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# 5 things to know about market upheavals

## To survive and even thrive in volatile times during the pandemic, it pays to be conservative and beware dangers of market timing

Financial markets started the year with a sense of optimism, with the signing of the phase one trade agreement by the United States and China in mid-January.

Then came the coronavirus pandemic and the S&P 500 finished with its worst quarterly performance since 2008.

But just when investors were bracing themselves for a further downturn this month, the market staged a large surprise bounce before the Easter weekend.

The worst quarterly decline was greeted by a record rally – the largest weekly gain of S&P 500 since 1974 and the best two-week performance of the Dow Jones Industrial Average since the 1930s.

Similar patterns of volatility appeared in other major markets and, not surprisingly, this has injected fear and confusion in many investors' mind.

Here are five things that may give you a sensible framework to think clearly about the market turmoil.

### 1. What drives the unprecedented volatility?

Widespread lockdowns to contain the pandemic have brought global business to a virtual standstill.

From late February, the fear of an ensuing recession caused investors to dump stocks indiscriminately, and abruptly brought to an end the longest bull market in the United States. The panic selling was so bad that rarely used circuit breakers were activated to halt trading four times.

In the meantime, massive fiscal and monetary packages announced by the US and other countries give the market hope that the economic damage from the Covid-19 crisis could be quickly contained and that the ensuing recovery would likely be swift and sharp.

Stocks launched several rallies from late last month and recovered much of the early losses.

An increasingly important force driving flash rallies and flash crashes – occurring 16 times since March 1 – is the rapid rise of high-frequency trading. Machines armed with natural language processing can now react at lightning speed to headline news such as unemployment and trade data, exacerbating the extent of market swings.

The US stock market has been roiled by increased volatility amid the coronavirus crisis. For example, the S&P 500 suffered its worst quarterly loss since 2008 but recovered with a record weekly gain. PHOTO: AGENCE FRANCE-PRESSE

### 2. Know what you don't know

Following work resumption in China in the middle of last month, markets had a V-shaped rebound.

The S&P 500 rose 18.6 per cent in three weeks starting on March 23. The Straits Times Index went up 12.2 per cent in the same period.

The drastic reversal of market sentiment appeared to be based on optimistic belief that the worst of the pandemic may be over.

Reality, however, is far more complex and full of uncertainties.

While the White House touts research indicating the quick end of the outbreak by the summer, new research by a team of Harvard scientists suggests that social distancing measures may need to be in place until 2022.

Investors should recognise the danger of placing bets based heavily on one's optimistic interpretation of the Covid-19 outlook while much of it remains unknown and unpredictable.

### 3. Brutal truth about market timing

The surge in market volatility creates deceptively attractive lures to buy low and sell high, making easy money quickly. As a result, trading volumes have increased sharply.

The truth, however, is that few can time the market consistently. A popular approach is to infer from past crises about the possible resolution of the current one.

History, however, does not simply repeat itself. For example, it took only 18 days to drop 30 per cent into a bear market in the current crisis while other black swan events in the past took at least 55 days in the US.

Furthermore, the subsequent rally of nearly 20 per cent from late last month was also viewed as an anomaly owing to the unusually short duration of the preceding downturn.

### 4. There are no bold, old investors

Bloomberg recently reported that more retail investors in Singapore are leveraging debt, through advances from credit cards and loans using one's home as collateral, to buy shares. Data from the Monetary Authority of Singapore also indicates a notable increase in bank financing for share investment.

Taking on debt in today's volatile markets carries a risk beyond one's control. Indeed, flash crashes last month triggered many margin calls.

Investors who stay in the market long enough know that unthinkable events do occur.

For example, Luckin Coffee's share price reached as high as US$51.38 in January before the coronavirus outbreak in China drove it down by 50 per cent. Just when some brave investors started bottom fishing, the stock fell off a cliff, down by an additional 81 per cent on April 2 after the company admitted to accounting fraud.

Investments require taking on calculated risk. However, speculative bets using excessive leverage are less likely to survive many periods of market volatility.

### 5. Conservative investors sleep well

Positive signs are emerging – the road to recovery has started in China and some European countries, and last month's trade data from China is better than expected.

But a new International Monetary Fund report paints a rather grim picture: The lockdowns on a global scale have led the world economy into a recession, likely the worst since the Great Depression in the 1930s.

Volatility is here to stay. If history is an indicator, adopting a conservative approach, by following the 4As, will serve investors better.

- Avoid leveraged finance so you do not have to face forced sales when the market suddenly tanks.
- Avoid companies whose high valuations rely largely on future promise and whose income statements have yet to show meaningful operating profit.
- Adopt a globally diversified portfolio using low-cost and highly liquid index exchange-traded funds.
- Abandon the notion of "cash is king". Hoarding cash now seems an ostensibly safe strategy to many. True conservative investors with a long-term horizon would instead deploy cash aggressively into high-quality shares when a window of undervaluation appears in the midst of market panic.

To end, I would like to quote from famed investor Henry Kaufman: "There are two kinds of people who lose money – those who know nothing and those who know everything". Overconfidence, pervasive in the investment world, is an underappreciated risk. So be cognisant of what you do not know and truly appreciate the danger of market timing. Being conservative would help one to survive and even thrive in volatile markets.

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