

# Trends in the Stock Market

## What's with the bull and the bear?

- The bull and the bear are the unofficial mascots of stock markets around the world and are used to describe market trends.
- Market trends are the upward (bull) and downward (bear) patterns of the stock market over a period of time.
- Trends can be short term, intermediate term or long term, and can apply to the market as a whole or to a single stock or commodity.

## Bull market

- A bull market is a period of generally rising prices. The start of a bull market is marked by widespread pessimism. This is the point when the crowd is the most bearish. The feeling of despondency changes to hope, optimism and eventually euphoria, as the bull runs its course. This often leads the economic cycle, for example in a full recession, or before a recession starts.
- The bullish investor buys up lots of stock and is optimistic about the future.
- A typical bull market lasts 8.5 years, with average annual gains of 14.9% to 34.1%. This adds up to average total returns of 458% per bull market period!\*

## Bear market

- A bear market is a general decline in the stock market over a period of time. It is a transition from high investor optimism to widespread investor fear and pessimism. According to The

Vanguard Group, “While there’s no agreed-upon definition of a bear market, one generally accepted measure is a price decline of 20% or more over at least a two-month period.”

- The bearish investor sells lots of stock and tends to be pessimistic about the future.
- A typical bear market lasts 1.3 years, with average annual declines ranging from -19.7% to -47%. This equals an average decline of -41% per bear market period!\*

*\*Findings from an analysis of stock market data from 1926 to 2014 by Morningstar*

## **Playing the market**

Both bull markets and bear markets represent opportunities to make money; the key to success is to use strategies and ideas that can generate profits under a variety of conditions. This requires consistency, discipline, focus and the ability to take advantage of both pessimism and optimism.

### *Profiting in bull markets*

- **Long Positions:** A long position is buying a stock or any other security in anticipation that its price will rise. The overall objective is to buy the stock at a low price and sell it for more than you paid. The difference represents your profit.
- **Calls:** A call option is the right to buy a stock at a particular price until a specified date. A call option buyer, who pays a premium, anticipates that the stock’s price will rise, while the call option seller anticipates that it will fall.
- **Exchange-Traded Funds (ETFs):** ETFs trade like stocks, and most follow a particular market average, such as the Dow

Jones Industrial Average (DJIA) or the Standard & Poor's 500 Index (S&P 500). ETFs seek to replicate the movement of the indexes they follow, less expenses. For example, if the S&P 500 rises by 10%, an ETF based on the index will rise by approximately the same amount.

### *Profiting in bear markets*

- **Short Positions:** Taking a short position, also called short selling, occurs when you sell shares that you don't own, in anticipation that the stock will fall in the future. If it works as planned and the share price drops, you must buy those shares at the lower price to cover the short position.
- **Put Options:** A put option is the right to sell a stock at a particular strike price until a certain date in the future, called the expiration date. The money you pay for a put option is called a premium. As the stock price falls, you can either exercise the right to sell the stock at the higher strike price, or you can sell the put option, which increases in value as the stock falls, for a profit.
- **Short ETFs:** A short-exchange traded fund (ETF) produces returns that are the inverse of a particular index. For example, an ETF that performs inversely to the Nasdaq 100 will drop about 25% if that index rises by 25%—but if the index falls 25%, the ETF will rise proportionally. This inverse relationship makes short ETFs appropriate for investors who want to profit from a downturn in the markets, or who wish to hedge long positions against such a downturn.

### **Predicting the future is not easy!**

- Markets trade in cycles, which means that most investors will experience both the bull and the bear in their lifetime. The key

to profiting in both market types is to spot when the markets are starting to top out or when they are bottoming.

- If these investment strategies seem complex and hard to understand, don't feel bad—they are complex and hard to understand! Professional traders, stockbrokers and fund managers spend their time analyzing the markets and looking at key indicators. Even experts aren't always able to predict the next bull and bear markets.

**Investing can be risky:** Investments made in stocks or commodities carry the risk of losing money, even when made through a financial advisor or financial institution.

*Sources:* First Trust Portfolios, Investopedia, Morningstar, StockCharts.com, The Vanguard Group