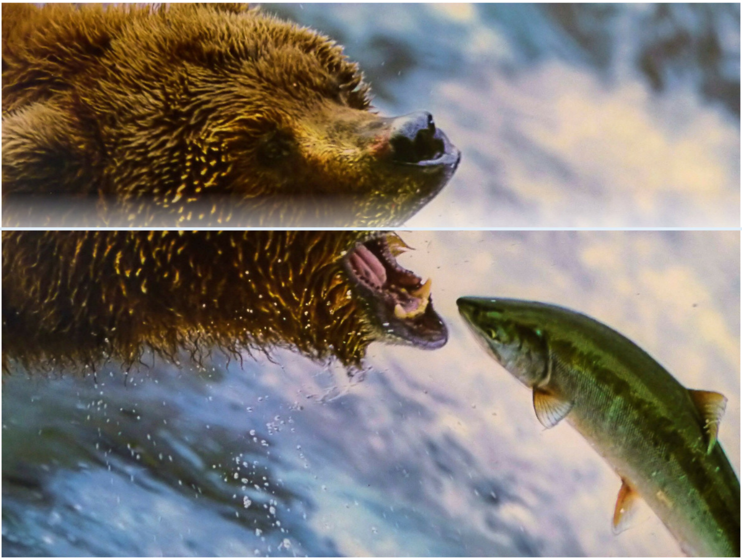
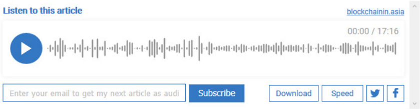
The Great Bull Trap of 2020

5 Reasons We Could Soon See The Buying Opportunity Of Our Lifetimes

Edward Iftody Follow
Apr 14 · 13 min read ★



I think I see an opportunity! — Pixabay



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Record unemployment numbers are announced and the market goes up. Rising death rates and news of community spread showing up in more places around the world, the market goes up. Alarming declarations that patients can get re-infected once pronounced cured and the market goes up.

If you've been confused recently, you're in good company. Investors, investment professionals, and especially CNBC guest analysts now also seem thoroughly confused by recent stock market action.

Today, I will offer 5 reasons why I believe we are somewhere in the middle of a massive bull trap (also known as a bear market rally) very similar to the one experienced in late 1929, and why the next leg down could end up creating the buying opportunity of our lifetime.

In this article;

- **Why the market is rallying**
- **A quick review of the 1929 crash**
- **5 reasons why the next market selloff could be brutal**
- **Historic stock market crashes and recovery times**
- **Final thoughts**

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Why the market is rallying

Some experts still think all the bad news is baked in and we are in the first stage of a V-shaped recovery. This outcome is starting to look more and more unlikely as more economic news becomes available.

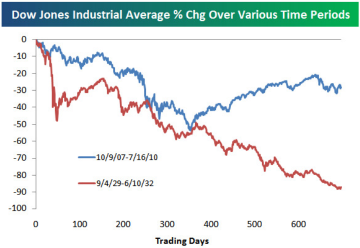
The reasons I think we've rallied so quickly:

1. Initially, there were the pensions and hedge funds reallocating profits from fixed income into over-sold stocks and the unprecedented interest rate cuts.
2. Next came optimism from the enormous amounts of money injected into economies around the world through various salary replacement and corporate bailout schemes.
3. Now I think we are seeing a combination of a short-squeeze (particularly in large-cap tech) and FOMO (Fear Of Missing Out).

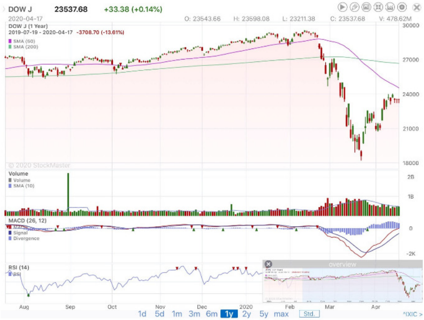
Bear market rallies are confusing and FOMO often draws in inexperienced investors at exactly the wrong time. However, with each passing day, a growing number of analysts and experts now seem to be coming to the consensus that we are in for a long, difficult recovery. I am now firmly in the camp that we should prepare for a deep, multi-month bear market that could last the rest of 2020 and possibly beyond.

