Will the Bull Run return in USA & Global equity markets?

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After Dow Jones Industrial Average (DJIA) touching a low of 7397.31 in March, 2003 – the bull run begun in the USA and started moving upward for subsequent years. With a dream run of four and half years, the DJIA made an all-time high of 14198.10 on 11th October, 2007, showing an increase of 91.94%. At that time, positive news of increasing consumption, high investment, benefits of globalization and robust financial developments including M&A activities especially by Asian companies had pushed up the world equity markets at new highs.

But, as every Bull Run has sustained bear run or subsequent sell-off, the USA market has also witnessed selling pressure on the back of various reasons. Sub-prime mortgage crisis, housing market bubble, increase in unemployment rate to 5.5%, slow GDP rate and high inflation rates have severely impacted investment sentiment across the USA. This has resulted in the fall of 18.1% in the DJIA from Nov'07 to Mar'08. All these resulted into bearish sentiments across the globe and brought down the world equity markets at considerable rate. All these are reflected in falling equity markets and rising credit crisis. The USA runs the risk of major/most severe economic slowdown of its past 30-40 years which should be seen as a sign of warning by investors.

INTERNEATIONAL EQUITY MARKETS (2007-2008)			
Index	**High**	**Low**	**Change (%)**
DJIA	14198	11635	-18.1
Nasdaq	2239	1832	-18.2
FTSE	6754	5339	-21
Paris CAC 40	6168	4417	-28.4
Swiss Market	9548	6770	-29.1
DAX Germany	8152	6168	-24.3
Nikkei	18300	11691	-36.1
Shanghai	6124	2730	-55.4
Strait Times	3906	2746	-29.7
Hang Seng	31958	20573	-35.6

Source: Dhaval P Vyas Investment Research

Notably, some of the over-valued markets have cool down and have taken a hit in last 6-9 months. For example, the Shanghai Index had zoomed from 998 in Jun'05 to 5955 levels in Oct'07 in almost two and half years showing a massive increase of 496.7% over mid-2005 levels. As the bubble of over-valued stock valuations got burst from Nov'07, the Shanghai market has lost 52.8% to make a low of 2812 in June'08. However, the rest of the world markets haven't tumbled liked the Chinese equity market, but of course they have felt the heat in the same period. This can be seen in the above mentioned table.

Is economic downturn of USA visible?

As far as the economic downturn is in the USA is concerned, several indicators have suggested a weakening economy. But, no signs of financial unrest in a big way have been seen yet in the USA. Recently, the US unemployment rate jumped to 5.5% from 5% which is expected to go as high as 6.5%. In fact, Finance and Housing sectors of the USA are in real mess as sub-prime mortgages & wholesale finance has suffered a significant setback. In USA, the Finance sector employs almost 6% of workers – however, one must note that only a small portion of these are employed in the much affected section – sub-prime & wholesale finance. So, effect would be limited on the same section. On the other hand, the Housing sector of USA accounts for three and half per cent of GDP from a high of six and half per cent before two years. All these have resulted in the severe housing market & credit market crisis in the USA.

What does the recent Financial Crisis mean to the USA economy?

The continuing financial crisis in the USA has impacted considerably which can be seen in the mounting pressure on capital of banks, higher credit risks, liquidity shortages, falling prices of structured products especially mortgage-related securities, decline in stock/equity prices. Moreover, the financial crisis may put a break on consumer spending in the USA, which can lead to low corporate profits and thus, lower employment. Moreover, on the Fed's try to lower inflation by slashing interest rates may not reap the fruits as expected the back of the rising costs of energy prices including crude oil and natural gas,.

Possible options for the Federal Reserve

Presently, the Federal Reserve has two options on hand 1) Lower/unchanged interest rate, 2) Increase in interest rates. First option of keeping interest rates unchanged or lower may not help to bring down the consumption and thus, inflation may not come under comfortable zone. On the other hand, if the Fed decides to increase interest rates, the already slowing USA economy may face severe consequences in the form of lower corporate profits, low credit growth, low employment opportunities. Therefore, it is a very crucial juncture for the USA and for the world's major economies as much of the economy change in USA can affect the financial markets worldwide.

Technical Perspective

Technically speaking, for short-term, the DJIA has very good support at 11700 and 11400 levels, while resistance for the market is at 12650 & 13000. Unless the DJIA doesn't close above 13000, the sustained Bull Run may not be witnessed from short to medium-term perspective. Notably, if the DJIA closes below 11100, the major bear market may be established which may bring down the DJIA to 10600. The worst scenario probability of the DJIA touching 8550 can't be denied by mid-2009 can't be denied. Overall, the DJIA is expected to consolidate during January'09 & Aug'08 before starting to see robust recovery.

What will happen to USA in 2008 and 2009?

As per our international economic research, the USA will continue to see slowdown in economy through-out 2008 and has the slight probability of recovering in the last part of 2008. Rather in the 1Q'09, the USA economy may start recovering from the financial setback felt during 2007-08. Therefore, the considerable upward change in interest rates will be seen in the 2008 year end and early part of 2009 as some of the indicators like decline in the unemployment rate and improved GDP growth rate are visible. So, don't expect a quick turn-around in the financial market of USA & worldwide in near future and also note that value buying in selected stocks across the globe will continue to exist as equity markets always outperform all available investment vehicles over long-period.