

# STUDENT OF THE MARKET RESEARCH

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The following piece documents the remarkably similar reasons why the bull markets of 1929 and 2000 were unique and should run forever.

Despite this reasoning and with remarkable fidelity, they both lasted for 116 months. That's from the top of the last business cycle with the old era of inflation to the euphoric climax of speculation.

## BULLISH FOREVER

### NEW FINANCIAL ERAS: 1990s AND 1920s

The enthusiasms in projecting most new financial eras seem to naturally group into four main reasons. The first is the new era itself, followed by the political shift from left to centre as CPI inflation diminishes with rejuvenation in Europe and opening of new consumer markets. Other points are the celebration of high technology and cost-cutting which were prompted by intense price competition in a disinflationary period. The end of the old era of inflation also provided the appearance of new found discipline in monetary policy.

The 1920s examples are from the well-known article by John Moody in the August, 1928 edition of The Atlantic Monthly. The examples from the 1990s were collected as they appeared in the Wall Street Journal.

### NEW ERA

**WSJ 1990's:** " Most Wall Street forecasters ... are still scrambling to come up with explanations [for the dramatic rise]. Most people don't realize that there has been a change in the nature of the U.S. business cycle.

**WSJ 1990's:** " Experts who watch the economy see reason for reassurance ... that several [longer] trends are coming together to fuel a global growth wave that is unprecedented in size and scope. We've entered a golden age that will last for decades."

**MOODY 1928:** " Nearly all of the accredited seers and economic experts have been at a loss to explain it. The mistake ... is to assume that times have not fundamentally changed. They have changed ... and we are in a new and remarkable era."

### POLITICAL SHIFT

**WSJ 1990's:** " The rejection of socialism by much of the developed world has also led to greater opportunity for low-cost production from these countries."

**MOODY 1928:** " All the European calamity prophets have been continuously discredited [and] there is a real possibility of a general renaissance developing ... during the coming generation."

**WSJ 1990's:** " The move to freer markets, in countries where state control stifled commerce in the past, is the best thing for prosperity you could possibly have."

**MOODY 1928:** " [O]ur own experiment in government operation of the railways had gone far to slight the ... propaganda of ... public ownership. After ... the restoration of the railroads to their owners, a remarkable increase in the speeding up of deliveries ... developed."

## HIGH TECH AND COST CUTTING

**WSJ 1990's:** " Dramatic enhancements in computer chips and software are revolutionizing every productive activity in U.S. companies ... Costs are dropping rapidly ... Companies are constructing factories where it makes the most economic sense – a cost cutting activity."

**WSJ 1990's:** " Technological innovation ... creates new industries and mutes business cycles."

**MOODY 1928:** " [D]eclining tendency in commodity prices ... narrowed profit margins. A very direct impetus was thus given to the modern effort toward the more scientific development of mass production and distribution and the cutting out of waste."

## REFORMED MONETARY AUTHORITY

**WSJ 1990's:** " Post World War II business cycles have [had] their stops and starts coming from identifiable tightenings and loosening [by] the Federal Reserve [but if inflation has peaked] the Fed's vigilance has paid off."

**WSJ 1990's:** " Monetary austerity and fiscal restraint are bolstering growth." " Most economists believe [less government economic stimulus] helps reduce inflationary pressure."

**MOODY 1928:** " Another vital fact which had gone far to stabilize fundamental financial and business conditions ... was the founding of the Federal Reserve Banking System ... The old breeder of financial panics, the National Banking Law, which had been a menace to American progress for two decades, had been replaced by a modern, scientific reserve system which embodied an elastic currency and an orderly control of the money market."

## EXQUISITE IRONIES

Under mounting credit pressures usually associated with the top of the great boom in 1873, the leading New York newspaper editorialized that the treasury system was superior to a central bank in sustaining the boom. "True, some great event may prick the commercial bubble, and create convulsions; but while the Secretary of the Treasury [U.S. was at that time between central banks] plays the role of the banker for the entire United States, it is difficult to conceive of any condition or circumstances which he cannot control. Power has been centralized in him to an extent not enjoyed by the Governor of the Bank of England. He can issue the paper representative of gold to the amount of scores of millions."

However, experts today imply that only a central bank has the necessary omniscience and power. The following, from the Financial Times in 1997, recorded the modern view: "The classic danger is of an unchecked panic, resulting in bank collapses and a sharp contraction of the

money supply. Yet such a crisis can always be halted, since there is no limit to the money a central bank can create."

## DURATION

The discovery of long term bullish reasoning and, in some cases, the closeness of the phrasing shows that great financial booms are remarkably similar. This makes sense as all six new eras followed an equivalent mania in tangible assets. Then shifting political forces and investor preferences eventually created a great speculation in securities. These typically completed in a dramatic climax in the ninth year after the last business cycle top of the old era of inflation.

Where monthly data have been available, the new era that completed in September, 1873 lasted 115 months, the September, 1929 example for 116 months, and the March, 2000 one at 116 months.

The last two are shown in the following New Era Duration charts. The consequent bear markets lasted from 1873 to 1878 and from 1929 to 1932.

ANNUAL DATA	
END OF "OLD" ERA OF INFLATION	DRAMATIC CLIMAX OF "NEW" ERA
1990	March 2000
1920	September 1929
1864	September 1873
1816	May 1825
1763	June 1772
1711	June 1720

## OBSERVATIONS

The duration of each new financial era shows little variation, but there has been considerable variation in the degree of speculation. Until our glorious example, the South Sea Bubble of 1720 was the most notorious. The Bank of England was the senior central bank and, as its shares were publicly traded, it was the premier stock. In the bear markets before and after 1720, it traded down to a 6% dividend yield. At the height of the 1720 folly, it traded at 3%. This, of course, has been the limit on the Dow on all bull markets from the 1920s until the 1990s when it reached 1.1%.

By this measure, our era of reckless speculation by investors and the senior central bank exceeded their incredible behaviour during the South Sea Bubble.

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