“IS THIS THE RIGHT TIME TO INVEST?”

Zain Jaffer - Apr 14, 2020, 3:43 pm

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“Have we hit the bottom?‟ “Should I get in now?‟ The market fluctuations caused by the “coronavirus crash” have been exhausting and erratic. It’s hard to understand how we see record job losses, a shutdown of the economy, horrific GDP projections, a bad earnings season, yet the market has regained half its losses and just entered into a bull market – or a “bull trap”! This is peculiar behavior when the markets are rallying on bad news and being buffeted about by politics, oil wars, and health-related news.

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Looking beyond a bad earnings season

There is a ~~great article~~ by *Ask Arora,* where Arora Nigam explains that the pre-Easter *stock market rally* could be driven by any (or all) of the following factors:

- short sellers who need to buy stocks to cover their short positions
- algorithms that see this activity and start to buy based on the short sellers' activity
- technical traders who jump in based on the buy signals generated by this resurgence
- others who see this rise and react (buy) based on the phenomena of "fear of missing out" (FOMO)
- small investors who act on that rise ("wow! I can see that we are now significantly above the bottom")

But then when the markets reopened after the Easter weekend, we entered back in negative territory once again, only to bounce once again.

Many people believe we have seen the bottom and are investing based on calculations of lower earnings in Q2 but higher earnings coming back in Q3 and Q4. Goldman Sachs has moved from its bearish outlook and has made the aggressive prediction that the S&P 500 will stand at 3000 by the end of this year.

In general, I agree with this analysis with the two following caveats, which can alter those projections:

- China has seen a resurgence in COVID-19 cases in recent days. They claim that those cases have foreign origins, but this calls into question whether China (and other parts of the world) might see a second wave of COVID-related devastation to human life and economic activity.
- South Korea is reporting some testing results that show reinfection for recently-recovered coronavirus patients. These patients have recovered from the illness but scientists apparently don't see antibodies present in these patients' bodies. If the situation proves to be more widespread, this could indicate the possibility for a second wave and delay economic recovery.

The world is asking how this recovery will happen. Experts are pontificating whether we will see a V-shaped recovery or more like an L- or U-shaped recovery. In my opinion, we will see a W shaped recovery, with more volatility to follow. It is all impossible to predict, as markets are not logical. There is a well-known saying among investors that 'Markets can remain irrational far longer than investors can remain solvent.'

"Is this the right time to invest?"

These types of questions will continue to swirl as the stock market erratically rises and falls in the coming days.

With last week's most recent gains, everyone will continue to want to know if the roller coaster ride is over, if the bear is gone for good and if now is really the right time to jump in.

My answer to this is "Yes," but I have some guidelines for your consideration

The current market shakiness will deter some investors, and we know that uncertainty drives down valuation. But for those who have the cash available, I do believe this is a good time to take advantage of today's poor earnings in favor of betting on stronger earnings in Q4 or Q1 2021.

Here are some considerations:

Bad Earnings Season? Take a long view

If you're a ~~long-term investor~~, it's a good time to invest as long as you focus on results that are *years away*. You need to adjust your expectations and understand that the majority of companies will experience a bad earnings season or two or three or four. Right now, many investors are looking at how a company might be positioned by the third quarter, but it would be wise to take an even longer-term approach.

You cannot invest in the same way that you did several months ago. The market dynamics are so very different. There are numerous market oddities and different influences in the marketplace right now. Pension funds keep attempting to rebalance--probably based on universally understood principles—trying to respond to irrationality with rational moves. Short sellers are getting squeezed, and the market is totally driven by fear and greed. Trading desks are closed, and algorithms are buying and selling "logically," programmed to react based on 'normal' stock market best practices . . . But these are not normal times. They may not be equipped to respond to emotional investors who are up or down 50% from an investment and making rash decisions.

Don’t try timing the market. The prevailing view from experts is that there will be lots of volatility and headline-driven reactions. In this extreme volatility, it’s important to stay focused on a price target and keep your emotions in check. The sophisticated investor stays firm or buys some insurance, like options. It is possible to short sell against your equities, but I don’t recommend this approach for long-term investors. Leave that to the short-term day traders or professional managers like Dan Niles or Jim Chanos.

Go in with a plan

I expect that we will see the S&P valued at 2500 or below again. Don’t try waiting for a bottom but save some cash in case we experience another big drop. Planning for irrationality can make it more manageable and can lower your emotional reactions. Perhaps deploy 20% when the S&P is between 2800-2500, 30% around 2500 and then keep another 50% on the sidelines if we re-test a new bottom.

Look for good stocks trading at a discount. You don’t need to go after the most depressed stocks, as there are plenty of good stocks trading at a large discount. Focus on stocks that have large balance sheets and good cash flow positions. There is a tendency for new investors to go after stocks based on dramatic charts, saying, "Wow, it’s down 50%," but you can find good returns that are a safer bet by focusing on winners.

If you must satisfy your craving for investing in certain names that are heavily bleeding, you should agree in advance on a what percentage of your portfolio should be “risky”, like 20%. Then you can consciously go after these “beaten down” stocks but put the rest in assets such as staple names or leaders.

Divide your investable cash into segments

Don’t buy the broad markets; instead, purchase individual stocks or sectors that are priced attractively. Even when the S&P market is up, some stocks are still down and vice versa. Develop a hit list of stocks and categorize them by sectors or risk/reward profile. Set price targets for those and commit to investing money into each stock when they reach a range close to your target.

Another way is to divide money into three to five tranches and just buy stocks agnostic of price today and then again at some other point in time or after an event. If you think we are in a lasting painful cycle, then stretch it out. History suggests that timing the market is impossible, but it also doesn’t make sense to invest at the very top of a range that is so far off the lows.

Choose your safe havens

Gold is traditionally a safe haven during bear markets; you can hedge with commodities; and bitcoin can help with currency erosion. However, these do not produce income like a dividend-earning stock does, and more changes in those markets may be coming soon. Consider bonds. They are low yield and very expensive right now, but it is important to have some portion of your portfolio safely tucked away.

Whatever equities or other investments you decide to move forward with, make sure your decisions and actions are strategically grounded and unemotional. Make a long-term plan and execute that plan without passion . . . but hold on to your hat, because the roller coaster ride isn’t over yet.

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Zain Jaffer is the Founder and CEO of Zain Ventures (https://zain-ventures.com), a global investment firm with over $100 million in assets under management. Zain Ventures invests in start-ups, real estate, stocks, fixed income, hedge funds, and private equity.

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