw more down days than up for equities.

Tip: This chart allows for the change region function.



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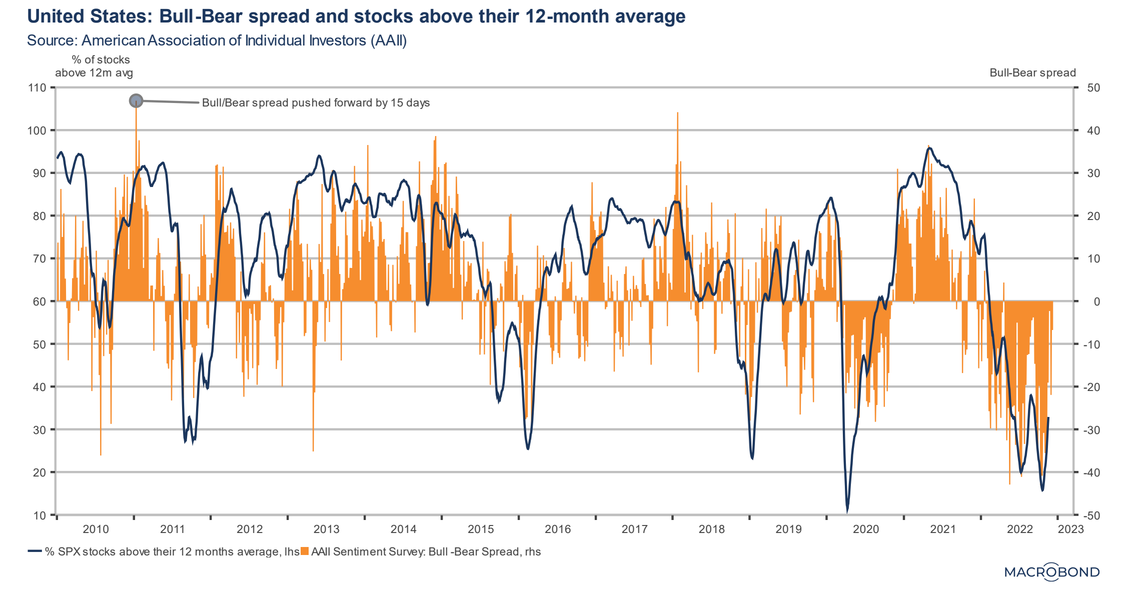
The Bull versus Bear spread correlates with equity performance

This has been a punishing bear market, but at least one indicator suggests it might be over soon.

The following chart plots the American Association of Individual Investors (AAII) Bull-Bear spread – based on a survey of whether respondents feel optimistic or pessimistic about equities – versus a smoothed series for the number of stocks in the S&P 500 that are above their 12-month moving average. (A negative number means more people are bearish.)

The two series are tightly correlated, with the sentiment series tending to lead by more than a year. Our analysis shows the highest correlation is at 0.55, with the AAII series leading by about 15 days. The Bull-Bear spread can thus be used as a leading indicator. After touching a record low in 2022, the spread has returned to more neutral territory, potentially indicating the bear market may be running its course.