It's true, no two bear markets are exactly the same, but looking back to historical models can give us some idea about the future. At this point, the 1929 model appears to be a frighteningly close match. Take a look at the graphs below. There is a striking similarity between the first 100 days of the 1929 bear market and the Dow 2020, up to mid-April. In both cases, there was a sudden, deep initial crash, followed by a significant and relatively lengthy, price rebound.

One significant way the two events differ is that in 2020, it appears modern trading and communication technology are causing events to unfold nearly 2x faster than they did in 1929. In only 30 days, we completed the initial crash and started a rebound. The initial crash in 1929 took about 50 days. The 1929 bull trap took about 100 days to form before the bear market resumed. If the model holds, we could be only weeks or even days away from the completion of a bull trap formation and a continuation of a much longer, more brutal, bear market – and ultimately, a fantastic buying opportunity.



1929 crash in red. Great Recession in blue.



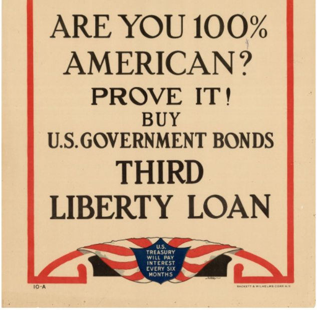
Updated on April 17th — It's looking worse

A quick review of the 1929 crash

Of course, history echoes rather than repeats. The triggers that sparked the two market crashes are completely different. However, while doing research for this article, I was struck by the alarming economic similarities between 1929 and 2020 that I think significantly strengthen the case for a bull trap. So, I've included some of my background research notes to help give more context.

WWI

During World War I, Liberty Bonds were introduced to the public and even celebrity-endorsed by Charlie Chaplin, to help fund the war effort. Many people bought the war bonds out of patriotic duty.



Are you 100% American? PROVE IT! Buy more shares and support the bear-market rally!-https://digital.library.unt.edu/ark:/67531/metadc417/

As you can see at the bottom of the Third Liberty Loan promotional poster, the U.S. Treasury guaranteed payment of interest, every six months.

Although not widely popular with the investing public, Liberty Bonds ultimately introduced average people to the idea of investing savings and receiving a financial reward.

The Roaring 20's

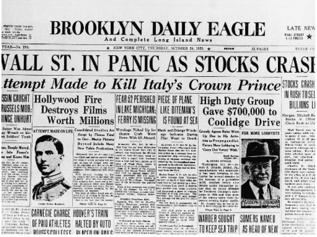
After the conclusion of WWI, there was a huge economic expansion and wealth building, referred to as the *Roaring 20s*. Over time, the public was introduced to stock investing and people started getting a taste for making easy money through publically traded stocks. By the end of the 1920s, there was a kind of general consensus that the stock market would continue to rise forever.

The Roaring 20's — Getty Images

The general public was still relatively new to investing, yet many amateur investors took on debt to invest in the ever-rising stock market. Some people made small fortunes before the bull market finally came to an end, after a strong 9-year run.

Black Thursday

In early 1929, there were signs of economic trouble — steel production and automobile sales were steadily declining, while consumer debt continued to rise due to easy credit. However, markets ignored the warning signs and continued to rise until September of 1929.



