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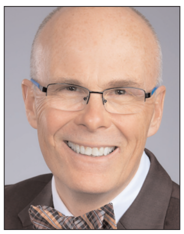
U.S. STOCK MARKETS ARE A STUMBLING, DRUG-ADDLED BABY

Tracking S&P 500 reveals easy money addiction



Keith Richards

Occasionally I like to update a chart of the S&P 500 stock index with annotations surrounding major market movements and U.S. Federal Reserve moves.

Since 2008, there have been some strong correlations between market moves and Federal Reserve stimulus programs. Let's take a look at the markets since the late 1990s to follow these Fed/market patterns.

You'll note on the left side of the chart *(see page 507)* the end of the 1982-99 bull market. Following the technology bubble ("dot-com bubble") and the Sept. 11 terrorist attacks in 2001, the market formed a rounded top. A crash ensued, followed by a bottom/consolidation formation.

Between 2003-07, the good times returned. The SPX barely made it past the 2000 highs. Then along came the subprime mortgage/banking crisis and energy bubble. A consolidation pattern ensued, leading us into the crash of 2008-09.

After a horrendous 53 per cent crash, the market consolidated from late 2008 to early 2009. Markets stopped going down.

The markets got off to a rough start after that last crash in 2008-09. That one wasn't like the one before it – which really came about because of a narrow market that was focusing on the dot-com hype. The 2008-09 crash came as a result of a debt and banking crisis, both domestically and internationally. Recall the PHIGs' (Portugal, Hungary, Italy, and Greece) near-defaults alongside the implosion of the over-leveraged North American consumer.

This crash was going to need more than just a simple rotation out of overdone stocks like Global Crossings and Nortel. Enter, the Fed.

The chart shows us where the various Fed QE (quantitative easing) and Twist stimulus programs started and ended. Please note the coinciding market rallies as each program began, followed by the declines as they ended. Clearly, the Fed had created a dependency problem with fiscal stimulation. After a couple of terms under President Barack Obama and Fed chair Ben Bernanke, in came Donald Trump. Markets were beginning to be weaned off of their favourite drug, easy money!

The last thing a guy like Mr. Trump wants is to see his name go down in flames in a market correction. So the program began. To be sure, some of his programs were legitimately very good for the economy and the markets. He did offer an economic insight that Mr. Obama, being the left-wing guy he is, wasn't likely to offer.

For instance, the business tax cuts and repatriation programs for

overseas money stimulated growth and jobs – without question. The market was able to respond positively to these initiatives.

The year 2018 saw markets in withdrawal from their fiscal stimulus fix. In fact, rates went up four times that year. No coincidence that the S&P 500 was a net loser in 2018. Like a child growing into an adult, it had to learn to stand on its own two feet without big-daddy Fed to hold it up. Growing pains are natural but necessary.

But the current president had a desire to enhance market returns, and the rough markets of 2018 didn't help his image. Something had to be done!

Perhaps this is where he made a mistake. By pressuring (now two) Federal Reserve chairs to cut rates (this, despite a stable economy and corporate earnings, as well as positive job stats) – he and the Fed reintroduced the drug to the rehab patient, to return to our earlier metaphor.

Thus, 2019 rallied on the new "high" of stimulus. The baby is forgetting how to walk, the problem is, this baby is now 10 years old, given that the stimulus programs began in 2009 (per the chart).

The big question

You can very clearly identify how reliant the U.S. market has become on easy money. And you can see what kind of declines we get when it comes off of that drug. Yet we all know that the stimulus train can't run forever.

Eventually, baby has to learn to stand on his or her own two feet. The big question is: will baby stand, or will baby fall?

Special announcement

Lately, we've been presenting Technical Analysis webinars for groups like the CSTA (Canadian Society of Technical Analysis), Share Clubs, and others. It occurred to us that, beyond these groups, my Investor's Digest readers might be interested in attending such a webinar.

We started off with a Technical Analysis primer- which has been recorded and is available for you to view. From there, assuming you like what you hear, you can participate in other webinars.

We'll cover market risk indicators. We'll talk about how to identify breakout candidates and perhaps even bring in Craig Aucoin (ValueTrend's chartered financial analyst) for a review of fundamental analysis.

Please contact Aleks Bozic at our office via email at abozic@valuetrend.ca to register for future webinars. He will keep your contact info on a list so you will receive a link to attend the seminar a day or two prior.

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