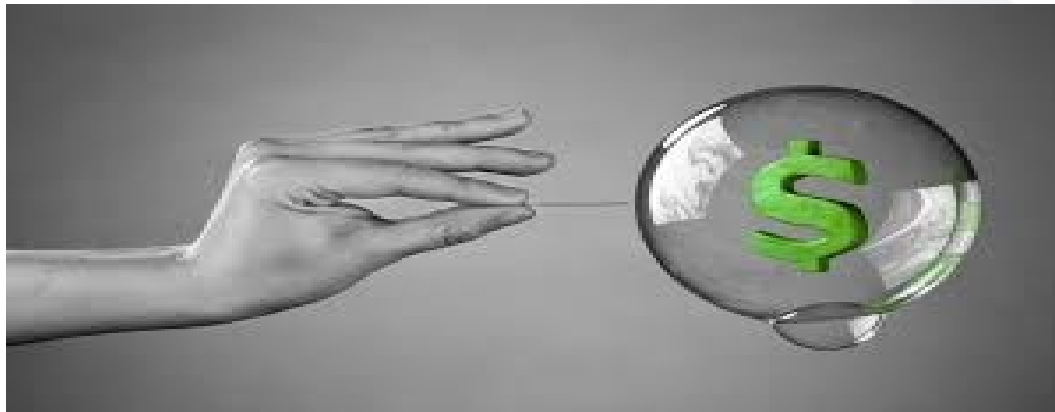


# How to tell if markets are ready to pop (or not)



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Russ Mould, AJ Bell Investment Director  
Shares Cenkos Growth & Innovation Forum  
London, Tuesday 30 January 2018

# Disclaimer

- The value of your investments can go down as well as up and you may get back less than you originally invested.
- We do not offer advice, so it is important you understand the risks. If you are unsure please consult a suitably qualified financial adviser.
- Tax treatment depends on your individual circumstances and rules may change.
- Past performance is not a guide to future performance and some investments need to be held for the long term.

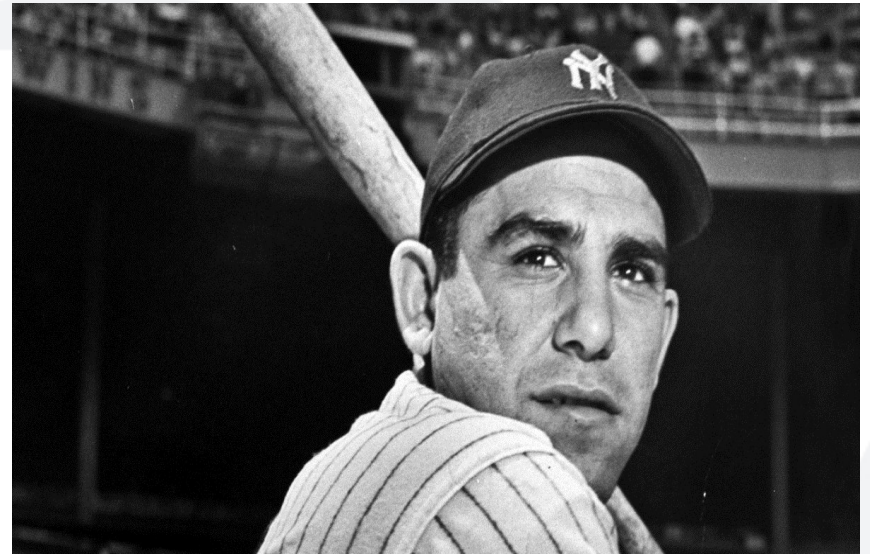
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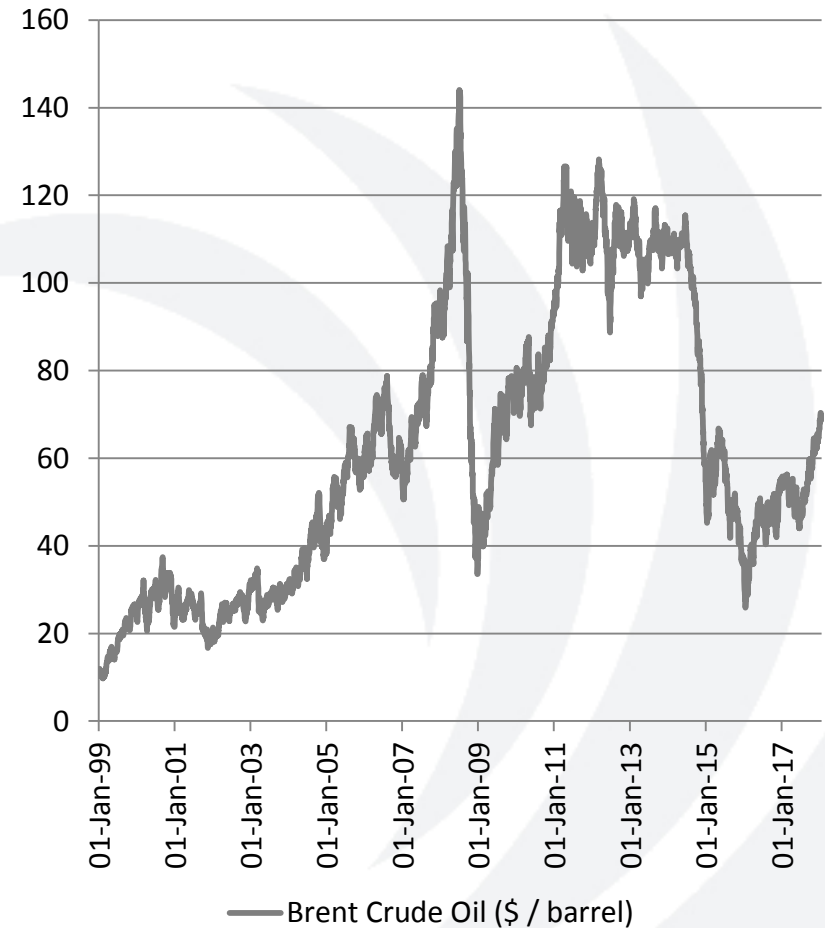
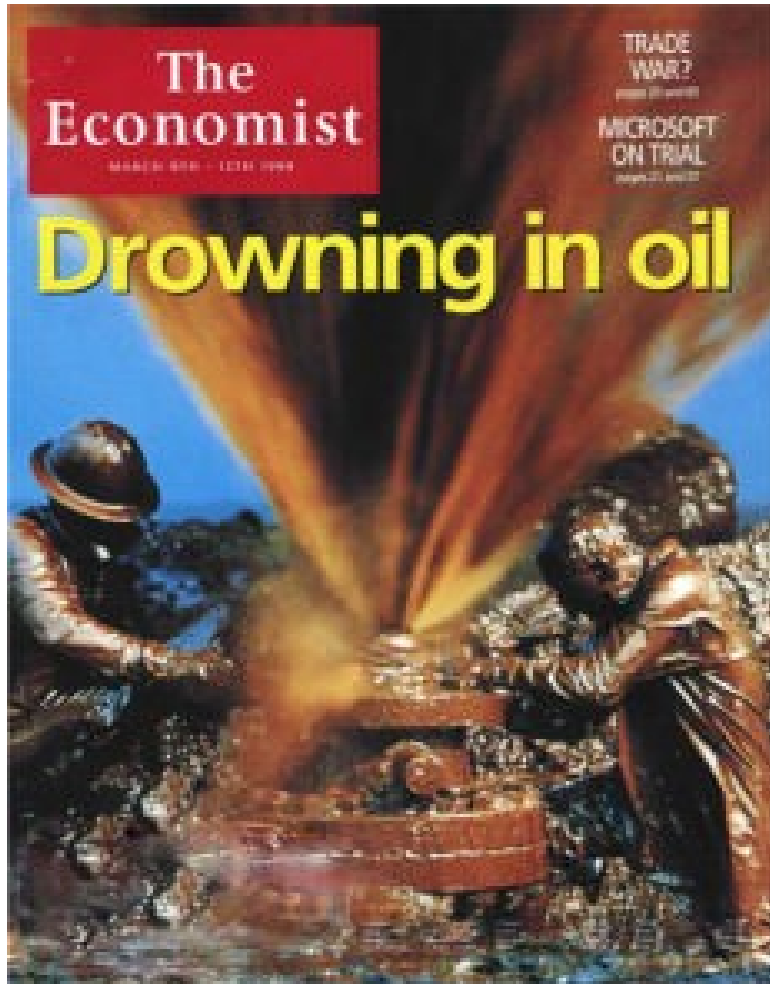


