

Timing - Long term

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Major Sharemarket Top:

A bull market of similar strength to that of 1993 should last until early 1998. As this will complete a long 9 year cycle (11 years from the 1987 top) a substantial bear market is likely to follow.

The bear market is likely to last 1½ - 2 years and be of similar magnitude to the decline of 1980 - 1982 when the All Ords. fell 38%.

Following on from this bear market low, the ensuing bull market should be very strong, comparable to the 1980's and the lead up to 1987. A top around 2006 would be equivalent to the tops of 1969 and 1987 as they were the end of an 18 - 23 year cycle.

Gann said that every 20 years there is a severe recession and every 20 year cycle (60 years) there is a depression. According to Gann's theory we should have had a depression starting in 1989 - 60 years after the 1929 crash. In 1989 the Japanese stockmarket peaked and began a severe decline which ended in a fall of 63% from its peak. The 1980's property boom also peaked in 1989 and commercial Real Estate fell about 50%. We have not experienced a depression, however it has been a very severe recession and some countries such as Russia **have** had a depression.

For the world economy, a depression is unlikely to occur until well into the next decade as the expanding economies of Asia and advances in technology have respectively increased demand and increased efficiency. Better financial management and the willingness of governments to do whatever is necessary to avoid an economic collapse has probably delayed this expected event.

The next critical time will be at the end of the next 20 year cycle which is expected to be 2006 - just over 18 years from 1987. A market decline of over 50% from the top over a period of 2 - 3.2 years can be expected if the decline is short and sharp or 5-5.5 years if a prolonged fall takes place.

In 1929 the market took three years to reach it's low and the fall from the 1969 Poseidon boom took 5 years which is an indication of how the market performs after a 20 year high. The fall from 1987 was 3.2 years. The duration of the fall may be dependent on the extent of the extremes reached in the preceding bull market. If the economy is well managed, an orderly decline over a long period could be expected, otherwise a mismanaged world economy could result in a crash in shares and property - in fact all real assets.

As far as the economy is concerned the 1990's can be compared to the 1970's when, following the severe recession of 1994, the economy remained flat with only a mild pickup at the end of the decade. The recession of 1982 marked the end of a difficult economic period and ushered in an era of apparent prosperity. The general business environment continued to improve through the 1980's culminating in a peak in economic activity in 1989 which coincided with a major peak in Real Estate.

The next decade should be comparable to the 1980's and a feeling of prosperity should prevail. This prosperity will be built on borrowings however and will not be sustainable. Extremes in credit creation eventually result in severe contractions to reign in inflation and liquidate debt.

Rising interest rates increase borrowing costs to companies and those with high gearing are vulnerable.

Falling economic activity results in lower company earnings and the ability of companies to service debt is diminished. This is a time when prominent companies collapse and many over extended businesses go into liquidation.

To avoid bankruptcy in a severe recession such as we experience every 20 years on average, corporations and small businesses need to liquidate debt while the economy is still booming. This may entail selling property, parts of the business or the whole enterprise.

Most individuals and companies only do these things when they are forced to - when prices have fallen and the chances of survival have diminished. This is human nature - most of us are too busy in our business and personal lives to notice the dangers that are looming in the economy.

Reducing stock levels and avoiding over expansion and increased debt when the economy is booming may be psychologically difficult but necessary if the business is to survive the price and cost pressures in the inevitable downturn.

Boom conditions are associated with good profit margins and high sales levels. It is easy to expect these good conditions to continue and the temptation may be to expand with high cost borrowings based on future earnings projections, however this phase is not sustainable. Even though it may last for a few years and lull us into a false sense of security.

The business world is subject to the winds of change and when the storm comes we need to be prepared. Our survival in tough economic conditions depends on how well prepared we are. If we are cashed up we can take advantage of the falling prices of real assets. Major purchases near the bottom of the 20 year cycle will pay handsome dividends when the economy eventually recovers - as it always does!

Note: The current low inflationary environment is probably a warning that we are sliding into a depression in a long term cycle sense. Governments are being forced to become more efficient and reduce debt which includes asset sales. The socialist era has passed - the trend now is towards more efficiency and less waste of public funds. Welfare payments are diminishing and we are now expected to fund our own retirement as the government cannot afford to.

Countries that have good, efficient government which allows companies to compete without being made uncompetitive by excessive controls and taxes will continue to grow, however those that hang on to their old inefficient ways will punish their economies which will slide further into decline with resulting high unemployment.

It is tough to "bite the bullet" and reform the economy as New Zealand and Britain have done however in the long run we will be forced to follow their lead. Hard times are ahead for the Australian economy as the current persistently high unemployment rate is indicating. It is always better to take our medicine early - before we become a terminal case. Hopefully Australia will reform itself before the next severe recession hits. If not, we will go through great economic hardship - at least those of you who have read this article may be prepared for what may be to come.

As with all forecasting, the above comments are the opinion of the writer and other views on this subject may need to be sought to gain a balanced outlook.