Triweekly Series

Ideas and Nuggets of News *You Can Use!*

LINDNER INSIGHTS

Records are Meant to be Broken

“When investing, pessimism is your friend, euphoria the enemy.”

Warren Buffett

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“Big enough to deliver, small enough to care”

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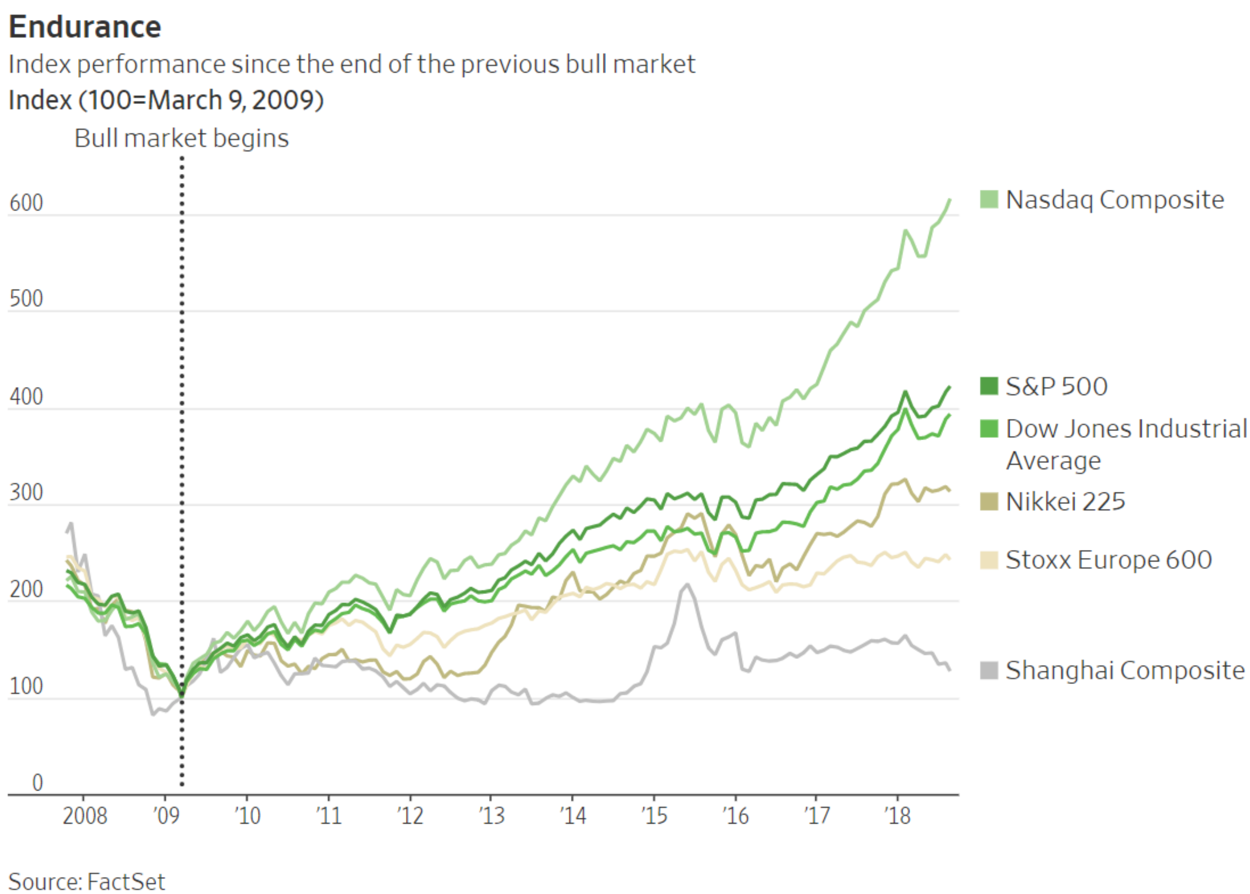
by Chris Briggs, CFP®

Records are Meant to be Broken

The current bull market will become the longest on record for the S&P 500®, according to S&P Dow Jones Indices. Stocks, as measured by the S&P 500 index have been continually rising, without a 20% pullback, since March of 2009. The current advance exceeds the nearly ten-year advance experienced by the index from 1990-2000.[1] I don't know of anyone who would have predicted that the longest bull run in history could follow the financial crisis the world experienced 10 years ago, but here we are.



[2]

[1] https://www.wsj.com/articles/no-stocks-arent-cheap-but-dont-act-rashly-1534863601?mod=searchresults&page=1&pos=1
[2] https://www.wsj.com/articles/u-s-stocks-poised-to-enter-longest-ever-bull-market-1534843800?mod=searchresults&page=1&pos=1

John Templeton famously said, "Bull markets are born on pessimism, grown on skepticism, mature on optimism and die on euphoria." Personally, I believe we are somewhere in the optimism phase. Here in the United States, unemployment is at 50+ year lows. We still have very low interest rates, and many business restricting regulations have been eliminated. Stock and real-estate prices have been consistently rising. Predictions call for the US economy to grow steadily, and consumer confidence is still near cyclical highs.[3] People have reason to be optimistic.

