

## **Global Financial Markets: Standing on the cusp of History**

### **Our World of Spirituality**

Over the last few weeks and months, we have been inundated with responses from our readers on the various aspects of our unconventional model of spirituality. In particular, miracles and whether we believe in their possibility has been a relatively common subject that we thought would be interesting to talk about. Here we go:

Yes, we do believe in miracles and have been blessed to experience and be a part of many of them and they did completely revolutionise our very existence. Giving a little background, we have believed since the age of 13, that the realization of "I" or "me", our consciousness, is the biggest miracle in this universe. We used to be completely fascinated with the idea of somehow calculating the numerical probability of experiencing the consciousness of "I" from the time of the Big Bang that happened about 14 billion years back. This probability is quite obviously a number infinitely close to zero and yet "I" exists in billions of minds all over. If we get the most sophisticated super computer in the world to calculate this probability we would probably need another computer to calculate the number of zeros in it! We thought at that time that a life time is too short to be sufficiently vowed by this miracle and resolved to spend the rest of our lives only experiencing what this life, and this consciousness, has to offer.

And then some time back, we experienced yet another miracle, in fact a bigger one, which completely blew our minds away. This was when we first experienced the incredible feeling of the "I" melting away. Some how it felt that our perception of "I" itself is undergoing a change. "I", quite miraculously and indescribably, expanded way beyond our own consciousness, and the consciousness of our fellow beings became a part of our own perception of "I". This may sound insane but we actually mean and stand by every word of it. This was a miraculous feeling and somehow felt like we could live a million lives all at the same time. And till we had this experience, we had thought that living one human life is the biggest miracle and blessing that could have happened! This change in our perception of "I" became a defining moment for us and has become our version of reaching a state of super consciousness.

Miracles to us are not about walking on water, moving mountains or bringing people back from the dead. Miracles are about overcoming our greeds and fears; miracles are about being able to live a million lives all at the same time; they are about destroying forever all mental walls and barriers, that we habitually create around us; they are about being in a perpetually self reinforcing virtuous cycle; they are about achieving a state of bliss irrespective of our physical world and state; and they are all about eternal love, empathy, hope and positivity.

We exhort our readers to seek health, knowledge and consciousness; find love and empathy deep within; to aim for an incorruptible purity of thought, absolutely uncluttered clarity of mind and an unbreakable and unshakeable strength of resolve; and we can guarantee that you would experience your own miracles, may be, not very dissimilar to the ones we were quite miraculously blessed with. And last but not the least, why live just one life when you can actually live and experience millions of lives all at the same time!

### **And now back to the markets!**

History is not just about the bravado of bull markets; it is at least as much, if not more, about the pessimism of the bear markets and the eventual emergence of an omni-potent fear and a sense of existential crisis at the point when long term bottoms are made. In fact, the market crashes and brutal bear phases of the last 100 years are much more engraved in our collective psyche than the bull runs that have captivated our imagination from time to time. We believe that we may be perilously close to one such time in history.

In our previous Newsletter dated March 19, 2017 (<https://www.linkedin.com/pulse/global-financial-markets-miraculous-confluence-macros-amit-goel>) we had argued in favor of deflation of the Trump trade and we are happy to report that the same has by and large played out in the Currency Markets, Bond Markets and Commodity Markets over the last 10 weeks or so. US Dollar Index has been hammered by more than 5% since then; US 30 year Treasury Yields are close to their multi month lows; Gold is not too far from its 2017 highs; and Industrial Commodities have

all corrected and Bloomberg Commodity Index is quite close to its 2017 lows. Having said that, we do most humbly accept our failure to read the tea leaves in the Global Equities setup. We believed, erroneously in hindsight, that the deflation of the Trump trade would have its natural consequences on the Equity Markets too. In reality, Equity Markets have not only resisted heeding calls of sanity but have actually made higher highs and are still pretty close to those highs, as we speak. This disconnect between equities and other asset classes is absolutely unprecedented and not seen before in recent market history. While this was not our base case, we did observe this divergence opening up in mid April. This divergence can at least partly be explained by the following:

