

A View From Here - September 2020

It Just Won't Crash

Since the arrival of the pandemic, the stock market has traded in vertical extremes. Prior to the realization that Covid-19 was becoming global, North American stock markets had been increasing to all-time highs for a narrow band of participants - mainly large capitalized technology companies. In fact this has been ongoing since 2017 as tech stalwarts moved higher while the wider market of companies lagged in comparison. Many of these laggards peaked in 2018 as more and more capital moved into a smaller number of investments. This might have something to do with ETFs being widely available and among some of the best performing investments over the past few years, thus attracting more and more capital.

I've been in the financial markets for over 30 years and, while there's always new ways for things to go right and wrong, one thing that seems obvious is when indexes go up like they did through most of 2019 and at the start of 2020, you know something is going to knock that cycle off, as days of stronger market performance turn into weeks, which can make us more complacent. Complacency seems to kick in just about when things change. Early in the new year the general direction of the U.S. market indices was climbing just as Covid-19 was starting to wreak havoc on more than just China. As such, we began a very nasty correction. Then came lockdowns and a self-induced recession reached our shores as fear of economic depression and predictions of our very own dystopian future began to emerge. If I would have told you in January that this virus we're starting to hear about would play out the way it has, how many would have predicted rising stock markets and asset prices?

But it's the fact that Markets haven't crashed which is encouraging. Sure, there was a 30% retreat between February and April, but it's important to note that, prior to that, stock markets were increasing at an almost unsustainable clip so a correction was inevitable. Adding the very real danger of this pandemic, one would think that even by subtracting the large cap tech companies from most indexes, the markets would be significantly lower. When we do that exercise, markets are down just under 10%. I see this as a good sign. If you think back to previous panics throughout history, in particular the ones that we've lived through in our lifetime, especially ones that at the time had the power to change life as we know it, markets have gotten the long-term right.

The stock market crash of 1987 was seen as a harbinger of things that didn't come, the currency crisis of the late 1990s, 9/11 and, of course, the financial meltdown of 2007-2009. In each case we have witnessed a rebound that did not change life as we know it. We kept traveling, like we did shortly after 9/11. So being down +/- 10% when global cases continue to peak is if anything, a good sign. Add the upcoming election, geo-political tensions around the globe and U.S.-China relations and there's enough fear out there to say that markets climb a wall of worry.

Often, someone will comment that we are living in a dream world and that markets will crash when people wake up, but if you think about it, the market digests all news, all-day, all the time. Let's look at this from a micro-standpoint using a company as an example, and then extrapolate it on a much wider spectrum. If a company is valued in a particular way the thing that is going to change that valuation is news that changes perception of its value. For example, if a company reports a better than expected earnings quarter or an event that changes the current perceived view of its worth, new revelations of its value will change to reflect the new information. Multiply this by millions of companies and you have to be aware that markets are continually revaluing and pricing in all current knowledge of all things which affect it. What it can't price in is what it doesn't know. It's the surprise that has the power to change value.

And that's how markets value companies...now expand it among the millions of public entities, and you have an idea.

In sum, despite all the concerns out there, I believe it to be encouraging that markets haven't fallen apart and in our world things are starting to really get better.

Let's hope we are right,

Thanks for taking a look and, as always

All Good Things,

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