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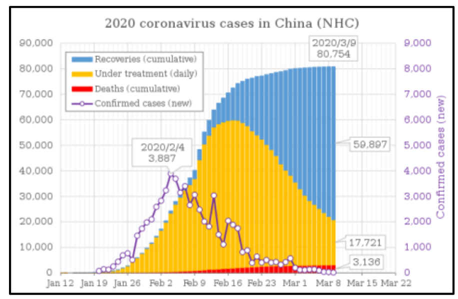
Perspective: The WHO Says... StormGuard's Indication

Mar 6, 2020

Coronavirus Fears Continue Rising

As detailed in the February Newsletter, the Coronavirus deaths are about 12% of the 2010 H1N1 deaths. Every year the ordinary flu kills roughly twice as many as the H1N1 virus. Yet the market was completely unfazed by the H1N1 deaths. The chart (right) of the 2020 Coronavirus cases in China per WHO (World Health Organization) shows that we should already understand that new cases in China have radically dropped in the past three weeks. Other countries indeed lag China in the overall cycle, but the news from China should excite us: It's going to cycle through and end quickly just like SARS and H1N1. Still, fears continue to rise.

China is Showing the Way
(click to enlarge)



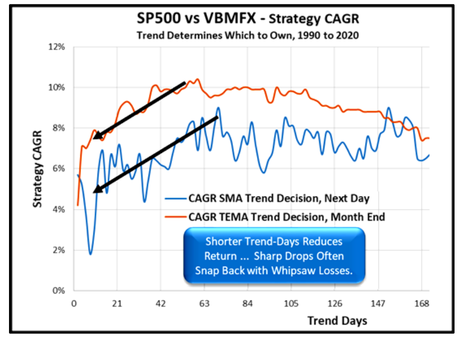
I offer two theories for why the market is treating the Coronavirus different from H1N1: First, H1N1 came after the 2009 market bottom when there were not many sellers left. Conversely, the Coronavirus came after a series of market highs with numerous financial pundits saying the market needed a serious correction. Was this all about a self-fulfilling prophesy just waiting for a trigger? Second, it is likely that AI neural networks are now reading the news but may not be able to distinguish between true news and sensationalism that produces more interesting headlines and sales. AI algorithms may be concluding that the sky is about to fall, and by trying to be the first ones out the door, they actually push the market lower.

(click to enlarge)

StormGuard's Response So Far

In the chart (right), it's easy to see that after Monday's large drop, StormGuard-Armor is poised to indicate bear market status quite soon. Two of the more common email questions I've recently received include: "Why didn't it trigger after the third major day of losses?" and "Will it trigger for sure by month-end?" The short answers to those questions are (1) sharp drops most often snap back and could lock in whipsaw losses if you exit too quickly, a (2) a sharp and sufficiently strong recovery could prevent StormGuard from triggering at month-end.

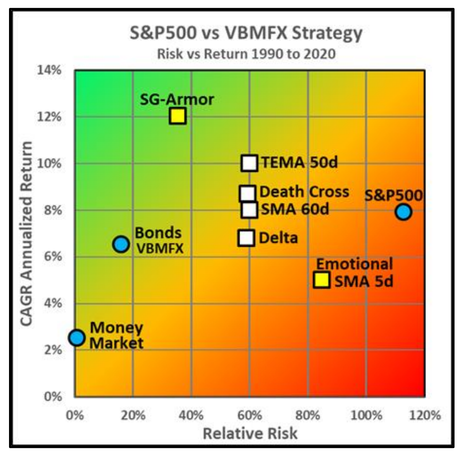
Reducing Whipsaw Losses
(click to enlarge)



Sharp Drops Often Snap Back

The chart (right) illustrates the performance of two strategies, each deciding between owning the S&P500 and an ordinary bond fund (VBMFX). The blue line uses an SMA (simple moving average) of duration "Trend Days" and the orange line similarly uses a TEMA (triple exponential moving average). In each case, the black arrows illustrate that shorter time constants perform substantially worse. The horizontal scale is in market days, and one month is typically about 21 market days. Judging performance in just five market days is the equivalent of jumping out of the frying pan into the fire.

SG-Armor vs Emotional Selling
(click to enlarge)



It's Better to be Right than Early

The risk-return chart (right) illustrates the effect of different strategies for switching between equities (S&P500) and bonds (VBMFX). The three blue dots are reference markers. The four white squares illustrate the performance of different methods of switching between the S&P500 and VBMFX. The lower yellow square marks the SMA 5-days method, which is what we do when we look at the past week and emotionally want to buy or sell right now. The upper yellow square is what we get when StormGuard-Armor takes its time to be sure. It also checks things in its 14 different ways. Being right is better than being early.

Final Comment

Many technical traders hoped that last Friday would prove to be the bottoming re-test that held before the market would head higher. Unfortunately, Russia started an oil price war over the weekend that it plans on using to hurt the US fracking industry. Buyers decided to step back a bit to see if their nervous colleagues were done selling, resulting in a market dive on Monday. Hopefully, it represents a washout of the emotional sellers and will mark the start of a strong rebound as investors put the coronavirus into proper perspective and re-discover the strength of the economy.

Surf Well and Prosper,

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