Geneva, October 31, 2022

"All the News That's Fit to Print"

The New York Times

Late Edition
New York: Today, increasing clouds. High 62-67. Tonight, cloudy, breezy, showers likely. Low 51-57. Tomorrow, showers ending. High 58-63. Yesterday: High 68, low 48. Details on page B6.

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STOCKS PLUNGE 508 POINTS, A DROP OF 22.6%; 604 MILLION VOLUME NEARLY DOUBLES RECORD

U.S. Ships Shell Iran Installation In Gulf Reprisal

Offshore Target Termed a Base for Gunboats

By STEVEN V. ROBERTS

Special to The New York Times

WASHINGTON, Oct. 19 — United States naval forces struck back at Iran today for attacks on American-registered vessels and other Persian Gulf shipping by shelling two connected offshore platforms that American officials said were a base for Iranian gunboats.

A few hours later, a naval commando detachment boarded a third platform five miles away and destroyed radar and communications equipment, Pentagon officials said.

No American casualties were reported in the actions, which occurred 120 miles east of Bahrain at about 2 P.M. (7 A.M., Eastern daylight time).

A 20-Minute Warning

American officials said the attacking force took pains to avoid killing Iranians, giving the crew on the first two platforms a 20-minute warning before four destroyers, stationed about three miles away, began the shelling.

At the United Nations, an Iranian delegate said "several innocent people" had been killed in the attack, but the assertion could not be confirmed.

With the bombardment, the Administration intended to send a message to

A Huge Blow to the Five-Year Bull Market

Does 1987 Equal 1929?

By ERIC GELMAN

News Analysis

As stock prices soared this year, a chorus of pessimists warned that 1987 was looking more like 1929, when a stock market crash helped to usher in the Great Depression. Yesterday, after a plunge reminiscent of the worst days of 1929, one pressing question was whether the aftershocks would be as devastating to individuals and the nation.

The quick answer, many economists say, is no. The huge losses on Wall Street constitute a substantial blow to the economy at large. But there are many safeguards in place today —

Moore, director of the Center for International Business Cycle Research at Columbia University.

To be sure, there are some unsettling similarities between the current era and the pre-Depression years. Like the Roaring Twenties, the 1980's have seen an astonishing boom Wall Street. Now as then, individual and corporate debt are high, and some sectors of the economy are extremely weak. Trade relations are strained, with protectionist sentiment growing.

But today's economy is better equipped to handle financial shocks. "I don't see this decline in the stock mar-

WORLDWIDE IMPACT

Frenzied Trading Raises Fears of Recession — Tape 2 Hours Late

By LAWRENCE J. De MARIA

Stock market prices plunged in a tumultuous wave of selling yesterday, giving Wall Street its worst day in history and raising fears of a recession.

The Dow Jones industrial average, considered a benchmark of the market's health, plummeted a record 508 points, to 1,738.74, based on preliminary calculations. That 22.6 percent decline was the worst since World War I and far greater than the 12.82 percent drop on Oct. 28, 1929, that along with the next day's 11.7 percent decline preceded the Great Depression.

Since hitting a record 2,722.42 on Aug. 25, the Dow has fallen almost 1,000 points, or 36 percent, putting the blue-chip indicator 157.5 points below the level at which it started the year. With Friday's plunge of 108.35 points, the Dow has fallen more than 26 percent in the last two sessions.

Unprecedented Trading

Yesterday's frenzied trading on the nation's stock exchanges lifted volume to unheard of levels. On the New York Stock Exchange, an estimated 604.3 million shares changed hands, almost double the previous record of 338.5 million shares set just last Friday.

With the tremendous volume, reports of brokers' trades on the New York

Dear Sir, Dear Madam,

It was 35 years ago to the very day that Black Monday occurred. The US market dropped, in just that one day, by more than 22%.

Back then, as the New York Times indeed asked, many stock market watchers wondered if this huge drop heralded the advent of a new Great Depression ("Does 1987 Equal 1929?"). But the days, and then the weeks, and then the months passed and, strangely enough, nothing happened. The market stabilized and then resumed the secular bull market that had started in 1982 and would eventually end only much later, in March 2000. How about the crisis we have been experiencing since the beginning of this year? Like 1987, 2022 will be in the history books, but can we hope on the rapid return of a bull market?

To say that the first nine months of the current year have been a drag from a stock (and bond) market perspective is quite an understatement. Everything that could go wrong did go wrong and, this time around, there truly was no place to hide. Stocks are down. Bonds are down. Real Estate (listed real estate even more so) is down. Gold is down (don't even ask about silver). Yes, oil is on the rise, but if we had told you that a war between Russia and Ukraine would break out and that

Europe would no longer have access to Russian oil and natural gas, you would probably have imagined that oil would rise very sharply. The West Texas Intermediate is, however, only up 11% since the start of the year.

Just like after Black Monday 1987, most prognostications about the future of oil, inflation and many other economic variables might turn out to be flat wrong. The US CPI (Consumer Price Index) is a good example. If you had known, in advance, the exact figures that eventually came out higher than expected, the week of October 17, it is very likely that you would have bet on a massive stock market down. You would have been right, for about thirty minutes, but the markets very quickly started to rebound, to close with an increase of about 2% compared to the previous day.

