Kenanga Investors

Date: 2 October 2018

NO BULL'S EYE IN READING THE MARKET

Focus Malaysia (29 September 2018)

By Ismitz Matthew De Alwis

- **NOBODY** CAN CLAIM TO BE ABLE TO READ THE MARKET WITH 100% ACCURACY
- **THE** BEST POLICY FOR INVESTORS IS TO HAVE A VERSATILE BACK-UP PLAN AT ALL TIMES

THE Dow Jones Industrial Index (DJIA) has scaled a dizzying height and it is both a boon and bane for investors (not to mention how the S&P 500 index and Nasdaq Composite Index have been churning out their best August performance since 2014). A boon because well-researched investors can continue to cash in on stock gains on condition that their stock selection is right, considering not all industries or sectors are thriving at any given time. A bane because having touched an all-time high of 26,616.71 on Jan 26 and has ever since been holding steady above the 25,000-mark, the Dow's cur-rent level heightens as much the likelihood of a market crash which would have dire consequences on emerging markets (EMs) given their vulnerability or sensitivity to any US market correction.

On this note, more market detractors – either out of good intent or with vested interest – have joined the chorus in expressing pessimism about the sustainability of the US$30 tril (RM124.06 tril) American equity market moving forward, presumably arguing along the basic physics law of "the higher the climb, the greater the fall." One of them is John Hussman, president of Hussman Investment Trust, who has often been dubbed a "prophet of doom" in the stock market circle. In a recent call, Hussman, whose claim to fame includes forecasting the market collapses of 2000 and 2007-2008, has predicted market losses – backed by what he refers to as the "Iron Law of Valuation" – in the order of -64% for the S&P 500 index, -57% for the Nasdaq 100 Index, -68% for the Russell 2000 index, and nearly -69% for the DJIA. Even using the Buffett Indicator which is what Warren Buffett, mogul of the Berkshire Hathaway empire, uses to get an overall feel for the valuation of US stocks, there are already tell-tale signs that the market is overheating.

Derived from the simple metric of just dividing the total market capitalisation of all US stocks (US$30.4 tril) by the latest gross domestic product (GDP), the current reading (as of Sept 3) of 148.9% is even higher than the 145% peak during the dotcom bubble era in the 1990s (which fell by 49% in March 2000) or 110% prior to the 2008 global financial crisis. While this indicator does not necessarily mean that the tides will turn anytime in the near future, it may be a smart idea for investors to chart their journeys a little defensively.

NOBODY CAN OUTDO THE MARKET

It is very common that even seasoned market forecasters often get their prediction either awesomely accurate or awfully miscued (otherwise they will no longer need to issue disclaimers at the end of their analysis). The truth is that no stock market metrics are 100% reliable at predicting corrections, crashes, rallies or stagnant stock markets. Otherwise, everyone would know exactly when to buy, sell and hold their

stocks in order to maximise their profits. In this regard, look no further than our 'super' investor-cum-philanthropist Koon Yew Yin who was humble enough to own up (in his blog) that he erred in buying too many shares of a certain main board counter.

Traders work on the floor of the New York Stock Exchange (NYSE)

He attributed his bullishness to his previous investments "which had gone up a few hundred percent within 2.5 years." As he bought the shares of that particular stock on margin financing, he has no better option but to dispose his holding at a loss when faced with margin calls (to complicate matters, the price of the stock dipped after it lost a court case). On a similar note, the 85-year-old savvy investor has also decided to stop posting his stock investment tips on a popular online forum effective Aug 31 to "avoid seeing senseless criticisms."

"Many a time, when I post buy recommendations with good intention, a few readers would say that I want them to buy so that I can profit off of them," he pointed out in what he described as his "last sermon on share investing." "But you must remember that even good shares with very good profit growth prospects do not move up or down continuously without temporary short-term corrections," he added.

CURRENT MARKET TRENDS

While every stock (or fund for that matter) has its own peculiarity (distinguishable patterns), it has to be accepted that – given that today's markets are inter-linked in many ways – the ability of a counter to outperform at both share price and profitability levels very much hinges on external as much as internal market developments. The recent US Federal Reserve's tendency of raising interest rates faster than expected has undoubtedly made emerging market assets less attractive.

Such a situation is further exacerbated by the recent financial crisis in Turkey – the country's worst currency crisis since 2001 – which will likely reduce investors' appetite for riskier assets while intensifying the movement of foreign capital from higher-yielding assets (i.e. hedge funds) to relatively safer ones (i.e. defensive stocks) in developed markets. Against such a backdrop, the greenback has been appreciating strongly – even against the ringgit – this year. On top of that, concerns over China's economic slowdown and intensifying global tensions have fuelled anxiety about the global economic growth and corporate earnings outlook.