# 1. Think about the future

- “It’s tough making predictions, especially about the future”
  - Yogi Berra

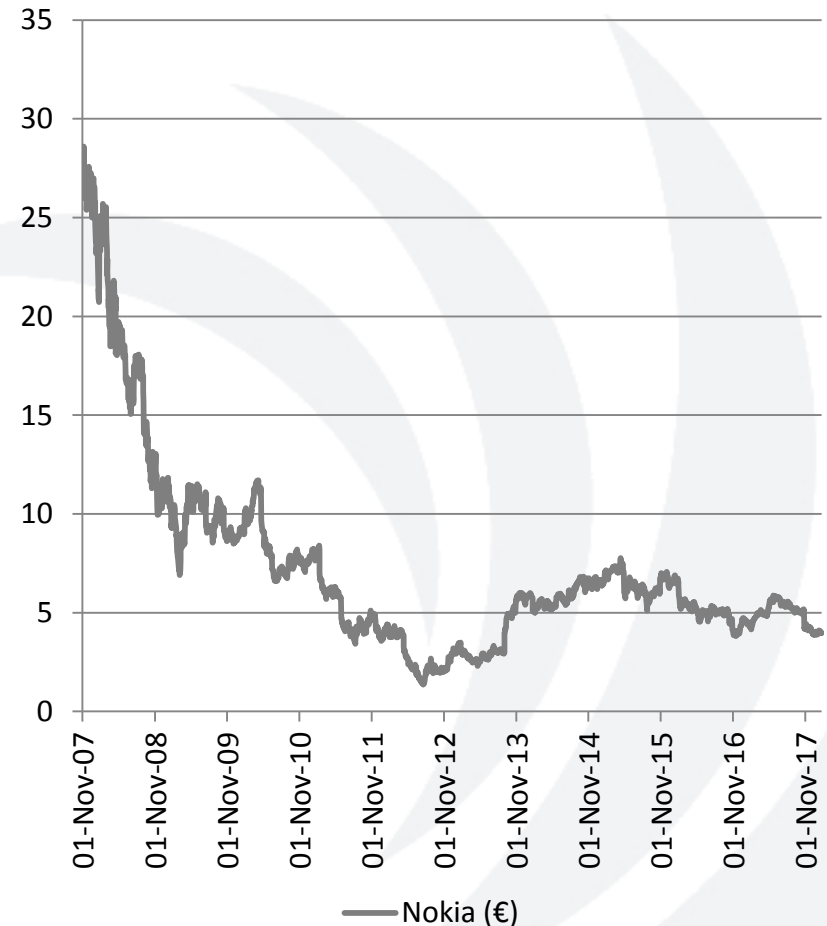


# Think about the future



Source: Thomson Reuters Datastream – with apologies to The Economist

# Think about the future



Source: Thomson Reuters Datastream – with apologies to Forbes

# Think about the future

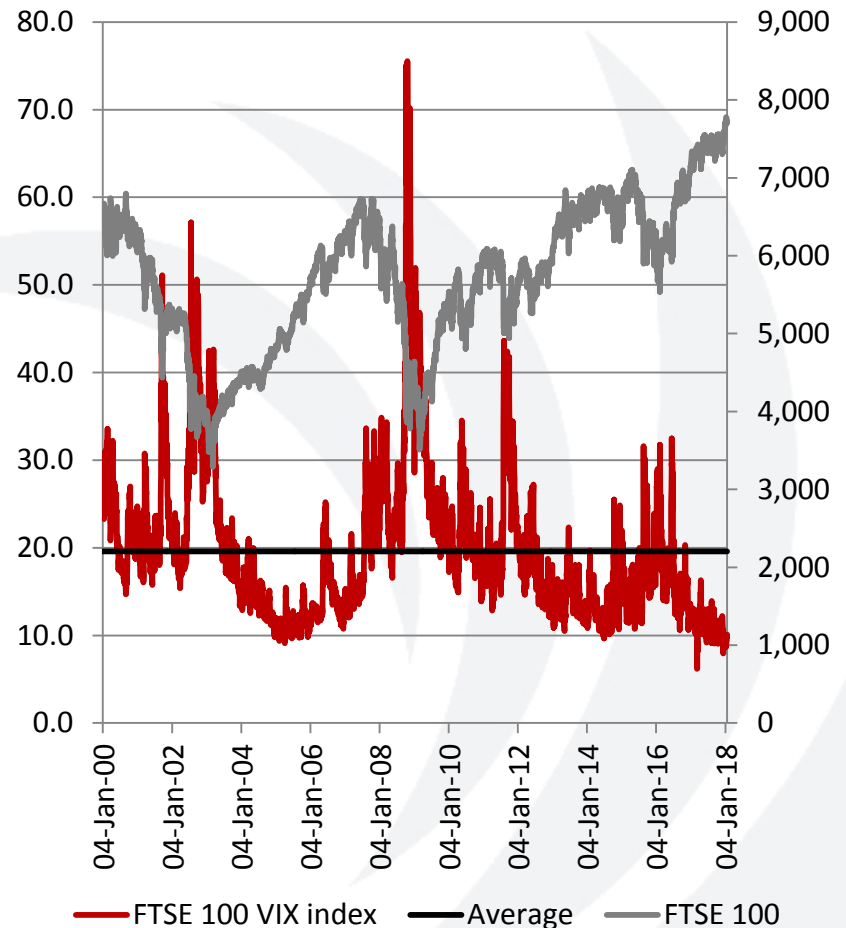
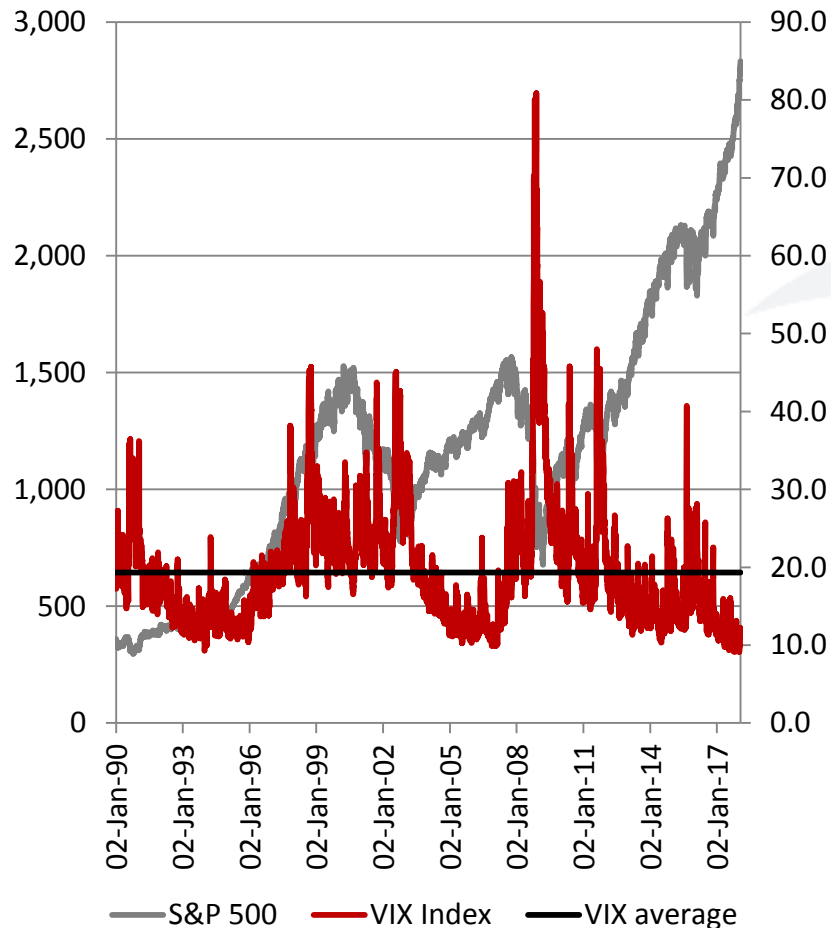
- “Stock prices have reached what looks like a permanently high plateau.” – *Irving Fisher (on 15 October 1929)*
- “The fundamental business of the country is on a sound and prosperous basis.” – *President Herbert Hoover (on 25 October 1929)*
- “It would be going too far to suggest that there will never be another crisis; I do think we’re much safer and I hope that it will not in our lifetimes and I don’t think it will be.” – *Janet Yellen (October 2017)*
- “We have a bit of fun as the bubble blows up and we all think we are going to get out five minutes before midnight but there are no clocks on the wall.” – *Warren Buffett*

