# Perfect Storm Now Brewing Could Soon Cause 1929-Style Crash

*Michael Markowski* Follow | *Monday, 27 June 2016 13:49 (EST)*

Because the S&P 500 closed down by more than 3% and near its low for the day on Friday, June 24, the probability of a 1929-style crash occurring for the week ending July 1, 2016 has increased considerably. There is no doubt that for the coming week the gatekeepers of the U.S. and global equities markets will face their stiffest test for any week since I began my career in the capital markets in 1977.

The volatility, which occurred for the global markets, especially since the equities markets all closed at multi-month lows on a "Friday" (June 24, 2016), has provided the environment for a perfect storm to form. The steady declines of two major European indices throughout Europe's Monday June 27 trading day has increased the probability of the storm forming by the end of this week. The storm's forming could potentially result in double-digit percentage point market declines for global markets for the week ending July 1, 2016. This occurring could be the catalyst to start a worldwide recession that could take the S&P 500 to new multi-year lows by the end of 2016 and a decline of more than 50% from its most recent level by 2018.

To understand why the markets are now precariously positioned all one has to do is take a look at how the crash of 1929 unfolded. What happened in 1929 is eerily similar to what is now happening. The 12% decline of the market on Black Tuesday, October 29, 1929, was the day that went down in infamy because it signaled the start of the Great Depression. However, that day was the culmination of a chain reaction that began on "Black Thursday October 24, 1929". The market lost 11% of its value upon its opening on heavy volume the Thursday that preceded Black Tuesday. Despite the action that was taken by the gatekeepers to prop it up the damage had been done. The market's volatility became the headline news for all of the newspapers over the weekend. The headlines induced panic selling. On "Black Monday, October 28, 1929", the market declined by 12% and the rest is history. Ironically, the chain reaction that caused the sell off on Black Thursday, October 24, 1929, was a crash of the London Stock Exchange on September 20, 1929.

The stock market indices do not respond well to significant corrections that occur late in the week, especially on a Friday. Headline-enabling market corrections occurring on a Friday, provides the investing public time to digest the headline news and fret about the correction over an entire weekend. Even worse, it gives investors the time to corroborate and commiserate with their friends and family who also have investments in the market. Anxiety is increased because advisors are not easily accessible to their clients throughout the weekend. This natural process leads to a deepening level of conviction by investors to instruct their advisers to "sell" when the market opens on the following Monday.

The increasing conviction by investors to sell is a critical intangible that should not be discounted. It can result in the advisors and wealth managers being swamped by clients who emphatically instruct them to sell. Because of the increased conviction levels the time required for an advisor to persuade each client not to sell increases exponentially. At some point, the advisor becomes overwhelmed and the sell orders are processed without consultations. As more and more sell orders are entered a vicious cycle of selling precipitates a downward spiral of the markets.

There are two conditions that must be fulfilled for an environment to be created that would enable a perfect storm to form. The market must have:

- I.Made a Friday correction sufficient to produce headlines for the weekend; and
- II.Declined significantly, and closed lower on the Monday following the Friday.

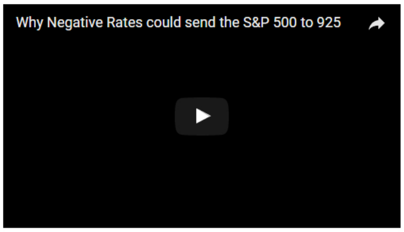
**The first condition was met on Friday, June 24, 2016.** The probability is high that the second condition will be met at the close of the markets at 4:00 PM on Monday, June 27, 2016 for two reasons:

- **European indices are proven leading indicators.** The German Dax (GDAXI) and the French CAC 40 (FCHI) market indices have both declined steadily throughout the Monday June 27 trading day. At 9:00AM EST both indices were down 2% and were at their lows for the day. Tracking these indices is key since there is a high correlation with large percentage declines for both of them being a leading indicator for significant percentage declines for the S&P 500 on same trading day.
- **Mutual Funds liquidation process.** The process that is utilized for the liquidation of mutual funds puts end of day selling pressure on the U.S. markets. Its because all mutual fund sell orders that are received throughout the trading day are accumulated. The orders are aggregated and the orders to sell the underlying shares of the companies held by the funds are entered between 3:00PM and 4:00PM. Because of the headlines over the weekend there is no doubt that many mutual fund holders will issue sell instructions throughout the June 27 trading day. There will be a significant amount of sell orders that will begin to hit the market at 3:00 PM. This virtually guarantees that wherever the market is at 3:00 PM, it will likely be lower by 4:00 PM. Because mutual fund sell orders continue to flow in throughout the day — up until 3:00 PM — it is impossible for even professional traders and market specialist to gauge or predict the amount of sell orders prior to 3:00 PM.