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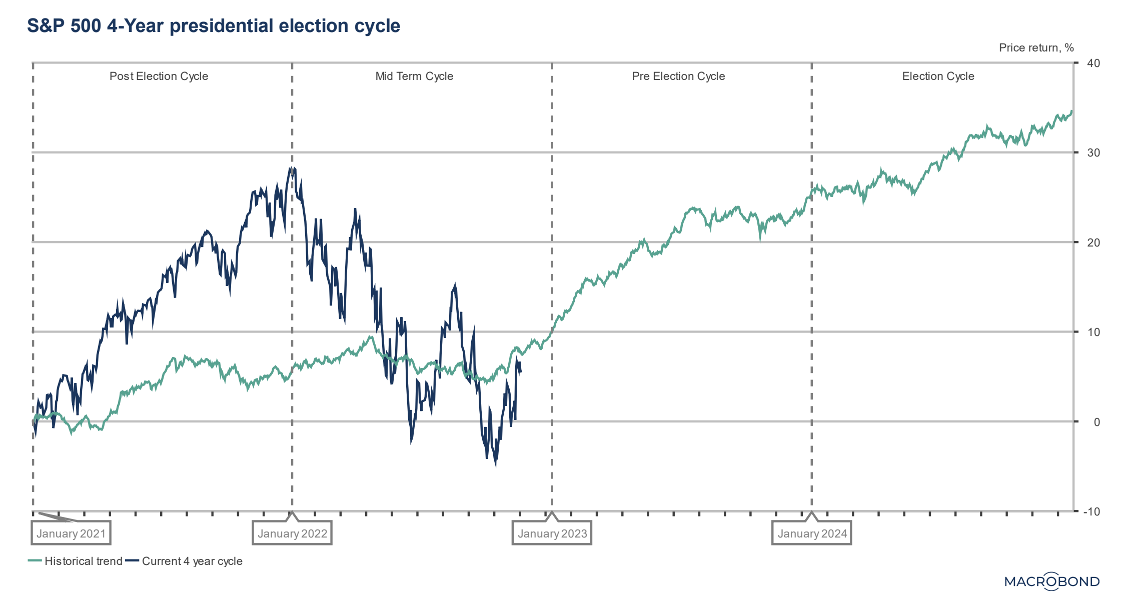
Equity market trends historically reflect the presidential cycle

The stock market tends to underperform prior to midterm elections and usually rallies in the aftermath.

The following chart graphs the performance of the S&P 500 during President Biden's current term against the historic trend for four-year presidential terms after World War II.

We shall see whether this cycle follows a similar pattern.

Tip: This chart allows for the change region function.



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Democrats and Republicans preside equally over economic misery

The “misery index” was initially created by economist Arthur Okun as a simple sum of the inflation and unemployment rates. (Subsequent variations have put a greater weighting on unemployment and included different variables.)

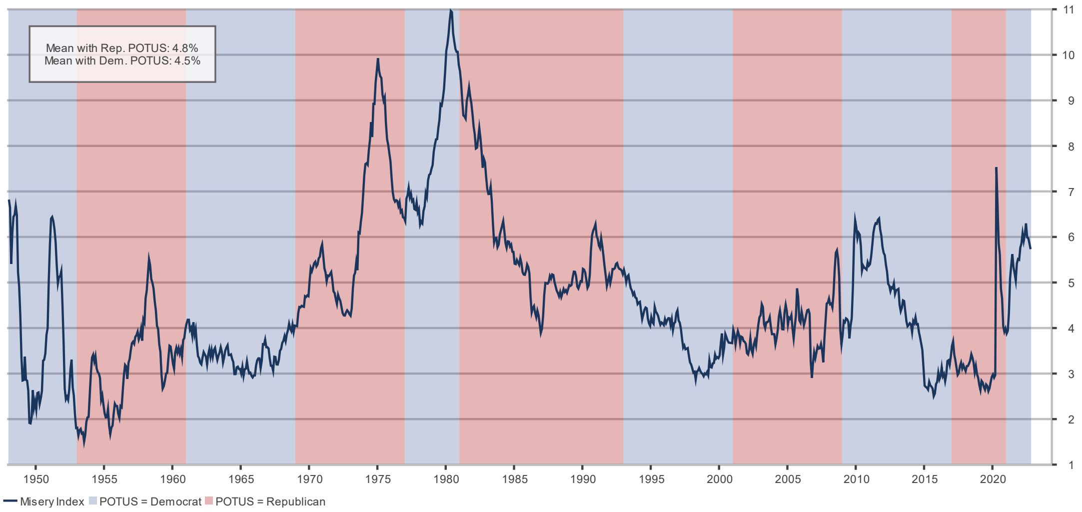
The following chart tracks Okun’s original misery index alongside the party occupying the US presidency at the time. Republican terms have been slightly more “miserable” than Democratic presidencies, but the difference is marginal and probably not statistically significant.