# Ten tests of the markets' temperature



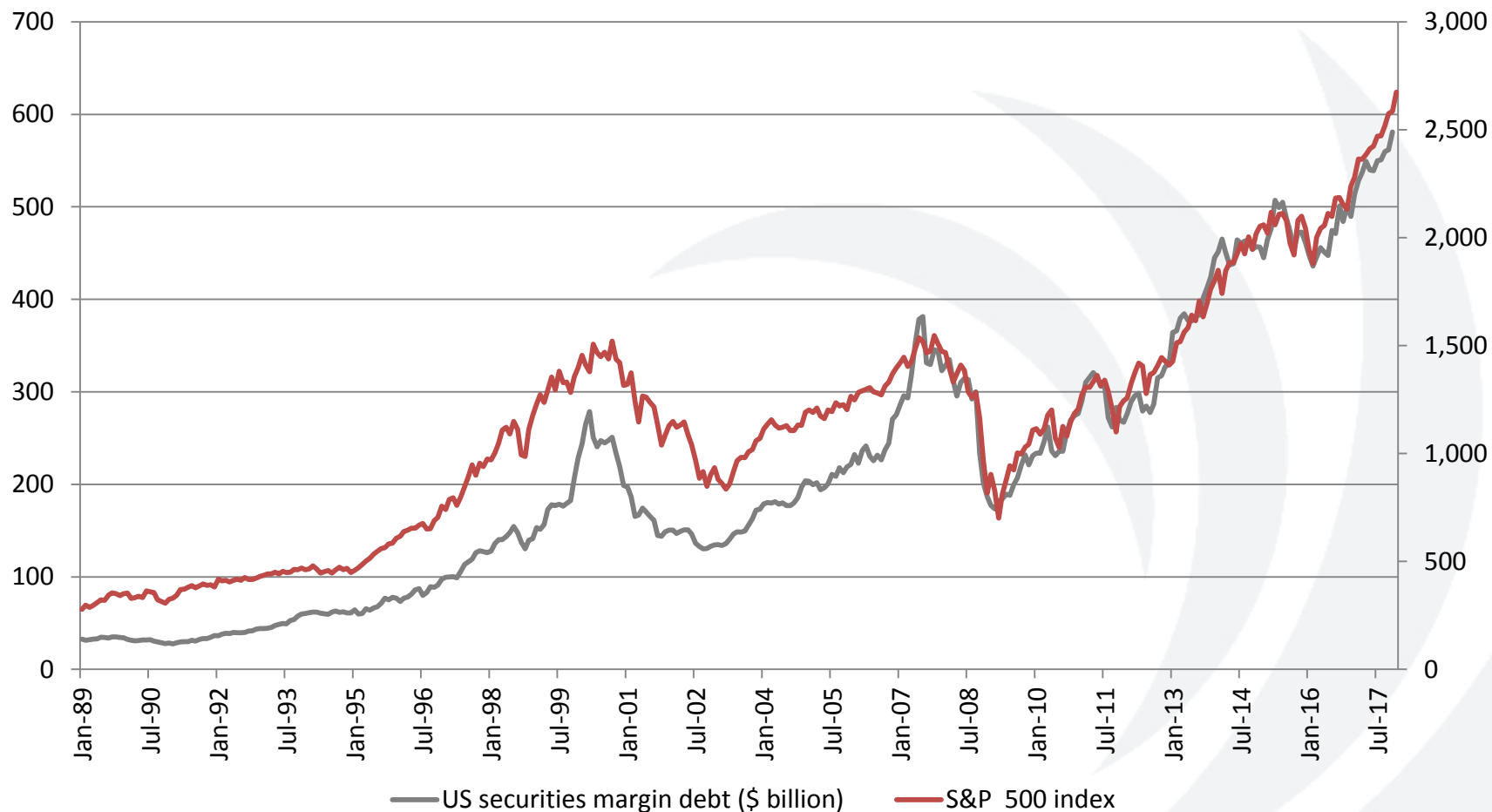


## i. Confidence – no fear here ....



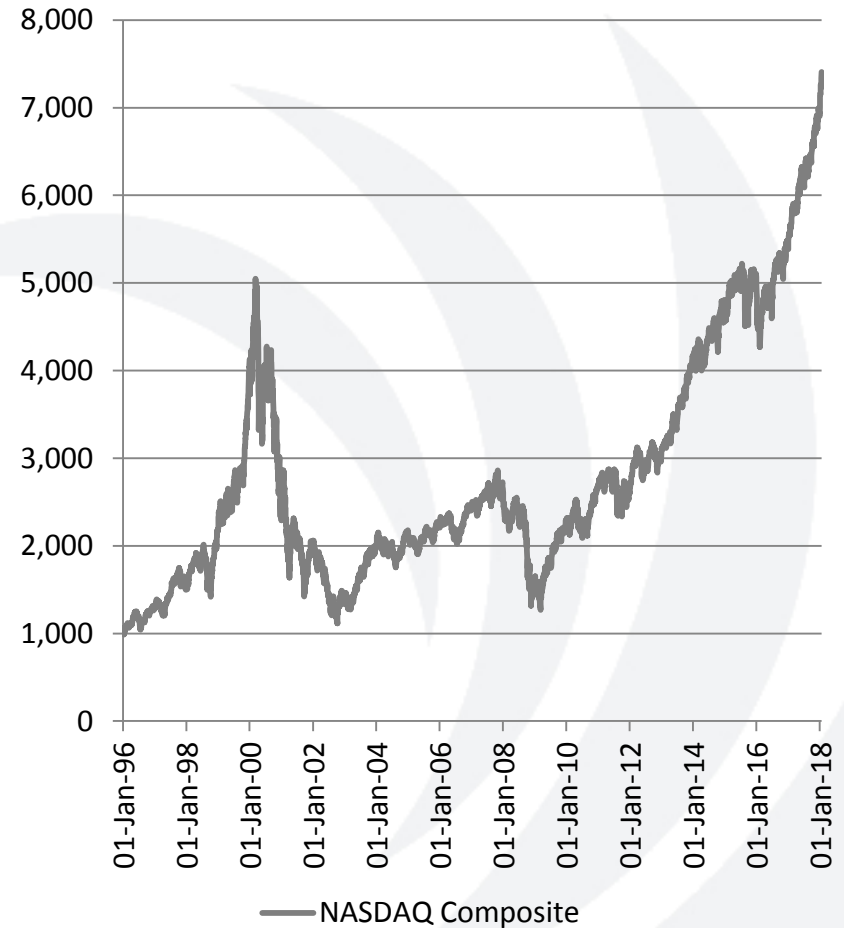
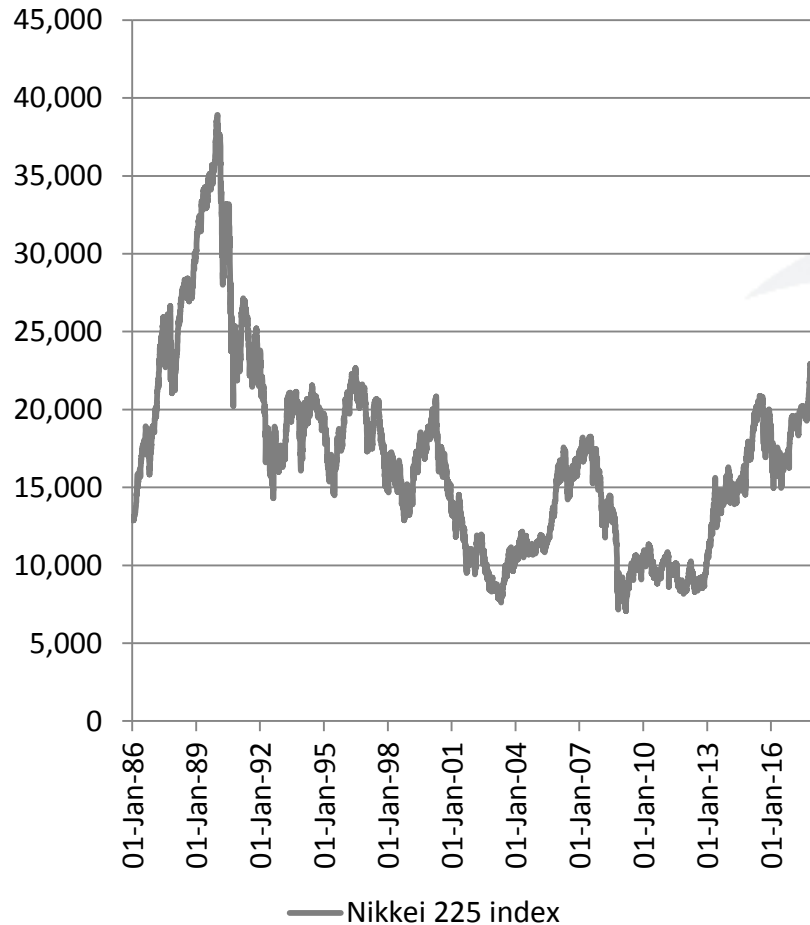
Source: Thomson Reuters Datastream

... or here!