BROOKLYN DAILY EAGLE
And Complete Long Island News

NEW YORK CITY, THURSDAY, OCTOBER 24, 1929. 32 PAGES

LATE NEW

VALL ST. IN PANIC AS STOCKS CRAS

ttempt Made to Kill Italy's Crown Prince

STOCKS CRASH IN RUSH TO SEL BILLIONS L

SSIN CAUGHT RUSSELS MOB; INCE UNHURT

Hollywood Fire Destroys Films Worth Millions

FEAR 52 PERISHED IN LAKE MICHIGAN; FERRY IS MISSING

PIECE OF PLANE LIKE DITEMAN'S IS FOUND AT SEA

High Duty Group Gave $700,000 to Coolidge Drive

ATTEMPT MADE ON LIFE

FOR MORE LOBBYISTS

JOSEPH R. GRUNDY

CARNEGIE CHARGE OF PAID ATHLETES

HOOVER'S TRAIN HALTED BY AUTO

WARDER SOUGHT TO KEEP SEA TRIP

SOMERS NAMED AS HEAD OF NEW

Getty Images — https://www.investopedia.com/terms/b/blackthursday.asp

There was an initial one-month leg down that many market participants considered a 'healthy correction'. Although there was a short, small recovery, market volatility steadily continued to rise. October 24, 1929, was Black Thursday — the market dropped 11%.

Prominent Wall Street bankers met to try and figure out how to regain investor confidence and halt the steep selloff of stocks. The bankers decided to pool a large amount of bank money to purchase shares of many of the blue-chip stocks of the day. The markets temporarily recovered.

October 28, 1929, was Black Monday — the market dropped nearly 13%. More cash was injected into the markets by prominent bankers — including the Rockefellers — however, selling ultimately could not be stopped and the stock market continued to crash until mid-November.

Although the initial crash was shocking, what happened next turned out to be even worse. The market recovered around 50% of its losses in a classic bull-trap rally over the next 5 months before ultimately sliding to its lowest low, from April 1930 to July 8, 1932. The total stock market decline represented nearly a 90% slide from peak to trough.

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5 reasons why we could soon see the buying opportunity of our lifetimes

The current market rally and underlying economic conditions share some remarkable similarities to the bull-trap rally of late 1929, early 1930.

1. **Record debt**

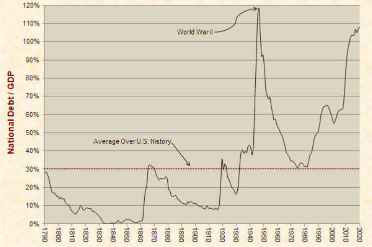
Markets have steadily risen since the end of the 2007–2009 Great Recession. Investors have made a lot of money and like investors of the *Roaring '20s,* even new investors are confidently investing money into ever more risky assets (now, even distressed assets like the cruise and airline stocks).

Although a recession was widely predicted for the end of 2019 or early 2020, the Trump tax cuts suddenly made investing a no-lose game. Stock buying accelerated through the fall of 2019, until the middle of February 2020, when the initial phase of the crash started due to pandemic fears.

Unfortunately, much like at the end of the *Roaring '20s*, household debt is now very high. Household debt now exceeds levels seen during the Financial Crisis. As you can see from the graphic below, National debt is also at levels not seen since WWII — and it's climbing quickly.

It's often quoted many households are unable to absorb even a $400 emergency. Many households are also over-leveraged. In a strange way, the over-leveraging makes sense. Why make extra mortgage payments and pay down debts at low current interest rates when you can make much better returns in the stock market (or lease a new vehicle)?

With everyone currently social distancing, this toxic mix of record household debt and non-existent personal savings could soon implode if workers aren't able to get back to work in the very near future. Without a reliable source of income, many households will have to resort to selling over-leveraged assets, including stocks, bonds, mutual funds, and real estate — regardless of market conditions. If things get really ugly, households will have to start deleveraging completely by walking away from underwater mortgages and leased vehicles.



https://www.justfacts.com/nationaldebt.asp

It's not only households that are over-leveraged. Many businesses are also seriously over-burdened with debt. Even during the epic bull market rally, many economists like Professor of Economics at NYU, Nouriel Roubini, warned of a looming credit crisis. Now, faced with a sudden economic shock, it is clear many businesses will not be able to meet debt obligations without significantly more financial support.