The 1970s stagflation is prominent on this chart, as is the massive increase during the pandemic. That reflects the impact of the inflation spike during a time of historically low unemployment.

Tip: This chart allows for the change region function.

United States misery index and political party in power

Source: Macrobond Financial AB, U.S. Bureau of Labor Statistics (BLS)



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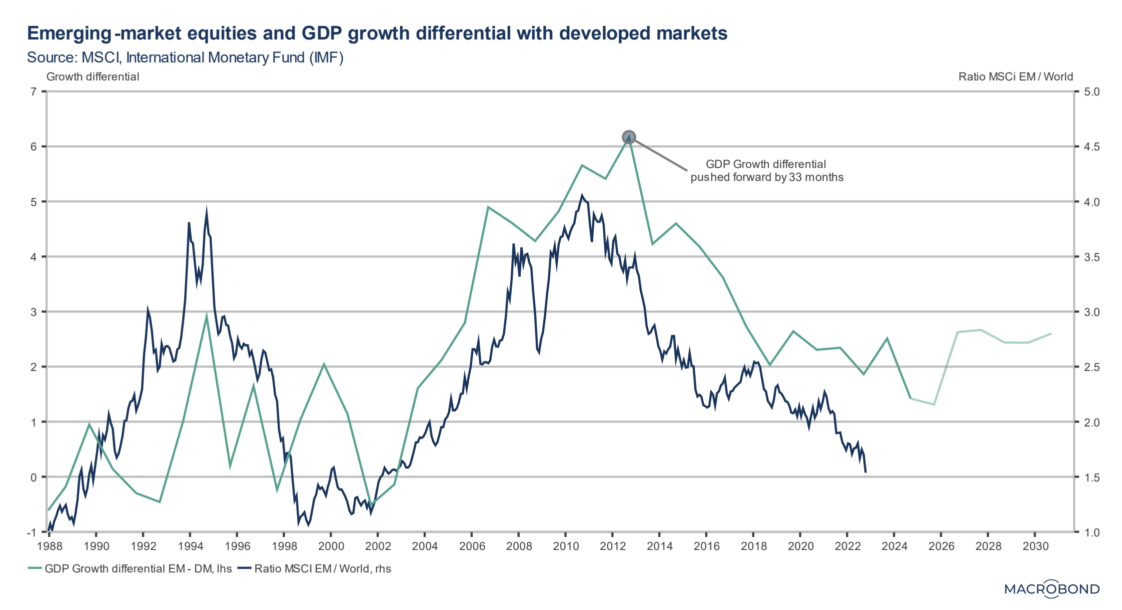
Emerging market growth and the outlook for equity outperformance

Emerging-market stocks have the potential to start outperforming their developed-market peers again.

The following chart uses IMF data to calculate when emerging markets are posting quicker economic growth than developed markets. Unsurprisingly, that differential is correlated with outsized equity performance (after a time lag of almost three years) – as measured by the ratio between price returns for MSCI's emerging market and global equity benchmarks.

Emerging markets did particularly well from the mid-2000s after developed economies stagnated due to the financial crisis.

IMF forecasts project EM economic growth is expected to stabilize at a level somewhat above that of developed markets. That could indicate a rebound for that stock ratio, which is trailing its usual performance.



