

# Wariness remains despite large gains

Peter Wells

The market's rally from multi-year lows continues, but analysts still contend the surge is more likely to be a bear market rally than the first stage in an outright recovery.

The benchmark S&P/ASX 200 Index gained 0.56 per cent yesterday, taking its gains in the past 21 sessions since it closed at a 5½-year low on March 6 to a robust 19.43 per cent.

The Australian market has not been alone either, with global markets including Wall Street up by more than 20 per cent from their March lows.

In the United States, the S&P 500 has risen 24.53 per cent in 19 days.

Commentators note, however, that it is not uncommon for shares to post substantial returns following a sizeable correction.

Furthermore, the challenges confronting the global financial system remain, posing the key risk that the rally may fizzle out. Only time will tell whether markets will hold above their recent lows.

Broker UBS has examined bear market rallies — which it stipulates as surges of 5 per cent or more — during six major bear market phases in the US since 1929.

It noted that their average price return was 13.5 per cent and their duration 44 days.

The average gain for the All Ordinaries in bear market rallies since the 1970s was 12 per cent and the average duration was 48 days, UBS said.

UBS equities strategist David Cassidy said the current rally was

## Grin and bear it

Performance of S&P 500 during significant bear market phases in the 1930s and 1970s

	Start date	End date	Return (%)	Duration (days)
▶ Bear market	Sep 1929	Jun 1932	-86.2	989
▶ Rally	Jun 1932	Sep 1932	111.6	98
▶ Subsequent sell-off	Sep 1932	Feb 1933	-40.6	173
▶ Rally	Feb 1933	Jul 1933	120.6	141
▶ Subsequent sell-off	Jun 1933	Mar 1935	-33.9	604
▶ Rally	Mar 1935	Mar 1937	131.6	727
▶ Subsequent sell-off	Mar 1937	Mar 1938	-54.5	386
▶ Bear market	Jan 1973	Oct 1974	-48.4	636
▶ Rally	Oct 1974	Sep 1976	73.1	719
▶ Subsequent sell-off	Sep 1976	Mar 1978	-19.4	531
▶ Rally	Mar 1978	Nov 1980	61.7	998
▶ Subsequent sell-off	Nov 1980	Aug 1982	-27.1	622



SOURCE: UBS

“getting pretty large in the scheme of things, even on a 70-year view”.

Because there were “no hard and fast rules” with bear market rallies, it wouldn’t be unprecedented to see a new low point for markets, he said. But “given that it’s been a pretty significant rally in either Australia or the US, I’d be surprised if there was a lower low out there”.

Morgan Stanley has also been examining the rally.

Equities strategist Gerard Minack said most Morgan Stanley strategists were sceptical about the rally.

He gave three main reasons for the scepticism, observing that “we

always need to be ready to call a more significant low in equities”.

The first reason was the speed, he said. “The fastest rallies tend to be bear market rallies.”

On Morgan Stanley’s numbers, the average duration of the five bear market rallies greater than 15 per cent the S&P 500 has experienced since 1929 (excluding this rally) is 56 days.

So on both UBS and Morgan Stanley numbers, the current rally has been incredibly rapid.

The second reason for scepticism was the rally’s composition, Mr Minack said.

“Those [stocks] that went down the fastest have bounced the hardest, and that’s classic bear market stuff,” he said.

“And third, specific to this cycle that has been such a credit-dominated cycle, we wouldn’t expect to see equities sustainably rally when there’s so much distress in credit markets. So we continue to be very suspicious of [the rally], but that doesn’t mean it can’t go higher.”

Thus far, the Australian market has looked quite strong despite the admissions of many investors that they expect the economic news to

remain quite dismal. However, equities are often credited for anticipating turning points in the economy six to nine months in advance.

The S&P/ASX 200 rally has come on record average daily volumes in excess of 1 billion shares. Traders have also commented that offshore interest in Australian equities has picked up.

UBS noted that in some very large secular bear markets, US shares enjoyed rallies of more than 100 per cent, which contradicts “the notion that equities necessarily meander sideways for years following a major market correction.”

In Australia, shares experienced a bounce of 101.5 per cent from September 1974 to August 1976 following a bear market fall of 59.2 per cent from January 1973 to September 1974.

Then, following a 22.5 per cent pullback, they rallied a further 181.1 per cent from November 1976 to November 1980.

The perspective of time was quite important for viewing bear market rallies, Mr Cassidy noted.

“Huge runs in equities for multiple years can, in the fullness of time, be just classified as bear market rallies.”

The US market in 2007 just managed to sneak past its tech boom highs before plunging back to its current level.

If it had failed to do this, the argument could be mounted that that run was simply a bear market rally, even though for many participants the period of 2003 to 2007 felt like a bull market.