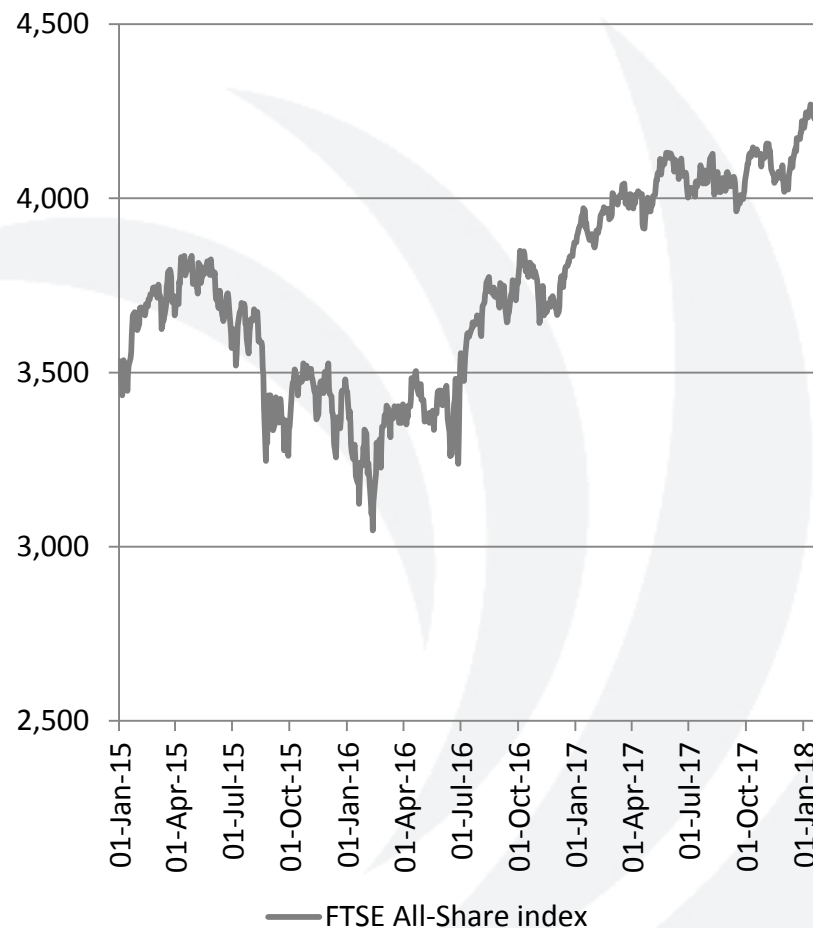
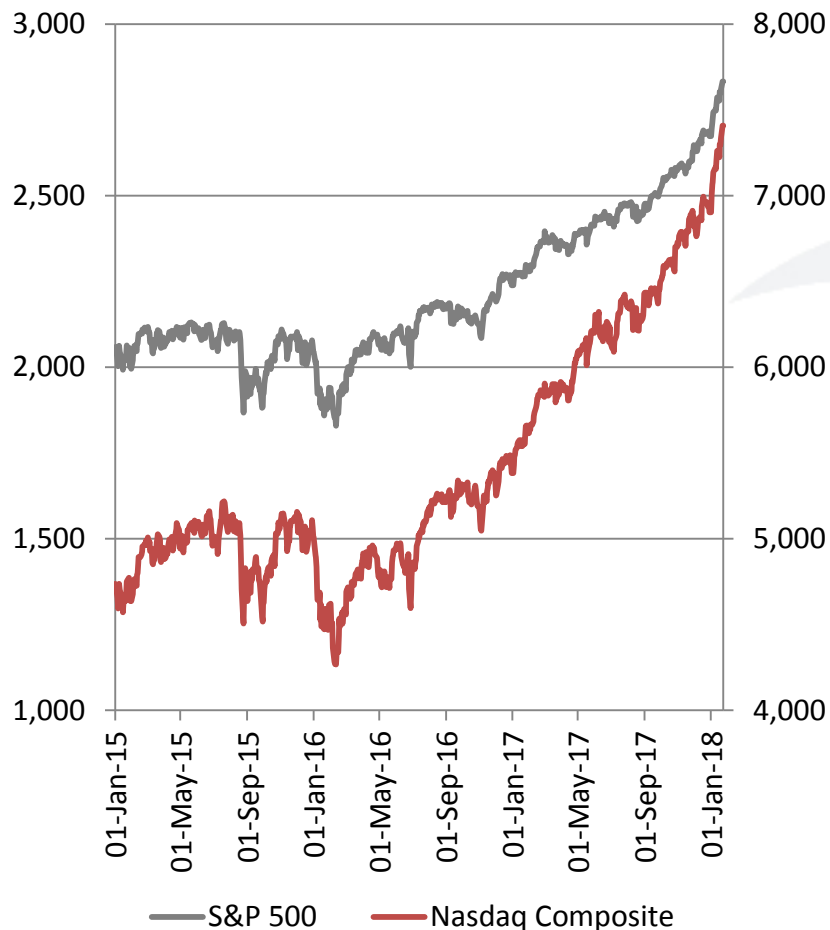
Source: NYSE, Thomson Reuters Datastream