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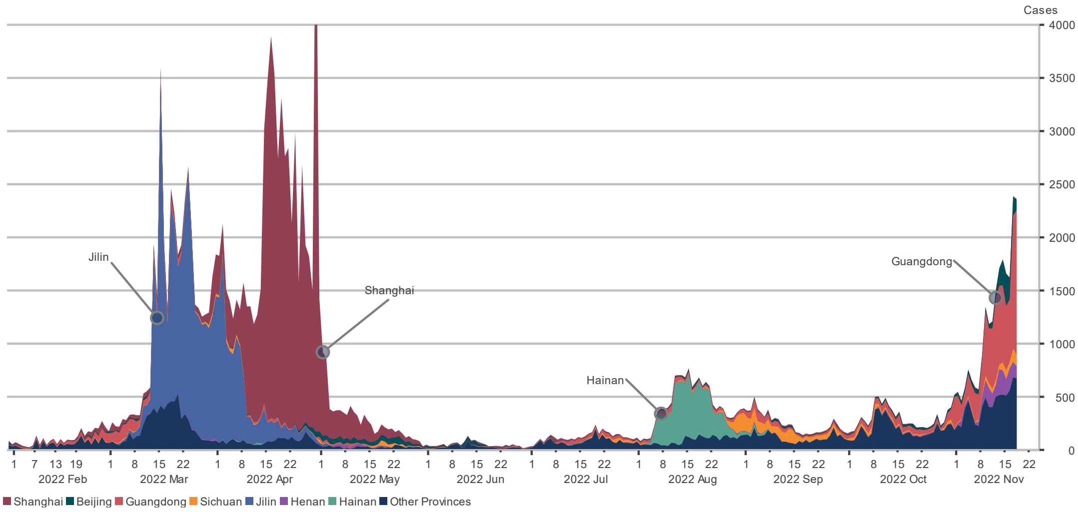
Chinese coronavirus cases flare up again

Speculation is rampant that China might soon revise its zero-Covid strategy, which has seen rolling lockdowns of large cities at a substantial economic cost.

The following chart shows how Covid cases are on the rise in the nation's major provinces again. A more fine-tuned zero-Covid strategy might influence the economic outcome that results.

China: Covid cases increase in major provinces

Source: DXY (Lilac Garden Family Clinics)



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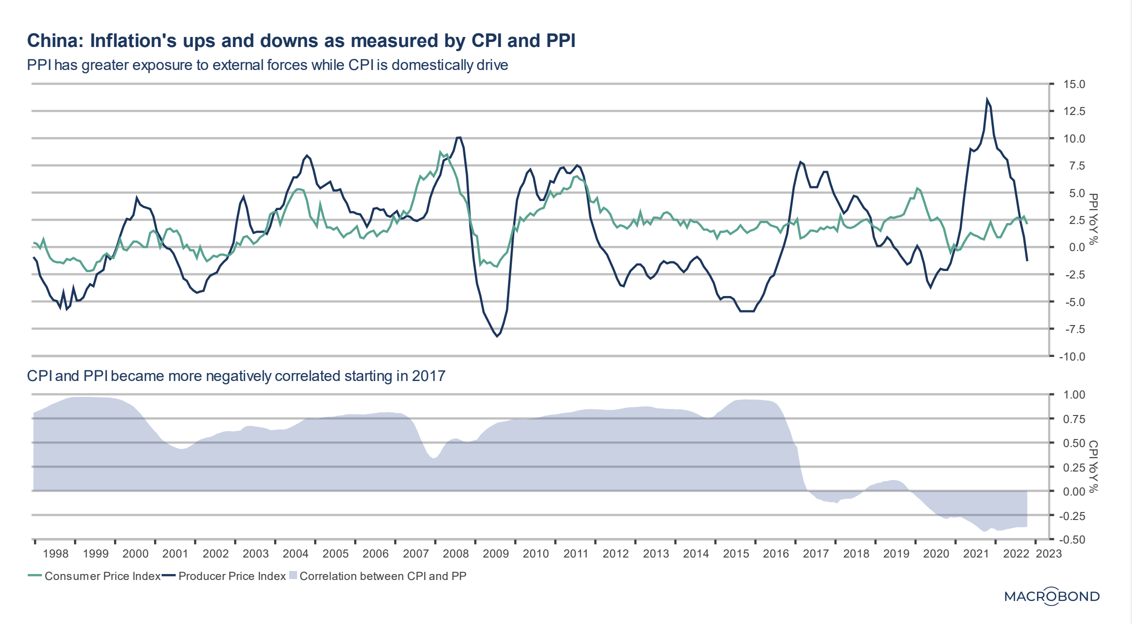
Chinese PPI is not passing through to CPI

When it comes to inflation in China, consumer prices aren't reflecting the pressure that producers are experiencing from input costs.

