Anything is Possible

March 29, 2020

As of last weekend, the same Wall Street institutions that were proclaiming a new bear market on Monday were saying that it was the shortest bear market in history (i.e., two days), and that now we're in a new bull market. Unknown, in my opinion. The shock to our economy and markets is quite significant.

We had the fastest decline in history off a peak and now we've had the fastest rally off a bottom since 1931. The average stock was down 50%. So what is it? Up or down? The government has done what it's needed to do, as predicted. Both the Federal Reserve and the Treasury are throwing everything they have at the problem in order to save our economy from the negative effects of CV19 and economic closedowns.

In 2008-2009, during Obama's tenure and the great financial crisis, quantitative easing, also known as money printing, was at a rate of $60 billion per month. Now, it's $125 billion per day. Normally, I would say great for stocks and bad for bonds long term as long as the money printing continues and confidence in the US government continues. Nobody really knows the result, because these levels of financial warfare are unprecedented in history. Much will depend on what the real economy does and on the economic damage caused by CV19 in the long term.

For now, let's look at the near term. Markets hit a bottom last Monday, followed by a huge rebound in anticipation of the fiscal stimulus, and every measure possible being thrown in by the Federal Reserve that followed. It looked like the average bear market rally. A retest of last Monday's lows is likely sooner rather than later.

So what's next? In October 1929, at the beginning of the Great Depression, markets went down at a similar rate and speed as they did the last few weeks, followed by a tremendous rally of 18% in two days. Then, you know the rest of the story. Down 26% in 13 days.

What's different today is that in 1929 the Federal Reserve tightened monetary liquidity, and today the Fed and Treasury are literally throwing the financial kitchen sink at the problem.

Am I ready to call this a new bull market? No. This might have been a very nasty correction triggered by the same algorithms, robots, and hedge fund strategies that propped up a severely overvalued bull market and everything will be fine going forward. Or, it's the first phase of a new bear market to be followed by a rip roaring bear market rally, to be followed by two more bear market declines, possibly down fifty percent from current levels. Bear market relief rallies in the first stage usually reassure the populace that everything will be fine. I doubt that will happen. If it's a real bear market, the eventual bottom will be the buy of a lifetime. The Roaring 20's began only 18 months after the greatest pandemic in history, the 1918 Flu.

A warning going forward. Nobody knows, no matter how confident sounding, how this will all play out. Our government is doing everything it can to relieve the economic stress caused by CV19 and to avoid a second Great Depression. In the last bull market, corporate share buybacks had much to do with propping up the bull market. That will not be happening this time around as both the government and public will not stand for it. Much of corporate earnings growth in the past 5 years was illusory. Corporate chieftains bought back corporate shares via easy money borrowing. That game is over. Buybacks will be severely limited.

The strategy for now is to buy tactically on big declines when psychological sentiment is in the pits and to sell on euphoric rallies.

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