2. Epic financial intervention

Much as the bankers did during the 1929 crash, the Federal Reserve has provided unprecedented financial support in an attempt to reassure and support markets. According to Axios, the Fed will ultimately lend up to $2.3 trillion in an attempt to shore up financial markets.

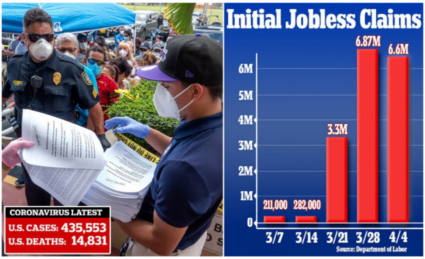
Although financial intervention is intended to create more certainty by removing the risk of a credit freeze, ironically it also adds uncertainty by blurring the price discovery of assets. For example, is Boeing getting a bailout? The answer completely changes the price of the stock. In a similar fashion, a financial intervention can also blur critical business decisions for SMEs (small and medium-sized businesses).

For example, the small business payroll grants don't seem to be going as smoothly as hoped. There are already videos all over YouTube created by small business owners detailing their struggles to access the financial aid — contrary to the assurances of Steven Minuchin.

It seems banks are unwilling or unable to extend government-funded payroll loans to SMEs. Some speculate because there is not enough of a financial benefit for the banks to take on the large about of administrative work. Others have reported banks only willing to extend credit to customers who already have loans with the bank. Perhaps banks fear they will be left 'holding the bag' if they extend loans to businesses that ultimately turn into fraud cases in the future.

Currently faced with extreme uncertainty concerning the availability of payroll loans, many SMEs are faced with the dilemma of keeping employees on the payroll and hoping the loans eventually get extended or firing employees, canceling commercial lease agreements, and hoarding whatever cash they have left in an attempt to save businesses that have taken years to build. I predict many businesses will follow the example of many national and multi-national companies — fire or furlough staff and protect cash balances.

3. Epic unemployment numbers



https://www.dailymail.co.uk/news/article-8204463/New-unemployment-claims-reach-record-6-6-million-week.html

In only a few weeks, millions of people — worldwide — are either now in, or soon will face, unemployment. Some economists believe unemployment numbers could ultimately spike higher than even during the Great Depression of the 1930s.

Sudden mass unemployment is already creating a domino-effect. Both commercial and residential landlords are being faced with significant numbers of renters refusing to pay rent. According to the New York Times, perhaps 31% of renters cannot pay rent.

Commercial real estate landlords all over the world might be in even more trouble. Many are leveraged themselves and now face corporate renters like Staples, who are unwilling to pay rents during government-mandated lockdowns.

Even if lockdowns end soon, no credible scientist thinks we will be able to remove significant amounts of 'social distancing' without risking more waves of infection. (In fact, both Hokkaido and South Korea are already seeing new outbreaks). It seems clear, both residential and commercial landlords will face significant financial pressure in the near future. It now seems certain, some will fall into bankruptcy.

4. Long-term reduction of consumer activity

Like during the 1930s, large numbers of unemployed over long periods of time will ultimately lead to significant long-term reductions of economic activity due to significant supply and demand destruction.

Non-essential businesses all over the world, are currently facing complete business cessation at the order of governments and health experts. Restaurants, hotels, and many other service industry businesses face a serious and totally unexpected, business threat.

Even when lockdowns are relaxed, people aren't going to risk getting quarantined on a cruise ship. People aren't going to risk getting trapped in a foreign country for the sake of a vacation. Restaurants will be forced to offer only take-out service or allow only a significantly reduced number of patrons to enter and dine within the restaurant, severely limiting profitability.

[redacted]

As mentioned above, the CARE and Paycheck Protection Program has not been going as smoothly as hoped. Even if lockdowns DON'T drag into months, a large percentage of these businesses might ultimately be forced to permanently close. This could leave large numbers of landlords with non-performing real estate, and force perhaps millions of more workers into unemployment, compounding an already bad consumer activity slump.