## ii. Up, up and away – then ....



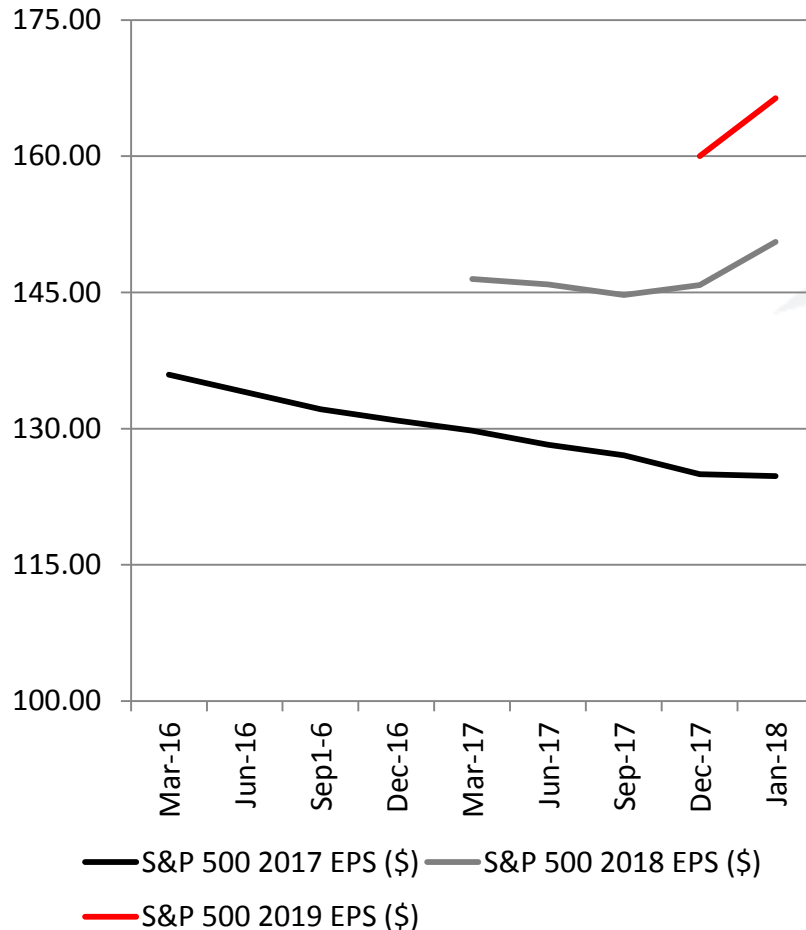
Source: Thomson Reuters Datastream

... And now

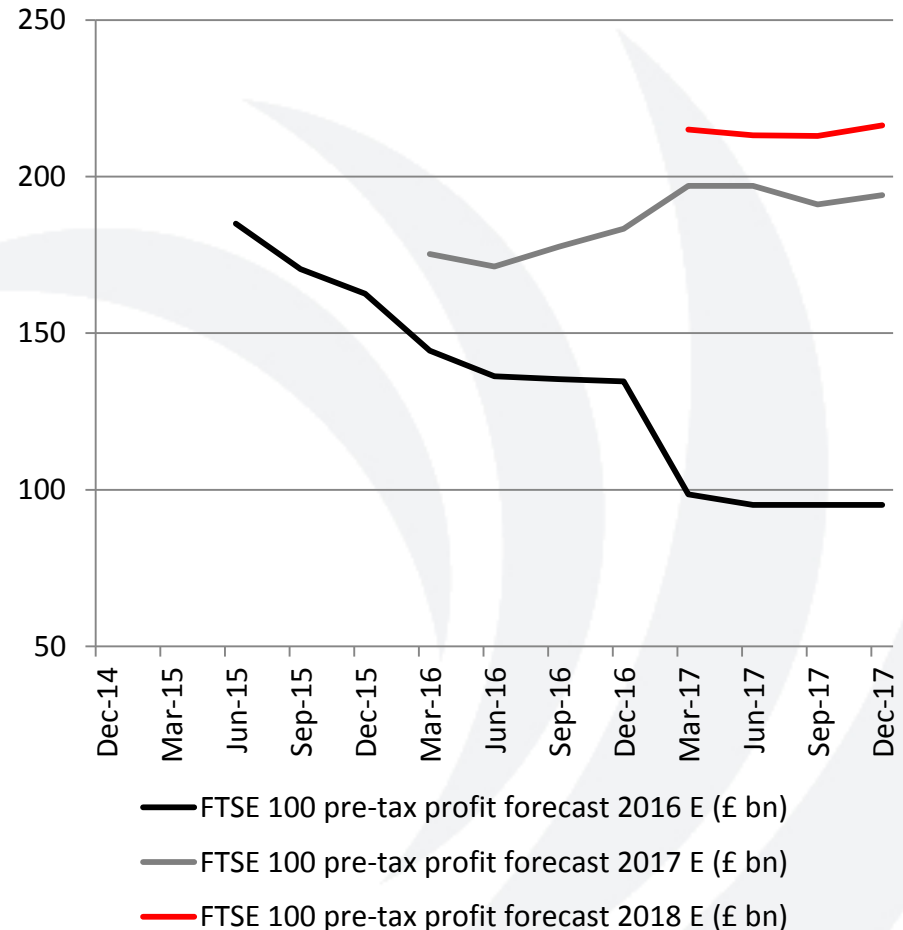


Source: Thomson Reuters Datastream

### iii. Earnings forecast momentum

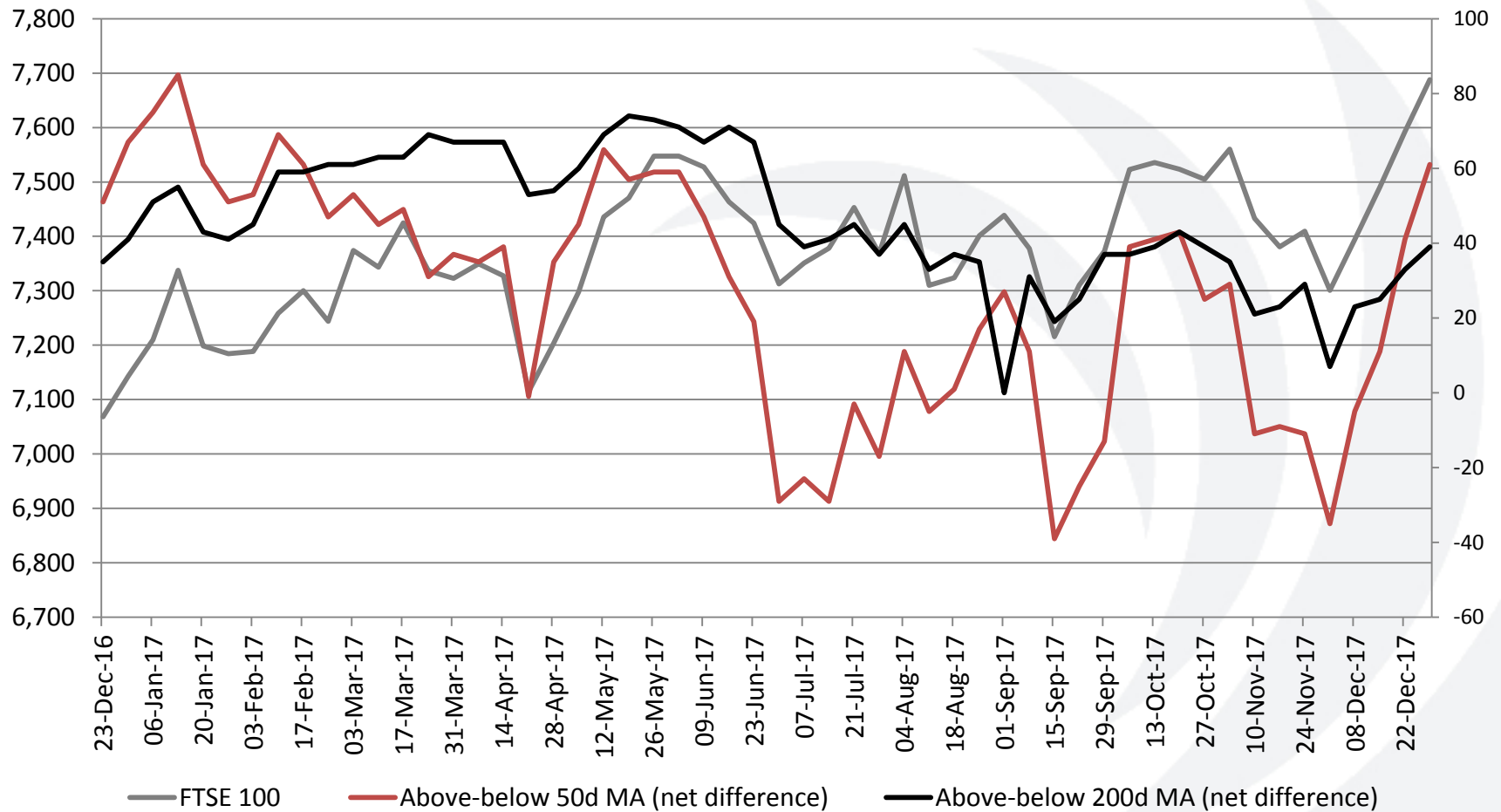


Source: Standard & Poor's



Source: Digital Look, consensus analysts' forecasts

## iv. Market breadth



Source: Bloomberg

## v. Move to defensives

### Best FTSE All-Share Sectors, 2018 to date

1	Autos & Parts	33.0%
2	Industrial Metals	12.6%
3	Elect. & Elect. Equipment	6.0%
4	Oil Equipment & Services	6.0%
5	Industrial Engineering	4.5%
6	Mining	3.5%
7	Banks	3.3%
8	Industrial Transportation	3.0%
9	Life Insurance	2.6%
10	Aerospace & Defence	2.4%

### Worst FTSE All-Share sectors, 2018 to date

30	Household Goods	(2.5%)
31	Healthcare Equipment	(2.7%)
32	Non-life Insurance	(2.9%)
33	Mobile Telecoms	(3.0%)
34	Real Estate Inv. Trusts	(3.2%)
35	Food Producers	(3.4%)
36	Software	(3.5%)
37	Beverages	(4.3%)
38	Gas, Water, Multi-Utilities	(4.6%)
39	Leisure Goods	(5.0%)

