The Forgotten Bear Markets

After closing at an all-time high on September 20, the S&P 500 entered a bear market on Christmas Eve. The technical definition is a 20% peak-to-trough drawdown, but I'm willing to give this 19.8% fall the benefit of the doubt.

There was a decent rally the rest of the week, but regardless if this was THE bottom or a bottom, I'm willing to concede this swift fall was a bear market because of the damage caused.

Whenever stocks fall like this it's easy for investors to go to a dark place. Those dark places for many include the Great Recession, the bursting of the dot-com bubble, the 1987 crash, the 1973-74 bear market or the Great Depression.

How could you not go to the worst case scenario when stocks are in freefall?

You can certainly never rule out an earth-shattering crash for the simple reason that the stock market is driven almost purely by emotions during a downturn. Crowd psychology can bring about these types of situations, even when the fundamentals wouldn't seem to warrant such an event.

But it's also possible that a bear market can occur without evolving into a complete and utter meltdown.

There's been plenty of ink spilled about history's great market crashes but investors pay little attention to the *other* historical bears that didn't reach ludicrous mode.

Here is a list and short synopsis of some of the forgotten bear markets of the past 80 years or so:

November 1938 to April 1939 (-26.2%): The 1930s is otherworldly when it comes to market volatility. No other time period even comes close. The nasty recession of 1937 ended in June of 1938 and stocks rallied hard into the end of the year. After falling almost 25% in March 1938, stocks rose 15% in April and 25% in June. Then they gave it back from the end of the year until early spring even though there was no recession. Basically, investors lost their nerve because they were still traumatized by the Great Depression.

October 1939 to June 1940 (-31.9%): Hitler invaded Poland on September 1, 1939, and U.S. stocks were up more than 10% the next day the markets were open. Then from October through June of the next year stocks would fall almost 32% even though there was no recession as a result. The prospect of another world war weighed heavy on the psyche of investors (surprisingly, the Dow was up 50% from the time WWII started until it ended in 1945).

November 1940 to April 1942 (-34.5%): Again there was no recession to cause this downturn but there was the Pearl Harbor attack and the U.S. entering World War II. Following the Great

Depression and its aftermath, most people had more or less given up on the stock market.

May 1946 to October 1946 (-26.6%): This post-WWII bear market was caused by investors wrongly assuming the end of war spending would cause an economic slowdown. Instead, there was a period of massive inflation coming along with pent-up demand as those who returned from the war looked to plant their roots. There would be no recession this time around.

June 1948 to June 1949 (-20.6%): This was the first post-war recession brought about by tighter monetary policy to account for higher inflation but it was relatively shallow in magnitude and duration.

July 1957 to October 1957 (-20.7%): The Fed tightened monetary policy in the two years leading up to 1957, causing a recession that saw GDP drop even further than it did during the more memorable 1973-75 contraction. Stocks had also risen enormously throughout the 1950s so the fact that stocks fell shouldn't have been a shock following such strong gains.

December 1961 to June 1962 (-28.0%): The original flash crash occurred in May 1962, when stocks fell 6% on a single day for basically no reason. But stocks had already been falling into this period even though the recession ended by February of 1961. The best thesis people could come up with at the time was markets came down because they went too high. That's as good of a reason as I could think of most of the time too.

February 1966 to March 1968 (-22.2%): There was no recession in concert with this tumble in prices but interest rates had risen precipitously since the start of the decade. The 10-year treasury yield rose almost 2% from 1965 through the end of 1968.

November 1968 to May 1970 (-36.1%): 1968 may be one of the most tumultuous years of the post-WWII era -- the Vietnam War, the assassinations of Martin Luther King Jr. and Robert Kennedy, anti-war protests, racial tensions and a general sense of anger around the country. There was also a minor recession in late-1969/early-1970 along with the end of the go-go years. By all accounts, this is one of the most underappreciated bear markets.

September 1976 to March 1978 (-19.4%): There was no recession in this period but stagflation was getting out of control as interest rates and inflation continued to skyrocket.

November 1980 to August 1982 (-27.1%): This period experienced two separate recessions, most likely caused by Paul Volcker and the rest of the Federal Reserve, who took short-term interest rates to 20% to combat inflation. Can you imagine a Fed chair getting away with causing two recession these days? I'm not sure how well that would be received politically. The end of this period was the start of one of the greatest bull markets in history.

July 1990 to October 1990 (-19.9%): This minor bear coincided with an 8-month recession and the start of the Gulf War. Interest rates had also been rising in the late-1980s. Stocks ended the year down 3% or so after rising every year from 1982-1989. They would go on to post gains every year from 1991-1999 in one of the most unbelievable stretches U.S. stocks have ever seen.

July 1998 to August 1998 (-19.3%): The end of the 1990s tech boom had a minor hiccup caused by currency issues in emerging markets. It's remarkable that even with a 19% drawdown stocks still finished 1998 with a 28% gain.

April 2011 to October 2011 (-19.4%): This one may have been caused by the release of the Michael Lewis book on the European Sovereign debt crisis. I'm only half kidding, but European debt issues were the main culprit here. The U.S. also saw its credit rating downgraded for the first time ever in this period.

People forget how scary this one was at the time. There was a ton of double-digit recession talk. I still remember the six-day stretch in August 2011 that saw 5 daily moves in excess of 4% on the S&P 500 (-4.8%, -6.7%, +4.7%, -4.4% and +4.6%).

The average decline over these 14 forgotten bear markets was -25%, lasting just shy of one year in terms of average length from top to bottom. By my count, 8 out of 14 didn't coincide with a recession.

There's no telling if the current swoon will go down as a bear market or one of THE bear markets. Time will tell.

Stocks could always crash more from here.

But just because stocks have fallen hard doesn't mean you should expect to see the Great Depression every time they go down.

It's important for investors to remember that these periods in the market are natural. Sometimes they just happen and no one really knows why, even after the fact.

Further Reading:
The Market is Rolling Simply Because It's Rolling