Market Update March 2, 2020

Last week's market activity turned out to be one of the fastest weekly declines in market history.

Just the way market movements to the upside were exaggerated by algorithms, quant models, and other mechanical methods, the downside is now being exacerbated by these same techniques. Dealer gamma hedging, CTA deleveraging, volatility selling, and other mechanical techniques have all contributed to the volatility we're now seeing. The market has become a perpetual motion machine feeding on itself in either direction solely based on its own movements. Throw in a trigger like Corona virus fears and last week is what we get.

Where do we go from here? Markets are again in the range of decline where we start to worry that the bull market may finally be over. Historically, declines resulting from panics (war, pandemics, etc.) are not long lasting. However, in this particular case, the bull market has gone on much longer than anyone could ever have imagined. Excessive stock valuations don't help. Monetary liquidity from global central banks including the Federal Reserve had much to do with it. The coming weeks will be critical. We've recommended above average money market and cash holding for a while so nothing drastic needs to be done immediately.

Much damage has already been done to popularly followed blue chip stocks like Apple Computer. Apple was down twenty percent from its recent peak to its low on Friday, all in the space of two weeks. Whatever the reason for the decline, it's a bit disconcerting and a hit to investor confidence to see the kind of damage that can be done in a very short period.

As mentioned many times, the stock market is a confidence game. Monetary liquidity provided by central banks is fuel for it and monetary tightening is bad. Should that equation ever change and investors lose confidence in the ability of central banks to control the situation, then all bets will be off.

Bond markets around the world are in an even bigger bubble than stocks are. Interest rates are at such low levels that they imply little growth in the economy for years to come.

For now, we are cautious. The S&P500 index reached a level of 2850 on Friday. Any further decline below 2800 or so will warrant further stock reductions. 2600-2650 is the line in the sand. That is the 200-week-moving-average of the index, and all corrections going back to 2011 have stopped there. If the market passes below this average then we will be in a bear market.