KESTREL CAPITAL

Ten years ago, today ....

Introduction - Today, March 6th, 2019 marks the ten-year anniversary of the Global Financial Crisis (intra-day) low for global stocks. On March 6th, 2009, the S&P 500 bottomed at the ominous level of 666, it is now at 2803. To mark the event, we want to take a quick *look back at those extraordinary times*, the *measures taken*, the *market response* and importantly ask the question, **what lessons can be learned?**

Extraordinary times called for extraordinary responses The Global Financial Crisis was the biggest economic shock since the 1929 Great Depression. Central Banks initial response was conventional, they slashed interest rates to zero. They then resorted to more unconventional measures which came in the form of quantitative easing (QE). Simply put, they turned on the money printing press. There is a saying that *"markets stop panicking when policy makers start".* In late 2008, central bankers did panic, and it is no coincidence that the stock market bottomed just three months after QE 1 was announced. Since 2009, the correlation between the major economies Central Bank Total Assets and the Global Stock Market has been 0.94. In other words, they have moved in lock step.

Ten years later, we are still feeling the impact of those policy decisions, ranging from the rise of populism in the political arena, to the current negative interest rate environment. We could argue about the timing and effectiveness of QE. However, I think most would agree that it achieved most of its goals, albeit not perfectly from a wealth distribution point of view. In the past 10 years, Global Central Banks have purchased $12 trillion of assets and slashed interest rates 713 times. These measures flooded the markets with much needed liquidity and risk assets responded positively.

Here is a look at some of the **equity market returns since the March 6th, 2009** low along with the **performance (in brackets) since July 1st, 2007**.

- Europe: Europe +135% (-5%), UK +101% (+7%), Ireland +218% (-34%)
- US: S&P500 +310% (+86%), Nasdaq +487% (+191%)
- Asia China +38% (-21%), Hong Kong +142% (+33%) & Japan +204% (+20%)

Three Lessons Learned?

1. **Diversification is not dead**

- This applies both from a regional and from an asset allocation standpoint.
- Despite the decent returns off the 2009 lows, the Irish stock market is still 34% below the levels seen in July 2007.
- Meanwhile, global equity markets are above their levels seen in July 2007 and moved to break-even from their pre-crisis peaks in Q1 2014.

- In 2007, an investor who had an all equity portfolio experienced a peak to trough draw-down of 51%, that draw-down lasted 16 months and it took a recovery time of 37 months to recoup. The 2007 draw-down wiped out 141 months of the prior gains.
- Meanwhile, for an investor who had a 60% Equity 40% Bond Portfolio in 2007. They experienced a peak to trough draw-down of 29%, that draw-down also lasted 16 months but the recovery time was only 22 months to recoup the losses. The 2007 draw-down wiped out 21 months of the prior gains.

2. **Liquidity Matters**

- As one investor said to us “liquidity does not matter until its starts to matter and when it starts to matter, it is all that matters”.
- As an economic cycle matures, investor’s focus on the importance of liquidity fades. We believe that this is a mistake.
- We believe that it is vitally important that investors know their own upcoming liquidity needs and the underlying liquidity of their investments. A failure to do so, can force oneself to sell assets at discount prices.

3. **Hindsight Bias and there are always reasons not to invest.**

- These are two sides of the same coin. For investors who did not invest post 2009, there were a number of reasons NOT to be invested over the period 2009-2019.
- Likewise, for people who were invested over this period, it is easy to look back at the gains over the past decade and call them “easy”.
- For investors who did not have a disciplined investment strategy in place, they were likely to achieve sub optimal outcomes and by extension, fell short in their financial goals.

Here are some of those events that we lived through in the past decade...

- The early rally seen in 2009 was shrugged off by many as a “dead cat bounce” that lacked any substance and was likely to be short lived.
- In 2011, fears around a Global Recession and the European Sovereign Debt Crisis saw global equities fall 17% in 2 months.
- In 2015, Chinese fears saw markets fall 15% in the month of August.
- 2015 also was the year in which we saw the first interest rate rise from the Fed in nine years. Investors were worried that the global economy’s reliance on cheap money might derail the recovery, these were unfounded.
- In early 2016, markets worried that Chinese growth would trigger a Global Recession. This caused markets to fall -16% in the space of 6 weeks. We also had the Brexit Referendum and Trump Election victory.

- In Q4 2018, fears of aggressive Fed hikes and an escalating trade dispute saw markets have their worst December since the 1930's.

Bottom Line - Despite all these headlines and fears, Global Equities have delivered returns of +189% since the 2009 lows. Understandably, many investors did not want to buy the market "at the top", especially after the scars of 2008 were very fresh. However, one must remember that the S&P 500 trades within a 5% of a record high 60% of the time, and only 12% of the time more than 20% below its last all-time high.