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Half-Century of Tradition Says Stocks Bounce Back Quickly

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If you're reaching that point where you're inclined to dump whatever stocks you have left, first consider this.

A money manager's study shows that during the past 50 years, the stock market has recovered 80 to 100 percent of its decline within six to 12 months after hitting a bottom.

"The most powerful and important advances within a whole market cycle occur when coming out of economic slowdowns and/or recessions. If you are not in the market during these periods, you sacrifice the period that is most responsible for allowing stocks to outperform all other asset classes over time," says James Demmert, a money manager with **Main Street Research** in Sausalito.



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This is not to suggest that stocks have hit bottom or that you should be loading up on stocks. Rather, it's a warning about the dangers of being out of the market when things look bleakest.

"People look at a market like today and say, 'I just can't stand it. I'm going to sell,' when they should be doing the opposite or at least standing their ground," says Demmert.

The Leuthold Group, a money management firm in Minneapolis, confirms that the best time to be in the market is when the economy is the pits.

Since 1945, there have been 10 recessions. On average, these recessions have lasted about 12 months, and the market has bottomed about six months into the recession.

Twelve months after hitting a bottom, the market was, on average, 36 percent higher.

"If you bought the stock market halfway through each recession, you would have done extraordinarily well," says Jim Floyd, a senior analyst with Leuthold. "The problem is, how do you know where you are?"

A recession is defined as a period when the nation's gross domestic product shrinks for at least two consecutive quarters. During the fourth quarter of last year, the GDP was still growing, albeit at a lethargic 1.1 percent rate.

Some economists suspect that GDP growth turned negative in the first quarter of this year, which ended Saturday, but we won't know for sure until the end of this month.

"If a recession started in December of 2000, you might expect it to be over at the end of this year," which means May or June would be a good time to buy stocks, says Floyd.

He explains that the stock market tends to bounce back swiftly because "there's panic selling at the bitter end; things go too far on the downside just like they do on the upside. Once people determine that the worst is over, there's a flood of money and things go back pretty quick."

What happens after the initial recovery, however, depends on economic growth, inflation and interest rates prevailing at that time.

After an excruciating bear market that ended in December 1974, the Dow Jones industrial average was within 90 percent of its all-time high 13 months later.

After that, the market essentially went nowhere for more than six years, largely because of "major structural problems (such as double-digit inflation) that do not exist today," says Demmert.

If you can look beyond the current crisis -- which is caused mainly by slowing demand and overcapacity throughout the high-technology industry -- there are reasons to be bullish long term.

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