**Because the probability is high that the market indices will decline substantially on Monday June 27, 2016, the first critical day that will determine whether or not the perfect storm will have taken form is Tuesday, June 28.** Should the market behave as predicted and not be able to recover from Monday's damages by mounting a relief rally on Tuesday, the risk is very high that the markets could collapse by 10% or more during the week ending July 1, 2016. There are two things that will make it very difficult for the U.S. markets to mount a sustainable rally this coming Tuesday, or anytime during this week.

- **Paper profits —** On Friday, June 24, 2016 the S&P 500 closed within 5% of its all-time high. Even assuming a 5% sell off on Monday, June 27, 2016 the S&P 500 would still be within 10% of its all-time high. This causes a great problem for advisors and wealth managers because the majority of their clients are sitting on significant paper profits. Having profits that can be cashed in will only increase the conviction of the clients to sell. From my years on Wall Street, during which I dealt with clients, I can tell you that it is impossible to persuade an investor who has profits, not to sell during such a scenario. The only thing that would dissuade most investors from selling would be a sale that resulted in a loss.
- **Memory of 2008 —** Investors vividly remember the crash of 2008. The paper and cash losses they incurred in less than six months were massive. These memories will only increase their conviction to sell and take profits. Additionally, many will want to sell so that they can buy in at lower prices, thanks to investor's recall of the market bottoming in March of 2009 and experiencing a V-shaped reversal.

With the chain reaction of market volatility that was set off by the Brexit catalyst on Friday, June 24, 2016, the S&P 500 has begun its downward journey that I have been predicting would occur during 2016. When the S&P reaches its final destination in 2018 it will have declined by more than 50% to 925 from its close of 2037 on June 24, 2016. My April 15, 2016, report entitled "Ridding the World of Negative Rates May Require Meltdown of Income Producing Assets" provides the rationale and math supporting my target of 925. The video below entitled "Why Negative Rates could send the S&P 500 to 925" features my interview by Jane King that I highly recommend for viewing.

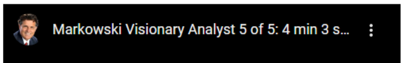



My recommendation is that all long ETFs including the SPY and the DIA and all stocks and bonds — with the exception of sovereign debt securities and micro-cap companies — be liquidated by the closing of the markets on Monday, June 27, 2016. Given that the U.S. indices including the S&P 500 and the Dow 30 closed within five percent of their all-time highs on Friday, June 24, 2016, the risk reward ratios are out of balance. Even assuming a decline of 5% on Monday, June 27, an investor having an opportunity to liquidate within 10% of an all-time high for the market that might not be eclipsed for years is nothing to sneeze at. Additionally, the behaviour of the markets on the close of Thursday June 23, 2016 is very disconcerting. The reading of my two most recent articles is highly recommended since both intimately cover the post Brexit volatility and the issues at hand.

- "NIRP Crash Indicator Signal Now at 'Red, All Out Crash Underway' Reading", June 24, 2016
- "Crash of '08 Haunting Markets: The Devil Shall Get His Due", June 26, 2016

Upon the securities being liquidated I recommend that investors deploy a black swan investing strategy. *The New York Times* best-selling author **Nassim Nicholas Taleb** devised the strategy of investing 90% of one's liquid assets in government or sovereign debt securities, and the remainder in extremely high-risk/high-return investments including venture capital and micro-cap and low-priced stocks.

Taleb's philosophy is both extremely simple and safe. Invest under the assumption that it is inevitable that there will be a "Black Swan" or one-off events that will devastate a market. Should such an event occur, the result would be that the shares of the companies, even those in the S&P 500 — arguably, the world's highest quality stock index — would get clobbered. Thus, it is ludicrous for an investor to believe that they have little risk because they are fully diversified. Diversification does not protect an investor during periods of extreme volatility or against unforeseen mega-events. Taleb made huge profits from the crash of 1987, the bursting of the NASDAQ dot-com bubble in 2000, and from the crash of 2008. In the 4-minute video below I provide details about the black swan and why it's the only fail safe strategy that an investor can utilize to protect their liquid assets.







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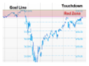
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***For an overview and access to links to the subjects that I cover, including the digital economy, negative rates, perfect shorts, and micro-cap stocks please go to* www.michaelmarkowski.net*.***
***Free access to the NIRP Crash Indicator is available at* www.dynastywealth.com*.*** Finally, because of the critical issues I have uncovered and the significant risk to the markets I will be providing real time updates by email to those who register for NIRP Crash Indicator alerts at Dynasty Wealth.