1. While Global Equities have been, by and large, in a pretty consistent bull run right since March of 2009, the picture in other asset classes has been much more mixed over the last 7-8 years. Many of the Industrial Commodities actually peaked out in 2010-11; most others did so by 2014; Gold made its multi-year lows in 2015 and not in 2017 (as conventional wisdom would have us believe), US and European Bonds peaked out only by mid 2016 and not much much earlier; and the Dollar index has been largely sideways since March 2015 (though it did eventually make its peak with the Trump trade in early 2017). Hence one can clearly infer that global equities have become, since 2015, the only brand ambassadors of this unprecedented global bull run of 2009-17 and have come to truly symbolise and epitomise the global economic recovery of this decade. This confidence and unshakeable conviction of equities, as an asset class, is now getting reflected in the behavior of countless equity investors and traders all across the globe, who by now swear by the equity cult like never before.
2. Equally importantly and as a logical extension to the above, it is the lack of opportunities and faith in other asset classes that has reinforced equities as practically the only investment of choice for billions of investors the world over. Commodities peaked out long time back making investments in commodities as well commodity businesses relatively unattractive in the last few years. Fixed Income returns in dollar terms, on a risk adjusted basis and after accounting for inflation, have been largely negative over the last few years. Whatever real returns investors have made in Fixed Income in last few years, have largely arisen out of playing duration or by taking credit calls. To highlight this, one can point towards the Trillions of dollars of global funds that are currently invested in bank deposits or government bonds at negative real, and even negative absolute rates especially in Europe and Japan. Gold peaked out more than 5 years back and hence has largely lost its lustre as an investment proposition in the last few years. Real estate has undoubtedly given superior risk adjusted returns, especially in US, UK, Canada, Australia and many emerging economies too, but because of its inherent opacity and liquidity issues commands only a fraction of global investors' money compared to the much more liquid and easy to reach out alternatives like Equities and Fixed Income.

The above two factors have resulted in the emergence and rise of the Equity cult, like never before in capitalistic history. Its sheer indispensability and dominance has also made the current equity bull run the biggest bubble of all times. This bull run also commands the distinction of being the most resolute, stoic, and stubborn bull run ever, a bull run which is almost immune to every possible Geo-political event, unfavourable economic data or even the sheer insanity and hollowness of a Trump presidency. In fact, what has practically wiped out the equity bears to extinction is not just the immensity of losses they have incurred over the last many years of equity bull run, but also the sheer frustration of seeing every bit of bad news being countenanced and ignored, without even the slightest bit of trepidation, by this audacious bull market. The sheer complacency of traders, investors and even fund managers, especially in the last 6 months, will make it go down in the echelons of history as the most gloriously entrenched and an all encompassing, omnipotent bull run in human history. The fact that CBOE VIX was less than 10 sixteen times this year, and that number is more than 50% of the total number of times it has gone below 10 in last twenty five years, is a mute testament to the above.

#### **Is the Bull Run over, or more importantly, will it ever be over??**

A bull run with infinite conviction and complacency (like the current bull run) usually does not die of bad news. More often than not, it dies of good news and the consequent euphoric climax that results from it. In fact, a bad news often goes to strengthen the bull run by providing an opportunity to the staunchest of bulls to further add stocks from the relatively weaker hands and at somewhat lower prices. On the other hand, good news often gives an opportunity to the smartest of players to encash the euphoria and look for pockets of under valuation elsewhere. It is practically a "Mission Impossible" (and also fraught with incalculable risk) to try deciphering successfully as to

which good news can trigger the climactic euphoria that might define an eventual top for the bull market. It is however, useful to realize that irrespective of the conviction and the sheer brute power of the bull run, there would come a time when the bubble will eventually get burst because of its sheer magnitude, unwieldiness and the physical and psychological limitations of the maximum possible bubble size. We believe that the current equity bubble has hit those limitations in recent weeks (after 8 weeks of one sided bull run on global equities) and the recent successful climbing of the proverbial and insurmountable wall of worries including Comey's testimony, ECB's monetary policy decision and the UK elections all at the same time, has given us the much needed climactic and euphoric burst that we were looking for. As a tell tale sign (or are we reading too much into it?), we did see some correction in US Tech stocks on Friday, and that to us looks like a harbinger of things to come. Yes, we do believe that the greatest equity bull run in human history may have come to an end, and the bubble bursting should truly begin from the coming week, if not Monday itself. We do understand that predicting the bubble top and acting on the idea can be life threatening, but we believe that this is as good a time as any, for us to stick our necks out and hope that the same won't be chopped off!

#### **What may happen now??**

The markets will probably correct rather gently to begin with as there are still some folks on the sidelines waiting to buy a possible correction. However, as this progresses and markets go down further, more and more traders would get an inkling that this is a medium term reversal and not just a healthy little correction. The trickle would eventually become a torrent, may be in about 3 weeks, and would finally pave the way for an inevitable climax of despair. Finally but surely, there would be a panicky stampede for exit and that would put in place a short term to medium term bottom.