5. A vaccine looks increasingly, far away

Donald Trump wanted people back to work by Easter. Shinzo Abe apparently believed if he ignored the virus, he might be able to save the summer Olympics. It seems neither leader initially listened to the scientists.

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Over 60 percent of people surveyed in Japan last month said the government was not handling the coronavirus outbreak...

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However, the scientists have continued to beat the same drum, over and over. Social distance, test, isolate. Yet, without a vaccine, there will be no long-term solution to the economic side-effects caused by this pandemic.

Although our world leaders seem to now understand the seriousness of this virus, I don't think all of them have come to terms with the fact of how long it might take to find a vaccine. Dr. Fauci has repeatedly stated there will be no vaccine for a year or 18 months. More recently, I have heard some physicians and thought leaders like Bill Gates say we might have to wait 18-24 months or more for a vaccine to be globally available.

A document recently leaked to the New York Times suggests we will have to remain at least partially locked down for many months if we don't want to experience more spikes in deaths. Twelve months of a partial lockdown will be terrible for the world economy. Twenty-four months will be absolutely devastating.

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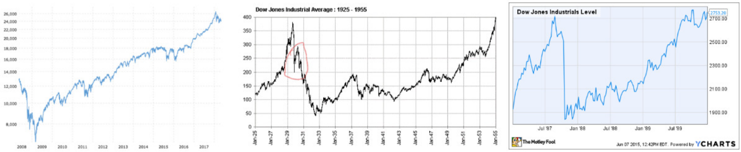
INTERVIEW:
BILL GATES

Bill Gates thinks a vaccine won't be available until the Fall of 2021.

Historic stock market crashes and recovery times

Top highlight

Major stock market declines typically take years to recover. Why will the 2020 stock market crash be any different?



Great Recession, left — 1929 with bull-trap circled in red, center — 1987 Black Monday and subsequent recovery, right

Final thoughts

It's hard to ignore how many of the preconditions that helped set the table for the 1929 crash and subsequent bear market rally are present again in

2020;

- way too much leverage
- too many exuberant investors
- and too much faith in policymakers' ability to solve the problem.

Some might argue our financial tools for fighting a market downturn have come a long way since the 1929 crash and ultimately financial intervention will save us. Yet even if the financial tools at our disposal are superior today than they were in 1929, it seems in 2020, we've been hit by the perfect storm. In addition to all the same problems we've repeated from 1929, we also have;

- record unemployment claims due to a sudden stop in economic activity,
- record debt levels that appear completely unsustainable in a suddenly stopped economy,
- a currently incurable virus that makes re-starting the economy difficult at best,
- and a general public who are not willing to sacrifice people for the sake of stock prices.

The Federal Reserve and Congress have worked hard to shore up the credit market and Jay Powell says the Federal Reserve still has a lot more ammunition to fight this downturn. Yet, I think the efforts may ultimately prove futile if a vaccine cannot be found soon.

In the long run, I think today's financial intervention techniques will prove to be as ineffective as the direct stock-buying scheme was in 1919. Rather than curing the problems, all of the fiscal stimulus and bailout money has simply created a more enticing bull-market trap for investors to chase.

If I were talking to a friend, I would caution against FOMO at this point — don't chase this rally. Everything has to go right for this rally to continue and there's so much potential for things to go wrong. Why not stay on the sidelines for now? If it turns out we are in the middle of The Great Bull Trap of 2020, then patience will be rewarded with one of the greatest buying opportunities of our lifetime. If I'm wrong and we've already started a new bull market, there will almost certainly be better entry points to add to your stock positions in the near future.

Disclosure — I hold approximately 95% cash as I publish this article. Please seek professional advice before making any investment decisions.

I'm Edward Iftody — If you'd like to learn more about disruptive investing, I encourage you to read more at www.blockchainin.Asia

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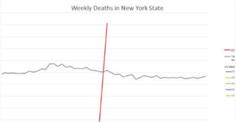

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