There was no other news that could explain the rebound. It just so happens that, at some point, markets have digested most of the bad news and start to rebound well before good news show up. This was the case in March 2003, when markets stopped the precipitous decline that had started two years earlier and started going back up on the exact day the US invaded Iraq. It was also the case in March 2009, when many US homeowners were still walking away from their subprime loans and the banking sector was mostly frozen shut. It was the case as well in March 2020, when it was completely unclear how deadly the pandemic would be and if and when vaccines would be available.

These bottoming events are only evident quite a while after they occurred. When they just happened, they are mostly dismissed as "just one more rebound in a bear market". It is only as time passes that we can safely say "that was the real bottom". So, clearly, it is too soon to say that last week's reversal was the real deal, the real bottom, or just another of the many rebounds we have already witnessed in 2022. This will depend on the earnings season now just beginning and also future inflation numbers (because that is what everybody is looking at during the current bear market) and many other variables. What is certain, however, is that pessimism is rife and that almost no one believes that this is the bottom. After all, most central banks are still hiking interest rates, the UK government is still a show and the war in Ukraine is still raging on with no clear end in sight. There is no particular reason to see the light at the end of the tunnel. But again, that is exactly when markets find a bottom, long before there was a good reason for them to do so.

What lessons can be drawn from this situation for coherent portfolio management? It is obvious that there is no correlation between past predictions, at least those that may have turned out to be correct, and the probability that future predictions will come true. On the other hand, it is always welcome to return to the fundamental principles in order to try to remain objective and to get rid of the sensational.

When we discuss investments with you, we always emphasize the long-term and that sounds great as long as markets hold. A year like 2022, however, complicates the situation and often calls management principles and strategies into question. As markets fall, investment horizons shrink from years to the next tick. It's only human. But keep in mind that nine months, as bad as they may have been, is not even considered short-term. It's less than short-term. Absolutely anything can happen in nine months in the stock market. Actually, absolutely anything can happen in one day, as Black Monday 1987 has shown us.

We are used to linear thinking and, in most of our daily lives, this is appropriate. Save some money and, little by little, your current account grows. Lay a wall brick by brick and, after a while, your house is built. In the stock market, however, you sometimes get the feeling that you lay the bricks and that, all of a sudden, a third of the bricks are gone. Markets act in a non-linear way and are therefore, by nature, less reassuring and more difficult to understand by this way of thinking.

So, the next best thing to do, once one is aware of this limitation, is to only invest in very good companies that will do well in almost all environments, be they inflationary, deflationary, high growth or low growth. We have always been fairly certain that around 85 to 90% of these investments will make money on the long-term. Indeed, 10-15% of these investments won't work out and, just like with bonds, we have no way of knowing which ones in advance, but as the outlook darkens for some, it will be possible to reduce exposure to reinvest in more profitable investments.

We believe, however, that one should not rush to sell, even with sometimes substantial losses. It is necessary, beforehand, to check carefully on the potential for possible recovery. Indeed, many successful investments (think Amazon, for example) have fallen 50%, sometimes repeatedly, before reaching all-time highs. We also believe it is better to refrain from averaging down, as this is when things can get very dangerous (a bad experience, accentuated by downward averaging, can have severe consequences).

Take the example of Meta (formerly known as Facebook). Very clearly, the loss following the company's name change and its investment thesis going from cash machine to burning billions of dollars in an unproven thesis (the metaverse) is gigantic. But it is quite possible that Meta will be an incredibly profitable investment again in the next few years. At the very least, the level of vitriol heaped at the company seems disproportionate (the company is less valued than a real estate company or an industrial company struggling to generate barely a few percent of margins). Especially as the company continues its massive investments in research and development, particularly in commercial livestreaming which might quickly boost Meta's turnover. This trend started in China and already represents 15% of its online business.

If the thesis proves incorrect, further losses should be inconsequential for the portfolio as a whole as the position keeps getting smaller. The secret, as stated before, is to not average down too early. Remember that Google's founders tried to sell the company to Microsoft for one million dollars and, when it did not happen, thought they had utterly failed.

Long term and resilient companies therefore seem to be adequate fundamental principles allowing, ultimately, to avoid the main market pitfalls. Ferrari, to take just one example, has benefited from a 23% increase in sales this year, with margins up to 35% per vehicle. The luxury manufacturer was not impacted by the pandemic, nor by the shortage in semiconductors. The company also continues its investments in research and development, particularly in electric motor solutions. Other companies, such as Richemont or Sonova, find themselves in an equally comfortable situation, while having very attractive valuations due to latest market turbulences. This brings, in our view, good investment opportunities.

At the same time, we believe it is appropriate to emphasize the importance of adequate currency diversification. Particularly this year. The dollar has been very strong, as have other currencies, such as the Swiss Franc and Scandinavian currencies. Furthermore, many companies in these countries have excellent growth prospects. As far as Swiss companies are concerned, they have shown themselves to be resilient to interest rate variations and have been able to benefit from their competitive advantage in relation to euro zone inflation.

All the best,

Your FFM Gestion team

FFM Gestion SA   Rue de la Cloche 8   1201 Genève   Tél : 022 716 03 20