Source: Thomson Reuters Datastream, 1 to 23 January 2018

## vi. M & A

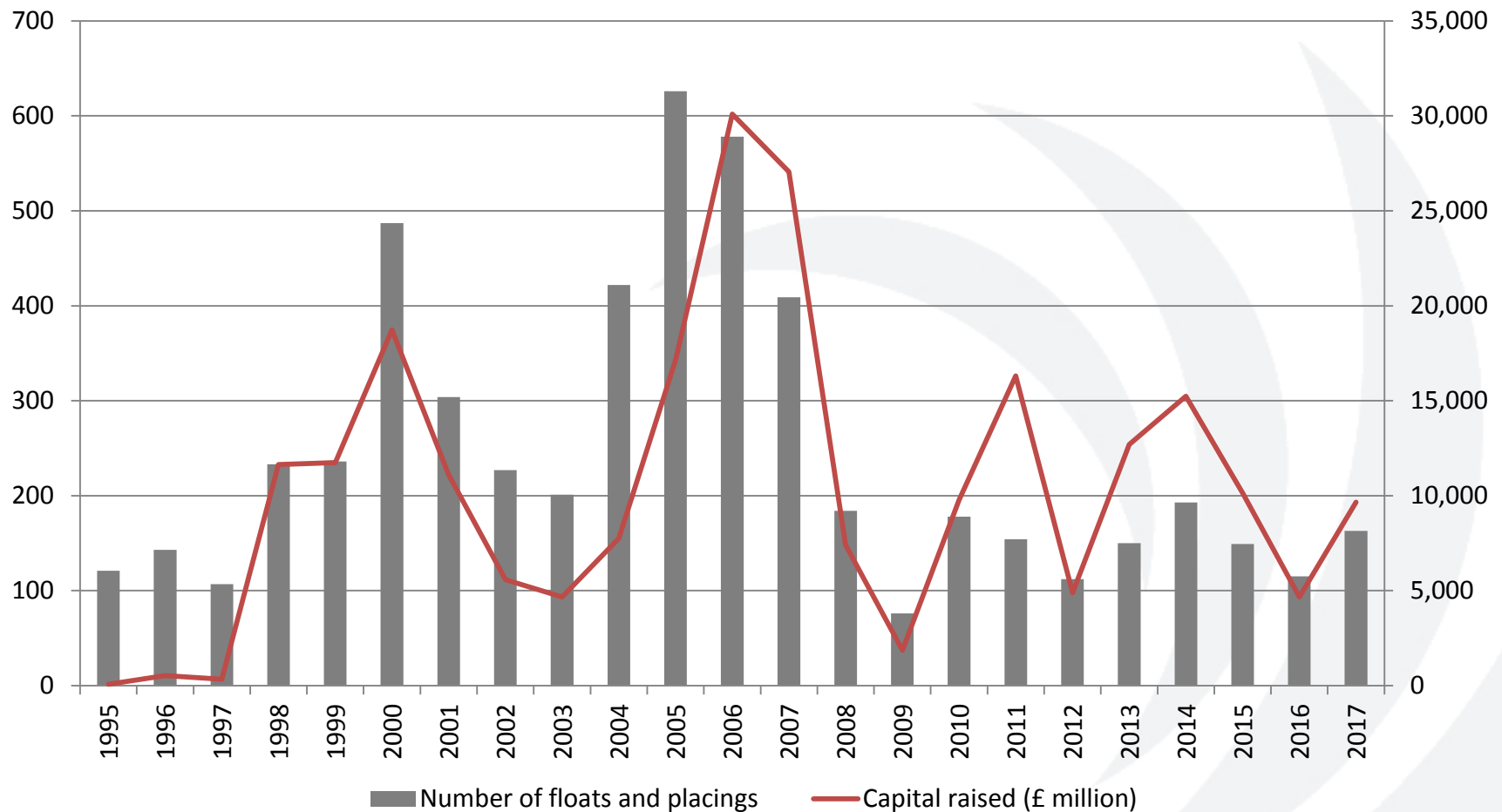
Acquirer	Acquired	Price	Year
Vodafone	Mannesmann	202	1999
AOL	Time Warner	165	2000
Verizon Communications	Verizon Wireless	130	2013
Anheuser Busch InBev	SAB Miller	130	2015
Dow Chemical	DuPont	130	2015
Pfizer	Warner Lambert	112	1999
AT&T	Time Warner	109	2016
Heinz	Kraft	100	2015
RBS / Santander / Fortis	ABN Amro	98	2007
Linde	Praxair	80	2016

*Source: Financial Times, Company Accounts.*

*One \$100bn-plus deal failed in 2017 – Kraft Heinz/Unilever (\$143bn) – while Broadcom/Qualcomm \$130 billion hostile bid is ongoing*

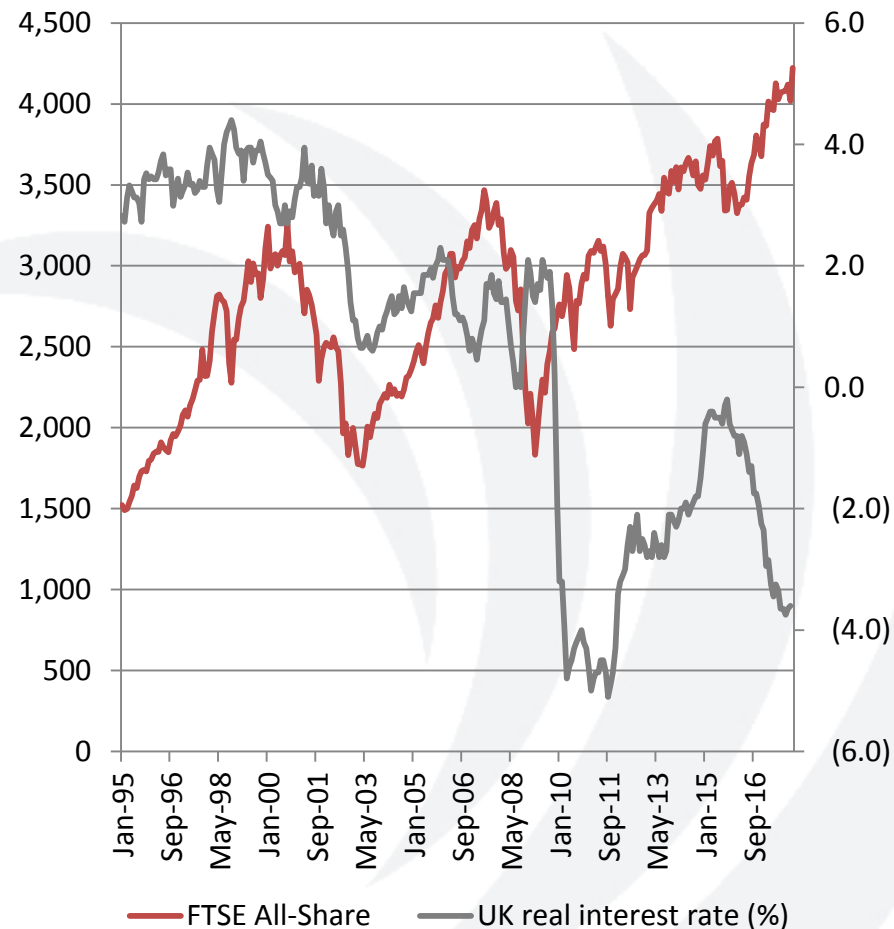
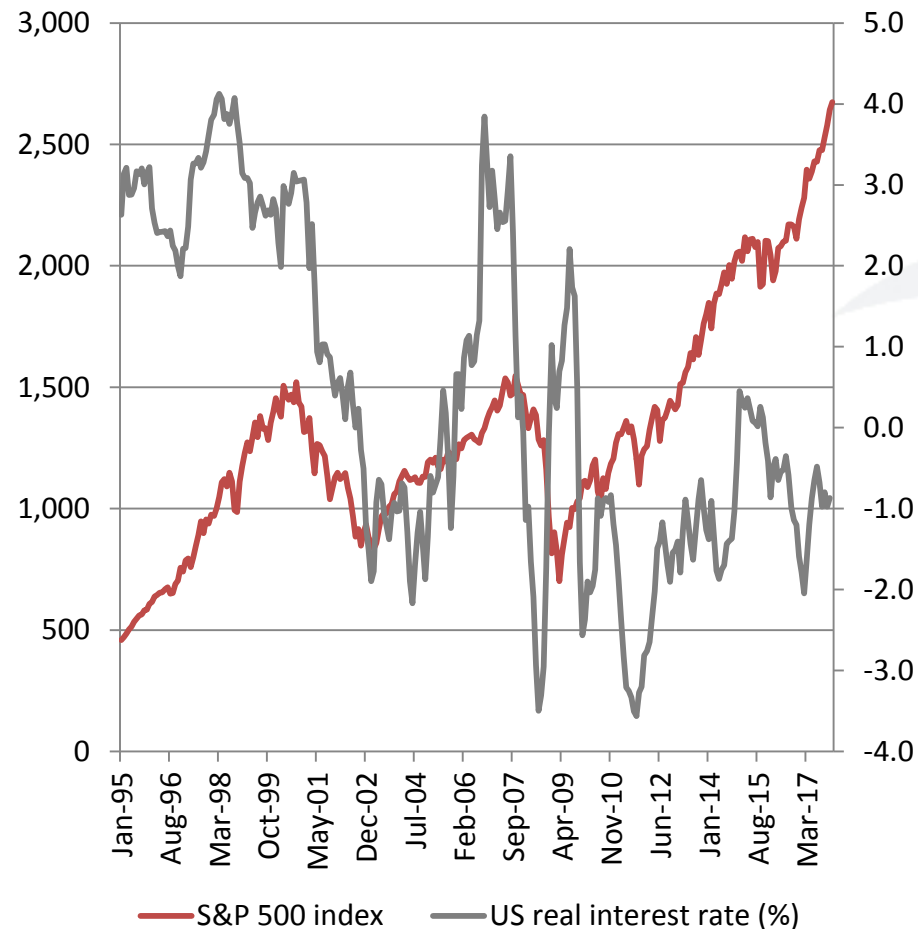


