FORSTRONG
GLOBAL

ASK TYLER

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LONG MAY YOU RUN

"We've been through
Some things together
With trunks of memories
Still to come
We found things to do
In stormy weather
Long may you run."

- The Stills-Young Band
"Long May You Run"*

Is this the end of the bull market that started in 2009?

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Neil Young was singing about his beloved car in the mid-1970s. Our subject is the bull market that began in 2009. As the curtain closes on 2018, "end-of-cycle" fears are again surfacing. Perhaps not a surprise. Volatility is up more than 40% in 2018 and a total of 12 days have seen spikes more than 20% — twice as many as in 2008.

Economic expectations have also collapsed. The US is widely predicted to slow as tailwinds from fiscal spending fade. China is viewed as a victim of US trade brinksmanship and a rapidly slowing economy. Emerging markets are seen as vulnerable to a virulent contagion replay of 1998. And, Europe has been left for dead.

But is any of this new? Forecasting doom has defined the genre of post-crisis literature. The GFC unleashed constant waves of disaster predictions, crash fantasy and other catastrophe clickbait. The more harrowing the narrative, the higher the readership. Even Alan Greenspan is now telling investors to run for cover.

We get it. To be first to spot the outlines of a looming crash can be glorious (and career-enhancing). But persistently trying to pinpoint the end assumes there will be a "big one" ... that markets are always balancing on a crumbly ledge between blue skies and calamity.

If only it were that binary and simple.

What if instead a series of smaller "resets" extended the life of this cycle? In fact, to date, that has happened. This cycle's major corrections coincided with significant economic downturns and adjustments, most notably the European crisis in 2011-2012, the commodity collapse and US dollar surge that began in mid-2014 and lasted until early-2016. And, now, 2018's hot mess (for lack of a better word).

Underpinning these resets has been some key post-crisis "regulators" — circuit breakers that constrain the overall level of economic growth and ultimately provide relief. Most crucially, high debt levels around the world have restricted how much rates can actually rise. Routine consolidation phases have occurred along the way as interest rate sensitivity acted to slow economic growth. 2018 has been no exception.

Unsurprisingly, central bankers are no longer seen as the maestros they once were. Instead, timidity has been the dominant characteristic. In the US, the Fed target rate has been lifted by a mere 200 basis points since December 2015. Yet, during the past 10 Fed tightening cycles, the median tough-to-peak increase in nominal rates has been a much bolder 500 basis points. Looking into 2019, with the Fed facing a combination of softening growth and lower inflation, a pause in monetary tightening looks highly likely.

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Commodity prices, which have been highly volatile in the post-crisis period, have worked similarly. Rising prices negatively impact net global consumption, investment and liquidity. In fact, every global recession in the past 50 years has been preceded by a sharp increase in oil prices. Conversely, on all recent occasions when the oil price has at least halved, faster global growth followed. This year has seen a sharp fall in oil prices which should contribute to overall higher growth next year.

And then there is valuation. This has become more of a behavioral regulator. The rules of investor engagement changed after 2008. Whenever prices surged and perceived values grew too rich, memories and predictions of another crisis were triggered, restricting overall investor enthusiasm. What is not well known is that most stock markets outside of the US remain well below their late-2000s highs in both local currency and US dollar terms. Deep corrections have plagued the post-crisis path.

Where to next? Looking back, each of these periods provided renewal and rebirth … breathing life back into a now born-again bull market. This episode will be no different.

INVESTMENT IMPLICATIONS

To be sure, there is real risk that end-of-cycle fears become self-fulfilling and feed into a more serious downturn. Other pressure points have surfaced too, notably broken leadership of the FANG stocks.

But global macro growth expectations are now the most pessimistic in 10 years, more so than at the major equity bottoms in 2011 and 2016. And while US economic and earnings growth will slow steadily over the next 12 months, it will be more gradual and modest than most investors fear. China's slowdown is already ending in response to easier policy, and the economy is likely to accelerate back to an above trend pace. Further, the euro area's soft patch is also likely to give way to firmer data, aided by currency weakness and stronger growth in Asia.

In short, the world is likely to settle back into "muddle through". What's more, given deeply depressed sentiment, a series of "upside surprises" is highly probable. Long may you run, dear bull market.

**Neil Young's unplugged version is particularly good:* https://www.youtube.com/watch?v=WYna-UAt75c