Federated®

The bull: younger and stronger than you think

With the secular bull marking its sixth birthday, there′s plenty of room left to run. Helping it along are the still-deep scars from 2008-09′s near-Armageddon experience.

Published 03-22-2019

Stephen Auth, CFA
Executive Vice President
Chief Investment Officer, Equities, overseeing all of Federated's equity and asset allocation products globally

There's been a lot of chatter of late about this bull market's 10th birthday, prompting the bears to warn this cycle is getting old. There's only one problem with this view and it's a big one—this secular bull didn't start when the S&P 500 hit its financial crisis low of 666 on March 6, 2009. It's not even 6-years-old yet. That birthday comes next Thursday, which will mark six years to the day when the S&P 500 closed above its last bull market high of 1,565 (Oct. 9, 2007)—the technical marker for the start of a secular bull. Given that secular bulls tend to last 18 to 20 years, if this one were a person, it would be graduating from college and getting started with its life, not entering its mid-40s when college tuitions and initial thoughts of retirement occupy one's mind. So ″Happy Birthday″ to the young bull!

I know, some of you who have followed my musings over the years may recall that, well before March 2013, I was suggesting the recovery from the 2009 lows could be just the beginning, and that we were likely entering a secular bull market. In fact, our equity team was a lone proponent of the well-out-of-consensus view that equities were in a long-term secular uptrend, in which the market consistently achieves higher highs and

higher lows. Just two months after the March 2009 low, we went overweight equities in our PRISM® stock-bond model and, save for the eight months running up to the 2016 election, have stayed there. And in August 2011, when the bears were saying "I told you so" as global markets were selling off amid a European debt crisis and decelerating U.S. growth, we remained firm in our convictions, writing we expected the secular bull to be confirmed by late 2012 or early 2013, with the S&P taking out its old high. That prediction proved true on March 28, 2013.

To be sure, definitions of bull and bear markets are more often in the eye of the beholder than the outcome of precise science. For our purposes, we have considered secular bulls as ones with a steady advance in the averages without enduring a generation-losing drawdown of 40% or more. Secular bears, on the other hand, are characterized by a protracted period of stock averages more or less going nowhere, continuously failing to break out to new all-time highs, and with scary intermittent declines of 40%—hardly an upside/downside mix that attracts long-term investors.

A CENTURY OF SECULAR BEARS AND BULLS

There have been three secular bears over the last 90 years: "The Great Depression Bear," which lasted from 1929 and was not finally exited until 1954, when the old October 1929 peak was finally breached. That bear, marked by two giant and several smaller recessions and World War II, experienced an 86% peak-to-trough decline, with four declines of 40% or more, two declines of 30% or more and five 20%+ down moves —"The good old days!" The second secular bear was the "Stagflation Bear" from 1973 to 1980, which experienced a 48% peak-to-trough decline and several corrections of almost 20%.

The third secular bear, "The Double Bubble Bear" that we exited in 2013, resulted from Fed attempts to prick two successive asset market bubbles, first in tech stocks in 2000 and then in real estate in 2007. This youngest bear experienced a 57% peak-to-trough move in that scary fall of 2008 and winter of 2009, along with an earlier 49% downdraft in the tech blowout from early 2000 through late 2002, with a 21% rally wedged between 37% and 34% sell-offs.

The secular bulls that followed each secular bear rose 277%, 1,170% and 83% (so far), respectively, from the point they exited the secular bear that preceded them. Based on both time and historical returns, this suggests there's still a lot of runway left for this secular bull. While it's true this economic expansion is four months away from becoming the longest in U.S. history, it ranks relatively poorly in terms of the actual size of the recovery—it's the second-weakest of the 11 post-World War II recoveries, having moved ahead of the Bush recovery the past two years under the pro-growth policies of President Trump. Expansions don't die of old age—they die of excesses, and it's hard at this juncture to find any. In fact, **for reasons we have laid out ad nauseam** in recent months, we expect growth to pick up in the back half of this year, with earnings rebounding and P/E multiples remaining attractive.

2008'S NEAR-ARMAGEDDON LINGERS—AND THAT'S GOOD

Incidentally, it is not simply an odd coincidence that all three of these great secular bulls followed a generation-scarring secular bear. This kind of searing event, that leaves ALL economic players and even government regulators permanently terrified of a repeat performance, virtually insures that the typical excesses that can lead to an economic meltdown (excessive capital investment, excessive lending, excessively loose regulations, excessively easy monetary policy, and excessive optimism on the part of investors that leads stocks to valuations far above present levels) never actually occur. This sets the stage for the secular bull's continued run higher. If you doubt this logic, ask yourself this question: were any of the market pundits whining about "late cycle" in 1999 or 2007, when they should have been? Or have any of your friendly taxi drivers given you the kinds of stock market or real estate market tips they were dispensing freely in 1999 and 2006?

Note too that secular bulls can and do see corrections of 10% for sure and sometimes even 20% to 30%. Most of the 20%+ declines occur around a garden-variety recession or economic soft patch, not a steep economic decline and/or debt crisis. Pullbacks of this kind wash out the weak hands, allow companies to reset and fuel the recovery to new highs that follows. Sometimes, a secular bull will actually experience a 20% decline without a coincident recession at all. In fact, there have been five such declines in the

last 60 years, the latest being the 20% pullback that ended last Dec. 24. Interestingly, when you get a decline of 20% within a secular bull and without a recession, it's time to load up the truck: markets on average rise 27% within the next 12 months. This partly explains why Federated's PRISM® committee has maintained a heavy equity overweight throughout the correction and actually added to that equity overweight in the fall and most recently last week.

So this coming Thursday, let's all celebrate this young bull's birthday with a nice party. Just make sure any gifts are age appropriate.

TAGS

EQUITY | MARKETS/ECONOMY

DISCLOSURES

Views are as of the date above and are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector.

Diversification and asset allocation do not assure a profit nor protect against loss.

Price-earnings multiples (P/E) reflect the ratio of stock prices to per-share common earnings. The lower the number, the lower the price of stocks relative to earnings.

PRISM® is a registered mark of FII Holdings, Inc., a subsidsidiary of Federated Investors, Inc.

S&P 500 Index: An unmanaged capitalization-weighted index of 500 stocks designated to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Indexes are unmanaged and investments cannot be made in an index.

Stocks are subject to risks and fluctuate in value.

Federated Global Investment Management Corp.

2005718742

Federated®

Copyright © 2019 Federated Investors, Inc.