## vii. New listings



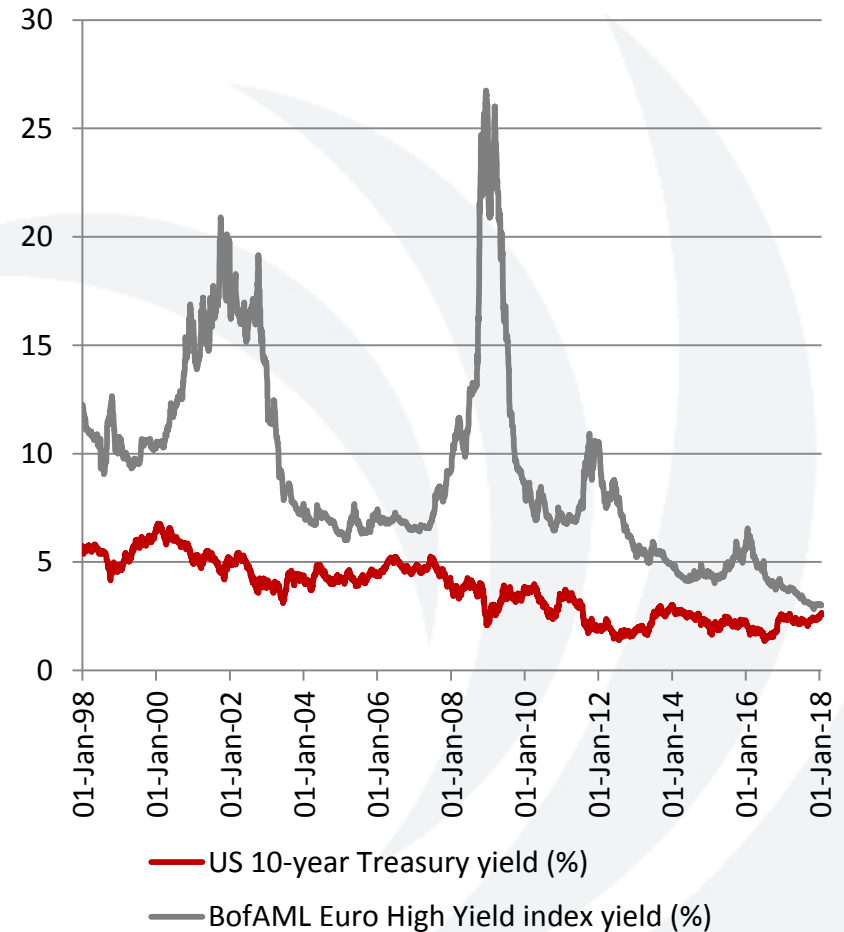
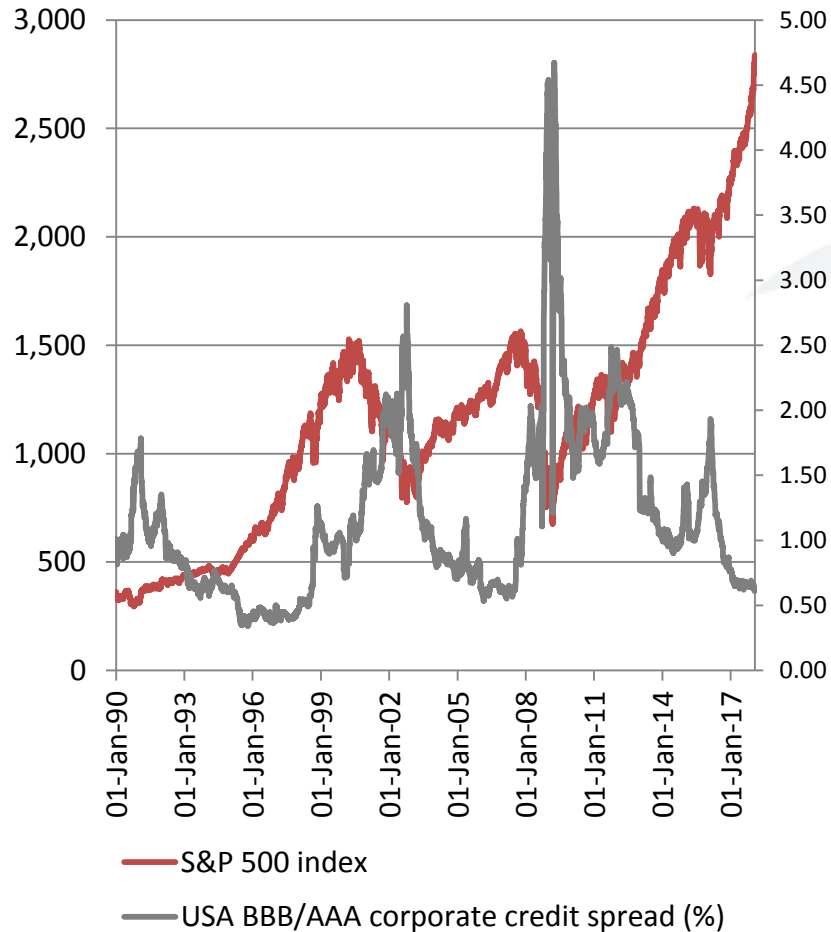
Source: London Stock Exchange