Emerging economies that are reliant on external borrowings to fund economic growth and large current account deficits such as Turkey and Argentina are feeling the heat. Year-to-date, their currencies have depreciated about 40% against the US dollar. Moreover, with trade disputes as well as tighter US monetary policy dominating headlines – and with both the US and China in the late stages of an economic cycle – some volatility is to be expected for the remaining months of 2018. However, there is a silver lining in that the tone is much more upbeat from a fundamental perspective. Many EM countries – especially in Asia – appear healthier with improving current account balances as well as lower external debt to GDP ratio. On-going structural reforms in major economies notably China and India are also likely to boost sustainable long-term growth.

The 10 Worst Bear Markets in U.S History

Here's a look at the percentage drops and the duration of the 10 worst bear markets in U.S history

Start Date	Drop	Duration (months)
September 1929	-86%	33
March 1937	-60%	63
October 2007	-57%	17
March 2000	-49%	31
January 1973	-48%	21
November 1968	-36%	18
August 1987	-34%	3
May 1946	-30%	37
December 1961	-28%	7
November 1980	-27%	21

Source: Bloomberg ,Money Morning Staff Research

READING THE MARKET

Wonder how many investors would recall that the Dow plunged 2.5% or some 666 points to 25,520.96 on Feb 2 – and suffered its worst week in two years – as concerns over rising interest rates and inflation from a perceived overheated US economy triggered a long-feared sell-off. It was the worst day for stocks since President Donald Trump took office and also rather a grim reminder that the market has been on a historic nine-year bull run. All-in, excluding the Feb 2's plunge, there have been 17 times when the Dow had declined 500 points or more in a single day over the past 25 years (since 1993). Although the tendency is such that the benchmark market index tends to rebound the next day or the following week, one should bear in mind that past performances do not always equal future returns. In other words, should interest rates continue to soar, they could trigger sell-offs that buck historical trends.

Whether that stock market cycle hypothesis does hold water or otherwise, one thing for sure is that intermittent market shocks and swings (e.g. currently market is down due to trade tensions between US and China) is inevitable. While a gung-ho investor relishes the thrill of betting his last penny on a strong upward trajectory till a more obvious tell-tale sign of a crash looms, investors with low risk appetites would have already commenced their 'market descent' measure, particularly by exiting their holdings of speculative stocks while maintaining (or even increasing) their holding of high dividend-yielding counters.

Whatever the case is, nothing beats having a versatile back-up plan at all times, for even in the most bearish of markets a genius investor is still capable of pouncing on the slightest opportunity in sight to reap handsome gains. In essence, the science of technical analysis (or fundamental analysis) has to be streamlined with investment psychology given economic cycles, market exuberance and stock market swings are many a time heavily linked to human psychology of greed and fear. While there are painful market crashes, investors tend to have short-term memories – deliberately or otherwise. Soon, greed will step in and wash away memories of past crashes, while pushing investors to drive the economy and stock markets into fragile bubbles once more. And the cycle repeats itself endlessly.

ENDS

Ismitz Matthew De Alwis *is the executive director and CEO of Kenanga Investors Bhd and president of the Financial Planning Association of Malaysia (FPAM).*

Kenanga

Kenanga Investors

Article Source:
Focus Malaysia. (29 September 2018)

- **Nobody** can claim to be able to read the market with 100% accuracy
- **The** best policy for investors is to have a versatile back-up plan at all times

No bull's eye in reading the market

by Ismitz Matthew De Alwis

The Dow Jones Industrial Index (DJIA) has scaled a dizzying height and it is both a boon and bane for investors (not to mention how the S&P 500 Index and Nasdaq Composite Index have been churning out their best August performance since 2014).

A boon because well-researched investors can continue to cash in on stock gains on condition that their stock selection is right, considering not all industries or sectors are thriving at any given time.

A bane because having touched an all-time high of 26,616.71 on Jan 26 and has ever since been holding steady above the 25,000-mark, the Dow's current level heightens as much the likelihood of a market crash which would have dire consequences on emerging markets (EMs) given their vulnerability or sensitivity to any US market correction.

On this note, more market detractors – either out of good intent or with vested interest – have joined the chorus in expressing pessimism about the sustainability of the US$30 tril (RM124.06 tril) American equity market moving forward, presumably arguing along the basic physics law of "the higher the climb, the greater the fall."

One of them is John Hussman, president of Hussman Investment Trust, who has often been dubbed a "prophet of doom" in the stock market circle.

In a recent call, Hussman, whose claim to fame includes forecasting the market collapses of 2000 and 2007-2008, has predicted market losses – backed by what he refers to as the "Iron Law of Valuation" – in the order of -64% for the S&P 500 Index, -57% for the Nasdaq 100 Index, -68% for the Russell 2000 Index, and nearly -69% for the DJIA.