The following chart displays China's CPI and PPI inflation rates, followed by the correlation between the two indices. Throughout 2022, PPI surged to a record high, reflecting the global increase in commodity prices. But CPI inflation remained moderate, probably as result of the country's domestically driven economic slowdown.

As the pass-through from producer prices to consumer prices did not occur, the correlation between the two series turned negative during the pandemic.



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Global current account imbalances feel like 2008 again

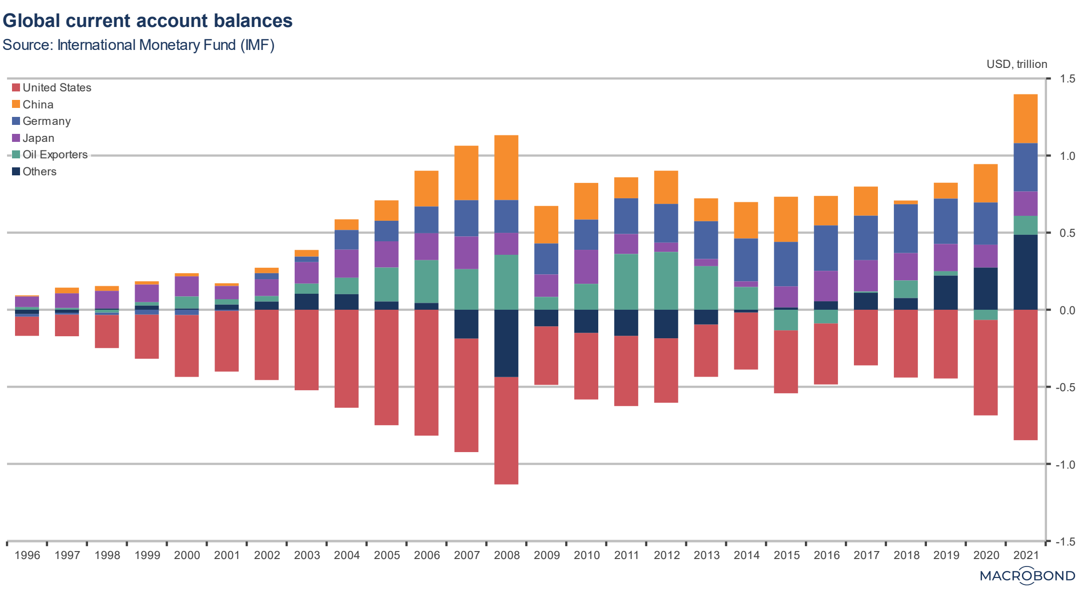
Current account imbalances are on the rise, renewing interest in one of the hottest topics in macroeconomics.

Economists like Maurice Obstfeld and Kenneth Rogoff argue that rising imbalances were a major factor in the crisis of 2008. More specifically, the global role of the dollar as the reserve currency inflated the value of US assets as capital from Asia and oil-exporting nations flowed in.

There was only a short period of normalization post-2008. The imbalances resumed their rise, especially during the first year of the pandemic.

As our chart shows, the US continues to be the main current-account deficit country; the rest of the world records surpluses. This doesn't reflect any particular US trade weakness. As Ben Bernanke explained, the trade deficit is the tail of the dog, adjusting to a variety of variables: interest rates, the currency exchange rate, global financial flows, etc.

Ultimately, the rest of the world still craves US dollar assets and exports capital to the US economy.



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