## viii. Interest rates



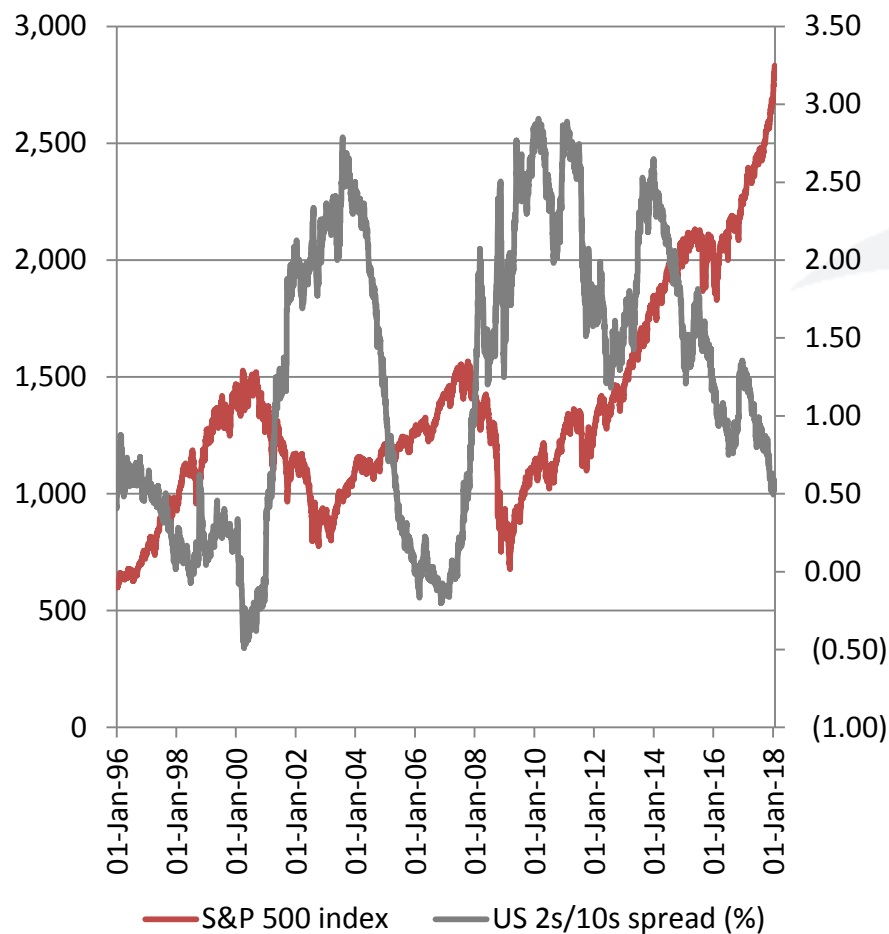
Source: Thomson Reuters Datastream

## ix. Credit spreads



Source: Thomson Reuters Datastream

## x. Yield curve



Source: Thomson Reuters Datastream

# Scorecard !

	Trouble ahead?
Earnings revisions are positive	Investor confidence levels are high
Market breadth is good	Credit spreads are low (but not rising)
No move to defensives	Yield curve is flattening
Real interest rates are (still) falling	
No deluge of new listings (yet) →	
No sign of a blow-off top (yet) →	
Merger & acquisition activity →	

### 3. Market cycles – Sir John Templeton's four phases

- “The four most expensive words in the English language are ‘this time it’s different.’”
- “Bull markets are born on pessimism, grown on scepticism, mature on optimism and die on euphoria.”

- *Sir John Templeton*



# The cycle

RECESSION	Current ranking *
Beverages	37
Electricity	22
Fixed-Line Telecoms	28
Food Producers	35
Food Retailers	11
Gas, Water & Multi-Utilities	38
Healthcare Equipment & Services	31
Mobile Telecoms	33
Non-life insurance	32
Personal Goods	29
Pharma & Biotech	25
Tobacco	20

LATE CYCLE	Current ranking *
Banks	7
Chemicals	15
Construction & Materials	12
Electronic & Electrical Equipment	3
Equity Investment Instruments	14
Forestry & Paper	16
General Industrials	13
General Financials	19
Industrial Engineering	5
Industrial Metals	2
Support Services	18

EARLY CYCLE	Current ranking *
Autos & Parts	1
General Retailers	24
Household Goods & Home Construction	30
Leisure Goods	39
Life Insurance	9
Media	27
Travel & Leisure	26

MID CYCLE	Current ranking *
Aerospace & Defence	10
Industrial Transport	8
Mining	6
Oil Equipment & Services	4
Oil & Gas Producers	17
Real Estate Investment & Services	23
Real Estate Investment Trusts	34
Software & Computer Services	36
Technology Hardware & Equipment	21

Source: Thomson Reuters Datastream for FTSE All-Share, 1 to 23 January 2018

# Templeton's four phases

## Pessimism (?)

Bricks & mortar retailers

Print / legacy media

Food retailers

Sterling

Value investing

## Scepticism (?)

Oil and oil equipment plays

Emerging market equities

Japanese equities

Precious metals and miners

The dollar

## Euphoria (?)

Cryptocurrencies

(European) junk bonds

FAANG stocks

(Chinese) social media / web stocks

Index proliferation

## Optimism (?)

Developed equities (especially USA)

Developed market bonds

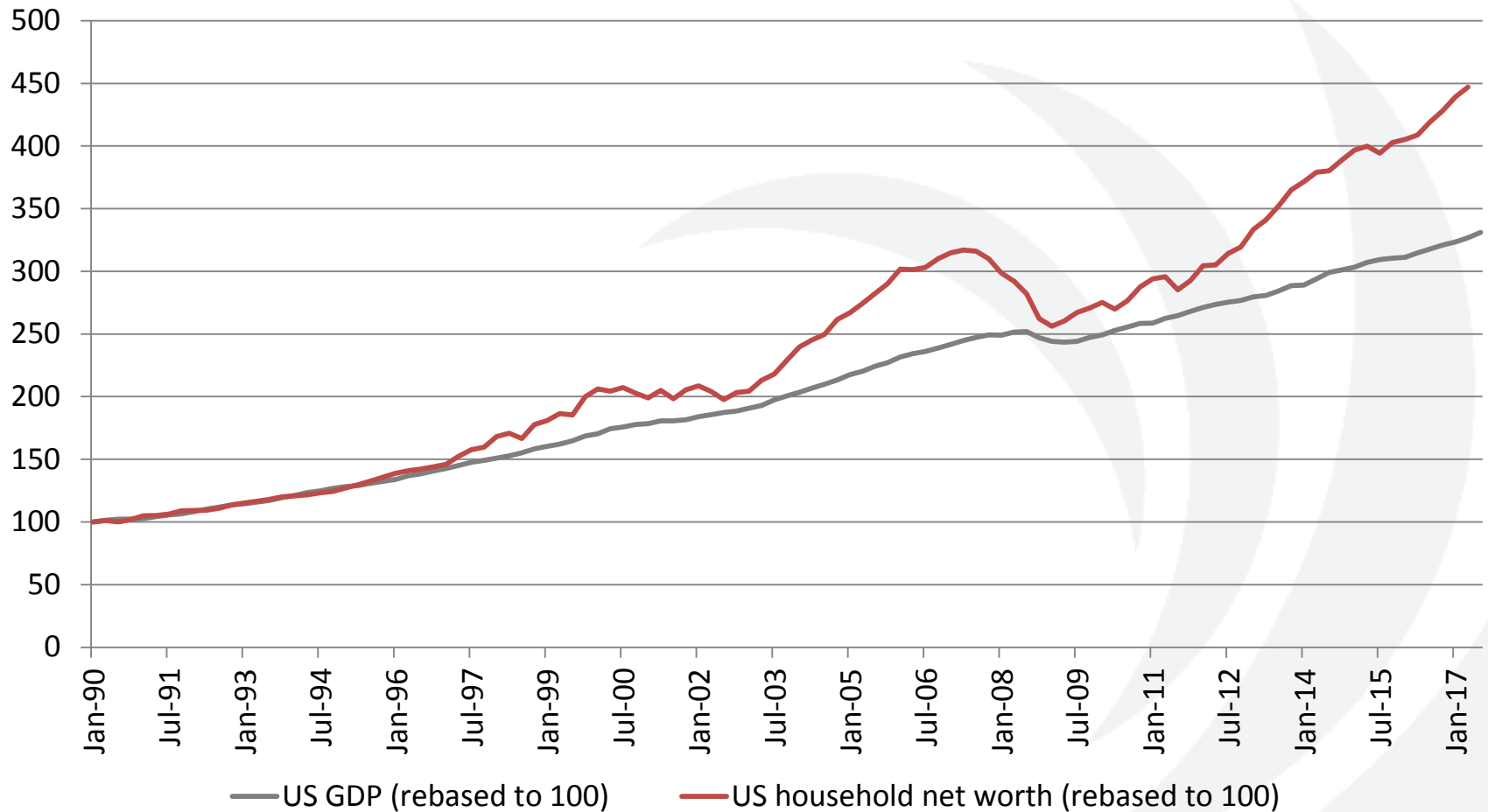
Emerging market bonds

Residential property

Income / growth & momentum investing



# The cycle



Source: 720Global, FRED, St. Louis Federal Reserve database

# The cycle

- “ The line separating investment and speculation, which is never bright and clear, becomes blurred still further when most market participants have recently enjoyed triumphs. Nothing sedates rationality more than effortless doses of money ....
- “ But a pin lies in wait for every bubble. And when the two eventually meet, a new wave of investors learns some very old lessons.
- “ First, many in Wall Street – a community in which quality control is not prized – will sell investors anything they will buy. Second, speculation is most dangerous when it looks easiest.”

- *Warren Buffett (2000)*

Enough said



# Conclusions

- “Rising prices are a narcotic that affects the reasoning power up and down the line.” – *Warren Buffett*
- Timing cycles is nigh-on impossible – think long-term and keep costs low
- There are still multiple potential outcomes – inflation, deflation, stagflation – all of which would require different portfolio solutions
- Consider risk as well as reward, especially after a bull run in nearly everything – some assets are now expensive relative to history

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