As advisors we need to be asking, are things as good as they can get? Including dividends, stocks have advanced 400+% from their 2009 lows and are now selling at 32.8x their long-term average earnings when adjusted for inflation. That puts them at roughly twice their typical level since 1881, according to economist Robert Shiller at Yale University.[4] Stock prices, and ultimately the market, are driven by earnings and dividend growth. Reported earnings, aided by U.S. Corporate tax cuts in December, have been strong this year. More importantly, company guidance for future quarters is strong.[5] Stock prices can continue to rise while these conditions exist.

A potential test of the current bull market is whether the "popular stocks" can continue to attract new investors and justify their current valuations. As we have mentioned in our past musings, the narrow group of stocks driving the S&P 500 could create a problem for index investors. The companies that make up the technology sector of the S&P 500 account for 22% of the bull market's return. This year, Amazon, Microsoft, Apple and Netflix are responsible for 40% of the index's return of almost 7%. Shares of communications companies led the market in 2000, as did banks in 2008, and both groups fared poorly in the subsequent downdraft.[6] This type of boom and bust cycle investors can experience from the concentration inherent in a capitalization weighted index like the S&P 500 is exactly why we diversify among thousands of stocks of various market caps that are domiciled all over the world. The chart on the next page shows cumulative global index returns from January 2000 - December 2009. Excluding dividends, the S&P 500 rose 417% in the 10 years preceding March of 2000, and since the 2009 lows, the move has been 323% (as of August 17, 2018).[7]

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3 https://ig.ft.com/sites/numbers/economies/us/

4 https://www.wsj.com/articles/no-stocks-arent-cheap-but-dont-act-rashly-1534863601?mod=searchresults&page=1&pos=1

5 https://www.cnbc.com/2018/07/18/earnings-growth-on-pace-to-top-the-first-quarters-record-increase.html

6 https://www.wsj.com/articles/u-s-stocks-poised-to-enter-longest-ever-bull-market-1534843800?mod=searchresults&page=1&pos=1

7 https://www.wsj.com/articles/u-s-stocks-poised-to-enter-longest-ever-bull-market-1534843800?mod=searchresults&page=1&pos=1

	Total Cumulative Return (%)
S&P 500 Index	–9.10
MSCI World ex USA Index (net div.)	17.47
MSCI World ex USA Value Index (net div.)	48.71
MSCI World ex USA Small Cap Index (net div.)	94.33
MSCI Emerging Markets Index (net div.)	154.28
MSCI Emerging Markets Value Index (net div.)	212.72

MSCI data © MSCI 2016, all rights reserved. ***Indices are not available for direct investment. Index performance does not reflect expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.***

[8]

Total Cumulative Return is for the period January 1, 2000 – December 31, 2009.

The Federal Reserve has indicated it intends to gradually increase interest rates, removing much of the accommodative policies of the last ten years. Stocks with high price to earnings ratios or companies who have depended on very inexpensive borrowing can become vulnerable as investors determine the impact of higher rates on future profitability.

Morgan Stanley determined a helpful a list of signals to watch for in the coming 6-12 months. In the past, these events preceded market weakness.

1) Credit spreads widen – lower quality debt begins to underperform high quality debt. This can be an indication of stress among highly leveraged companies.
2) Equities rally sharply – emerging markets and technology stocks rally hardest late into market cycles.
3) Bond yields rise – the macroeconomic backdrop which produced the bull market has spurred growth and inflation. Bond yields rising result in higher cost of funding for businesses.
4) Emerging market currencies dominate – macroeconomic forces produce strong demand for raw materials purchased from emerging nations. The Japanese yen tends to strengthen.

[8] https://my.dimensional.com/csmedia/cms/issue_briefs/2016/03/issuebri_2/Why_Should_You_Diversify_US.pdf

5) Commodities stay strong – strong demand from producers keep commodity prices high on things like industrial metals and crude oil, resulting in higher costs for producers and consumers alike, hurting profit margins and purchasing power.

We have witnessed some of the signals occurring in the last 9-12 months. “The performance of U.S. equities, global discretionary and materials stocks, Japanese government bonds and copper all line up with the market being within a 12-month peak.” Other indicators such as the performance of emerging markets and European stocks are not signaling late cycle characteristics. High yield bonds are also outperforming which is a positive sign that the peak isn’t near. [9]

There is an old Wall Street saying “records are meant to be broken, but were records for a reason.” In no way are we expecting large drawdowns in equity prices, but we are entering one of the longest periods of growth on record for both the economy and stock prices. It is our job as advisors to remind clients that corrections and bear markets are inevitable, but they will be rewarded for taking a long-term view on the markets and their investments.

[9] https://www.morganstanley.com/ideas/bull-bear-signals

About LCA...

Lindner Capital Advisors, Inc. is a federally Registered Investment Advisor based in suburban Atlanta, Georgia, with representation throughout the United States. Our investment platform provides access to institutional fund strategies and exclusive money managers that are not readily available to the retail market. Our portfolios are designed to be consistent with a client's unique investment objectives, individual time horizon, and tolerance for risk. LCA has been CEFEX certified since 2006 and is committed to our fiduciary responsibility.

Ask your Relationship Manager for a copy of "The Educated Investor" written by Robert Lindner.

For more information, call (770) 977-7779 or email portfolios@LindnerCapital.com.

Visit LCA's website at www.LindnerCapital.com

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