HARD LESSONS OF THE STOCK MARKET

Poole Locke Associates

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If you're like most people, you believe there's a great deal of truth in the adage, "history tends to repeat itself more often than not." That's an important adage to keep in mind when it comes to saving and investing for retirement because it allows you to get a glimpse into the future by knowing something about the past. The fact is, the stock market has been repeating itself consistently enough throughout history to allow us to see some repeatable long-term patterns, or market "biorhythms," which are important to recognize and understand when it comes to building a smart, defensive investment strategy.

First, you need to understand something about what particular "version of the truth" Wall Street and most brokers like to tell when talking about the stock market. Most people have probably been told that the market averages about a 9% return over the very long run. The way that breaks down is that 2-to-3% of this return comes from stock dividends, and 6-to-7% comes from capital appreciation — in other words, a 6-to-7% average growth rate over the very long run.

That may sound pretty good, but you must bear in mind something about how "averages" can be determined and why they can be misleading. If a friend told you that he jogged "an average" of 10 miles per week with his business partner, you might be impressed until he explained that his partner jogged 20 and he didn't jog at all. Together, they do still "average" that 10 miles, so he did tell the truth, but it was a misleading "version of the truth."

That's kind of how that "average" growth rate is determined for the stock market. The way the 6-to-7% breaks down over the long run is that there are huge periods of time where the market experiences extreme volatility, but the net result is zero growth. Then, there are huge periods of time where the market does very well, averaging over 10% growth and often into the 12-to-15% range. Factor zero in with that high range, and there is your 6-to-7%.

Secular Market Cycles

So, what exactly are these huge periods of time that alternate between growth and stagnation? They are the long-term market cycles mentioned above. Specifically, they consist of one long-term secular bull market (growth) period, and one long-term secular bear market (zero-growth) period, which collectively comprise one market biorhythm. Here is the complete history lesson:

From 1899 to about 1921—based on the most commonly available stock market indicators from that time—the market experienced tons of volatility. There were big gains and huge drops, but in the end, all the good and bad years over that long stretch of time washed each other out, resulting in a period of zero growth over 22 years. Right after that came an eight-year stretch (1921–1929) that represented, at that time, the best decade we had ever seen for the stock market. These "Roaring '20s," as they were known, came to an abrupt halt with the stock market crash of 1929 and the start of the Great Depression.

But an interesting note ignored by most history books is that "The Crash" signaled the start of something very much like that 1899 to 1921 period of zero growth. From 1929 to 1954, the market again experienced tons of volatility; big gains and huge drops that ultimately washed each other out, resulting in 25 years of zero growth. Then came another long stretch where the market did incredibly well: 1954 to 1966 was the Eisenhower era, when America was totally on top of its game. Unemployment was very low, and people were making good incomes and living well.

But in 1966, things started to turn again. Once more, we entered a long period, this time almost 17 years, from 1966 to 1982, where the market had major ups and downs that ultimately canceled each other out and resulted in zero growth over all that time. The Dow Jones Industrial Average hit 1,000 in 1966, and in 1982, it was still at 1,000. Then — right on schedule you might say — the market took off and we enjoyed the best bull market we've ever seen in U.S. history for 18 years. In that time, the Dow went from 1,000 to almost 12,000, a 12-fold increase that culminated with the high-flying 90s.

What's even more interesting is that these biorhythms go back even before 1899, to the very beginning of the New York Stock Exchange in 1792. Throughout all of market history, we've consistently seen extended good times (long-term secular bull markets) followed by extended bad times (long-term secular bear markets) that resulted in zero growth.

The 21st Century

So, getting back to the historical progression of these biorhythms after 1899, where do we stand right now? Well, of course, after enjoying the best bull market in our country's history for 18 years, everything turned again in 2000. The new century started with another major market drop, and in the last 22 years, we've experienced tons of volatility and altogether two major long-term drops that have wiped out previous gains and then subsequently moved on to all-time highs.

Let's look closer at these alternating historical cycles and ask ourselves: how long is the average secular bear market, historically speaking, and how long is the average secular bull market? On average, these long bear market cycles have lasted about 20 years or more, while the bull market periods have averaged 10 to 15 years. With that in mind, how long does it take for the market to go through one full cycle or one full biorhythm? The answer is about 35 years.

In other words, statistically speaking, if you have money that you know for sure you're not going to need or want to spend for 35 years, you should, in theory, be able to invest it for growth in the stock market and have it outperform most other investments. That's because, as we've said, over the very long run, the market averages a 9-to-10% return. But now you know just what that term "long run" really means, and unfortunately, there aren't too many people in a position to just sit on their nest egg, or even part of it, for three-and-a-half decades.

What else can the lessons of market history tell us about how we should be saving and investing for retirement in the present? Well, another characteristic of every long-term secular bear market cycle we've been through is that each has included at least three major market drops. As noted, we've had two drops in our current secular bear market cycle so far. Although we had a third drop of around 40% in response to the coronavirus crisis, the market quickly rebounded due to massive amounts of quantitative easing by the Federal Reserve.

A New Age of Economic Uncertainty

This brings up an important point. Ever since the Financial Crisis, the Fed has injected historically unprecedented levels of artificial stimulus into the U.S. economy. Even worse, central banks around the world have followed our reckless lead and done likewise with their economies. Has this practice permanently disrupted the markets' natural biorhythms, or are the Fed's tactics merely delaying the next long-term secular bear market cycle—and potentially making it worse than anyone we've ever seen?

Only time will reveal the answers to these questions. But one thing that's certain now is that all the Fed's artificial meddling and manipulation of economic fundamentals this past decade has created an all-new "Age of Economic Uncertainty." Central banks have turned the global economy into one giant lab experiment. As with any experiment, the ultimate result might be a great success or catastrophic failure. With that in mind, it is especially important for investors — especially those in or nearing retirement — to stay educated, and to make asset protection their top priority.

Cyclical vs. Secular

At this point, you may be wondering why, when you hear a financial analyst on television talking about a "bear market," they never say anything about it lasting 20 years or more. To most analysts, a "bear market" lasts two or three years at most. Here, again, they're telling you an alternate "version of the truth". Remember, one of the key characteristics of a long-term secular bear market is volatility. There are a lot of ups and downs, often lasting several years at a time. These ups and downs are the "cyclical" bear and bull markets that occur within the longer-term secular cycle, and they are what TV analysts prefer to focus on when they talk about market conditions.

Why? Well, it's all tied to what Wall Street does and doesn't want the average investor to know, and its need to speak optimistically as often as possible. It's important to understand that Wall Street knows it can make more money and get more people to invest in their products if people are optimistic and think the markets are going to do well. The reality is that if they talk about short-term cyclical cycles, they can speak optimistically about the markets more often.

Take Action!

Now, how can you start putting the lessons of stock market history to good use today? Simple: By contacting a qualified financial advisor who specializes in the universe of non-stock market investments designed to help generate income through interest and dividends. This is income you can spend if you're retired or that you can reinvest to help grow your portfolio organically, or "the old-fashioned way," with less worry over damaging losses that could impact your life and sideline your retirement plans.

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