#### **Which are the biggest bubbles in the world equity markets today?**

While the whole global equity class fits the bill for a gigantic bubble, there are certainly markets and geographies which are looking more vulnerable than others. We believe that NASDAQ 100, FANGMA (Facebook, Amazon, Netflix, Google, Microsoft and Apple), S&P 500 and some Emerging Markets like Taiwan, South Korea, MSCI China, Hangseng, Singapore, Indonesia, India and Pakistan will fall more sharply than others. Within the major geographical markets some sectors will be more vulnerable than others. For example, Canadian and Australian Real Estate, Indian Private Banks and NBFCs, American Autos and Brick and Mortar Consumer Discretionary Retail, Taiwan and Korea's Technology Sector, Banks in Australia, Brazil, Hong Kong and Singapore may be the worst hit. We believe that emerging market currencies particularly Mexican Peso and those of East and South Asia will go into an extended bear phase.

#### **The Trajectory and the phases**

The bear market should play out from June 2017 till December 2018. We have broken down the stages into following: **Phase 1A**, **Phase 1B** and finally **Phase 2**. We believe that these phases may well capture about 80%, if not more, of the ensuing bear market.

We believe that **Phase 1A** will play out from June till the beginning of July and will cause the maximum damage to the more vulnerable markets mentioned above. We expect all global equity indices to fall between 10 and 20% depending on their respective vulnerability quotient. **Phase 1B** should play out from the second half (or end) of August till the end of October and should result in another 10-20% fall. However, between Phase 1A and Phase 1B there should be a sharp recovery in the markets and equities may retrace 35-65% (depending on the sharpness of the previous fall) of their losses suffered in Phase 1A. This is because the conviction of an 8 year old bull market will not die so fast and most traders and investors may be misled into believing that the fall was just a bull market correction and not the beginning of a long term bear market.

The **Phase 2** would happen well into next year and we may be in a better position to understand the dynamics only once the Phase 1 is over. Some time in between, FED would step in and start taking down the interest rates, which would certainly give some temporary relief to investors and traders, but only as much.

#### **Where to hide???**

For the long only folks, the best investments for the next 2 years in general and for the next four weeks in particular, would be Euro, JPY and Gold; US 30 year Government Bonds (along with the necessary currency hedge to Euro and

JPY) would also be a brilliant investment. For hedge funds, apart from going long on Euro, JPY and US 30 year Treasury Futures, going short on NASDAQ 100, FANGMA stocks, Indian BANKNIFTY, and indices like Hangseng, DAX and KOSPI should do the trick. Shorting EM currencies against Euro and JPY can be a multi bagger idea too.

### **Indian stocks**

We have decided to devote this particular section to the Indian context as we believe that there are some special circumstances which may well define the market reversal that we are about to witness there. Apart from the usual exuberance and swagger, which by definition characterise any equity bull market, there is this almost fanatical zeal and a religious missionary like faith and conviction about this bull run that makes the Indian situation very special. Indians have truly come to believe that this is their century, and it will witness the emergence and rise of India as a truly global superpower both economically and politically. While the size of the bubbles are not strictly comparable, we have rarely come across this kind of synchronisation and reinforcement between faith, ideology, polity and the animal spirits of the financial markets. The belief system, conviction and faith and also the reinforcement and sync with financial markets are not very dissimilar to what we saw in Japan in late 80s, or the Asian tiger economies in mid 90s. However, the end game and the economic evolution will most certainly be very different.

India, given the conviction and the size of the bubble, would in all probability lead from the front in the ensuing bear market. The proposed introduction of GST from July 2017 and the consequent economic uncertainty will only make the reversal in the markets more brutal. The ongoing agitation on farm loan waiver threatens to become a countrywide movement and is being cheer led (may be even stage managed) by the opposition parties which have been nearly decimated by the ruling coalition in one election after the other. This could emerge as yet another threat to the magnificent bull run that we have witnessed in the Indian markets. We believe that Indian equities and the INR may become one of the worst performing equity markets and currencies respectively, over the next few weeks.

### **The probabilities**

We believe that the probability of a full fledged bear run hitting the equity markets over the next 4-6 weeks is as high as 60%. Probability of just another bull market correction is about 20%; balance 20% being the probability of the bull market continuing unfazed and unabated as it has in the last 8 weeks.

### **On the sidelines - Is Trump the new normal????**

Just when we were about to write off Trump as a freak and a one off in world history, the world of politics has challenged our understanding yet again! What kind of infinite shamelessness and insensitivity does it take to be who Theresa May has become of late. After leading a disastrous and suicidal campaign and leading Tories into what is certainly a moral defeat for her and her party, she refuses to step down and is pretending to be the leader of the party and an almost inevitable choice to be the next PM. We are appalled! Only slightly less spineless is the reluctance of her party leadership to bear with her shenanigans rather than prop up another name to lead the party, even if that name happens to be that of Boris Johnson!!

**Stay blessed, seek higher consciousness and enjoy your journey!!!!**

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