CBL WEALTH MANAGEMENT

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Market Brief

December 26, 2018

Market Snapshot

Closing Values as of 12/26/2018

Dow	22,878
S&P 500	2,468
Nasdaq	6,554
Gold	$1,269

Wounded bull or emerging bear?

With the exception of new highs set in September, the markets have spent much of 2018 in a state of correction. The pullback that began in October accelerated in December until the markets fell into bear market territory on Christmas eve. With stocks being fundamentally solid and the economy still expanding there seems to be little reason to have expected a bear market for Christmas. Then again, one of the hallmarks of a bear market is the lack of rational behavior. One of the questions on investors minds is whether the previous bull is merely wounded or has a full fledged bear market emerged.

It is normal to have market pullbacks and corrections throughout the year, even when there is no apparent underlying economic condition to warrant the behavior. Believe it or not, it is also not unprecedented for a bear market in stocks to occur even when there is no economic recession. In fact, of the 14 post World War II bear markets, five occurred independent of a recession.

So what is it that turns a simple market correction into a full blown bear market if not economic recession? Even when the economy is not in or nearing recession bear markets have occurred against a backdrop of a "slowing" economy. Although a bear market can be sparked by many things there seems to be 4 conditions common to bear markets that occur independent of a recession: Slowing growth, policy mistakes, financial crisis and excess speculation.

Whether these conditions actually exist or not, concerns that these conditions may exist have dominated and driven the markets all year. Despite strong economic indicators and expectations of continued expansion, fears that the Fed has made or will make a major policy error by tightening too much, too quickly, sparked the correction in early 2018 and seems to be a major driver behind the current declines. The pending Brexit has the potential to result in a significant economic crises that causes ripples far beyond the European region. Speculation in the FANG stocks helped push Amazon and Apple to the trillion dollar market cap mark.

I would venture to say the current bear market will earn a place in history as being unlike others that have occurred outside of a recession. The major difference being that the markets were driven downward by anticipation, speculation and rhetoric rather than realization and fear. The fundamental data has been largely ignored as investors focused on what the predictive indicators "might" predict at some point in the future. Adding to the uniqueness of this market break down was how orderly the breakdown appeared. It appeared as if algorithms and computerized trading locked the indexes to technical charts, making the market movements highly predictable from a technical level. As a result, much of the early decline occurred with very little fear or volatility.

There may be some good news though. Bear markets that have occurred independent of a recession have been much less painful than those that coincide with a recession, they also tend to be shorter in duration. It isn't possible to know in advance how long a bear market will last or how deep it will cut, but history has proven time and time again…they ALL end, often with as little warning as they began. I don't know how much further the markets might fall before they reach bottom but the current values are quite attractive.

In the trading days since setting the bear market low on Christmas Eve the markets have had impressive (even record breaking) moves upward. As tempting as it is to believe the recovery form the bear market lows will be a rapid and steep "v" shaped one, history and experience tells us we should expect at retest before a full recovery can occur. Although the current pricing is VERY attractive, it is possible the markets may drift even lower before finally recovering from this bear downturn.

Whether you should be selling into rallies or buying the dips will depend on your individual needs and long term goals. If you anticipate needing additional cash in the near term, selling into rallies can help to avoid larger losses that can occur if forced to sell when markets drift lower again. If you have sufficient cash flow and a long term investment objective, buying into dips and/or dollar cost averaging with regular additions can turn market volatility into a growth tool.

The upcoming earnings season, shifting monetary policy and a China trade deal could be the catalyst for a substantial recovery. Failures on any of these fronts could prolong the current bear market. Accepting that the markets will remain volatile until the political and economic unknowns are better understood will make the next few weeks/months much more tolerable.

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