Market Crash: Are Negative Surprises Coming?

Description

Legendary billionaire investor Howard Marks and author of the popular book *Mastering the Market Cycle* recently warned investors that the current environment may pave the way for "the lowest prospective returns in history" and that investors should expect lower returns moving forward. Marks also noted that the market could be vulnerable to "negative surprises" amid uncertainties related to the coronavirus pandemic.

"In my view, when uncertainty is high, asset prices should be low, creating high prospective returns that are compensatory," said Marks in a rather sombre note.

Another billionaire money manager with muted expectations

Following the recent rally out of those March lows, there's no question that the market doesn't appear to have the best risk/reward trade-off. Given the wide range of potential outcomes with this pandemic, the magnitude of risk taken on by investors is undoubtedly difficult to fathom, even given the U.S. Fed's commitment to preventing an economic depression for which the likes we haven't seen in nearly 100 years.

Higher potential risks should, in theory, come with greater returns. But after the latest market run-up, many pundits don't seem to think that prospective returns from these levels make up for the profound magnitude of risks going forward. Just have a look at the **S&P 500**, which is a few percentage points higher than where it was back at the February 20th peak.

Given we're nowhere close to being out of the woods with this pandemic (**Johnson & Johnson** recently hit the pause button on its COVID-19 vaccine trial), it's not a mystery as to why Marks thinks the market set up isn't looking too good for those looking for big gains over the coming years.

Negative surprises could spark another market crash

So, does the sub-par projected return trajectory call for a catastrophic market crash? Will investors be doomed to suffer a prolonged period of historical underperformance? Or is Howard Marks being too bearish given the profound backing by the U.S. Fed and the abrupt recovery trajectory that we could be in for?

Howard Marks is a genius investor. There's no question about that. But nobody, not Marks nor Warren Buffett, knows with certainty where the markets are headed next.

Could things be brighter than Marks believes? Sure, but without a safe and effective vaccine that's readily available for broad distribution, it's tough to go all-in on stocks based on optimism, the Fed's backing, and further stimulus packages. Nobody knows when that vaccine breakthrough will come, but if it happens sooner rather than later, there's a chance that Marks could be wrong with his expectation for lower returns moving forward.

What I'm more inclined to agree with is Marks's warning that the markets could have a higher chance of being hit with "negative surprises." There's no telling how many further outbreaks or waves of COVID-19 we'll be due for before the coronavirus dies down. And there's also no telling how much worse such waves could get. If things take a turn for the worst this winter, there's no question that the stock market could be in for another round of panic-driven selling that could rival the market crash suffered back in February and March.

Battening down the hatches

That's why it's wise for investors to tread cautiously, as we move deeper into uncharted waters. Warren Buffett is one of the newest bulls on shares of **Barrick Gold**. And if I had to guess, he's probably not looking to "play" near-term commodity price moves with his substantial stake.

I also don't think he's forecasting the same V-shaped recovery that many beginner investors have been positioning themselves for in recent months. Buffett is playing the long game with Barrick Gold, and it'll allow his portfolio to be better able to handle whatever surprises Mr. Market serves up in this highly unpredictable, pandemic-plagued environment.

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Date
2025/08/26
Date Created
2020/10/14
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