Why There Will Be a Recession by October 31, 2019

### Description

When it comes to superstition, I am generally not a believer. In my opinion, words such as coincidence and happenstance are better ways to describe things that occur without any good reason.

When it comes to the economy, I am a firm believer in the October Effect. The October Effect is a belief that stocks tend to decline during the month of October.

Historical events that support this include the Panic of 1907, Black Monday (1929) and Black Monday (1987). The crash that occurred in 1987 resulted in the **Dow Jones Industrial Average** (DJIA) dropping 22.6% in a single day.

In many ways, it can be described as a self-fulfilling prophecy, as people who believe the market will crash in October will act accordingly by shorting stocks and closing long positions. That said, let's analyze two major historical events that support this theory.

## Panic of 1907

The underlying sentiment during this time was skepticism, as there were plans to regulate trust companies, which historically adhered to less regulation than banks, fueling panic among investors as the future of trust companies became increasingly uncertain.

The Panic of 1907 started in October and was said to last six weeks. The trigger was the bankruptcy of two brokerage firms, which created a sentiment of uneasiness.

This unease spread to trust companies and was amplified when **JP Morgan** refused a loan to Knickerbocker Trust, which caused investors to become reluctant to invest in the financial services industry.

Eventually the federal government injected $30 million, and with the help of leading financial institutions, fledgling companies were saved which restored public confidence in the markets.

Given the current trade war between China and the United States, this feeling of uncertainty persists, which makes the markets vulnerable to major correction. Similar to the Panic of 1907, all it takes is a small fissure that could trigger a major economic earthquake.

## Black Monday (1987)

On Monday October 19, 1987, the DJIA fell 22.61% and the **S&P 500** fell 20.4%. It took two years for the DJIA to recover from this loss.

Prior to the drop, the market enjoyed a bull market for the better part of five years and increased 43% in 1987 alone.

Further to this, investors became uneasy as the federal government passed anti-takeover legislation that would eliminate tax deductions for loans used to finance takeovers.

Interestingly enough, the tax provision was removed from the bill before it became law but the panic already spread.

There were also computerized trading programs with stop-loss conditions whereby it would sell off stocks when the price reached a certain point. All of this created an inflated market susceptible to a major correction.



This should concern you as an investor, as we have arguably enjoyed a bull market for the past 11 years and the computerized trading systems used today are much more sophisticated than before. What this means is the upcoming recession will have a *tremendous impact* on the economy.

## Bottom line

No one truly knows what direction the economy will take in the future; however, there is an old adage that says those who do not learn from history are doomed to repeat it.

Given that humans continue to experience basic emotions of greed and fear, there is a very good chance that a recession is likely to occur this year. Based on evidence, October has historically been a bad month for stocks and there is nothing to suggest that this year will be different.

If I were you, I would be very cautious with the stock market this year.

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