Even using the Buffett Indicator which is what Warren Buffett, mogul of the Berkshire Hathaway empire, uses to get an overall feel for the valuation of US stocks, there are already tell-tale signs that the market is overheating.

Derived from the simple metric of just dividing the total market capitalisation of all US stocks (US$30.4 tril) by the latest gross domestic product (GDP), the current reading (as of Sept 3) of 148.9% is even higher than the 145% peak during the dotcom bubble era in the 1990s (which fell by 49% in March 2000) or 110% prior to the 2008 global financial crisis.

Traders work on the floor of the New York Stock Exchange (NYSE)

While this indicator does not necessarily mean that the tides will turn anytime in the near future, it may be a smart idea for investors to chart their journeys a little defensively.

Nobody can outdo the market

It is very common that even seasoned market forecasters often get their prediction either awesomely accurate or awfully missed (otherwise they will no longer need to issue disclaimers at the end of their analysis).

The truth is that no stock market metrics are 100% reliable at predicting corrections, crashes, rallies or stagnant stock markets. Otherwise, everyone would know exactly when to buy, sell and hold their stocks in order to maximise their profits.

In this regard, look no further than our 'super' investor-cum-philanthropist Koon Yew Yin who was humble enough to own up (in his blog) that he erred in buying too many shares of a certain main board counter.

He attributed his bullishness to his previous investments "which had gone up a few hundred percent within 2.5 years."

As he bought the shares of that particular stock on margin financing, he has no better option but to dispose his holding at a loss when faced with margin calls (to complicate matters, the price of the stock dipped after it lost a court case). On a similar note, the 85-year-old savvy investor has also decided to stop posting his stock investment tips on a popular online forum effective Aug 31 to "avoid seeing senseless criticisms."

"Many a time, when I post buy recommendations with good intention, a few readers would say that I want them to buy so that I can profit off of them," he pointed out in what he described as his "last sermon on share investing."

"But you must remember that even good shares with very good profit growth prospects do not move up or down continuously without temporary short-term corrections," he added.

The 10 Worst Bear Markets in U.S History

Here's a look at the percentage drops and the duration of the 10 worst bear markets in U.S history

Start Date	Drop	Duration (months)
September 1929	-86%	33
March 1937	-60%	63
October 2007	-57%	17
March 2000	-49%	31
January 1973	-48%	21
November 1968	-36%	18
August 1987	-34%	3
May 1946	-30%	37
December 1961	-28%	7
November 1980	-27%	21

Source: Bloomberg, Money Morning Staff Research

Current market trends

While every stock (or fund for that matter) has its own peculiarity (distinguishable patterns), it has to be accepted that – given that today's markets are inter-linked in many ways – the ability of a counter to outperform at both share price and profitability levels very much hinges on external as much as internal market developments.

The recent US Federal Reserve's tendency of raising interest rates faster than expected has undoubtedly made emerging market assets less attractive.

Such a situation is further exacerbated by the recent financial crisis in Turkey – the country's worst currency crisis since 2001 – which will likely reduce investors' appetite for riskier assets while intensifying the movement of foreign capital from higher-yielding assets (i.e. hedge funds) to relatively safer ones (i.e. defensive stocks) in developed markets.

Against such a backdrop, the greenback has been appreciating strongly – even against the ringgit – this year. On top of that, concerns over China's economic slowdown and intensifying global tensions have fuelled anxiety about the global economic growth and corporate earnings outlook.

Emerging economies that are reliant on external borrowings to fund economic growth and large current account deficits such as Turkey and Argentina are feeling the heat. Year-to-date, their currencies have depreciated about 40% against the US dollar.

Moreover, with trade disputes as well as tighter US monetary policy dominating headlines – and with both the US and China in the late stages of an economic cycle – some volatility is to be expected for the remaining months of 2018.

However, there is a silver lining in that the tone is much more upbeat from a fundamental perspective. Many EM countries – especially in Asia – appear healthier with improving current account balances as well as lower external debt to GDP ratio. Ongoing structural reforms in major economies notably China and India are also likely to boost sustainable long-term growth.

Reading the market

Wonder how many investors would recall that the Dow plunged 2.5% or some 666 points to 25,520.96 on Feb 2 – and suffered its worst week in two years – as concerns over rising interest rates and inflation from a perceived overheated US economy triggered a long-feared sell-off.

It was the worst day for stocks since President Donald Trump took office and also rather a grim reminder that the market has been on a historic nine-year bull run. All-in, excluding the Feb 2's plunge, there have been 17 times when the Dow had declined 500 points or more in a single day over the past 25 years (since 1993).

Although the tendency is such that the benchmark market index tends to rebound the next day or the following week, one should bear in mind that past performances do not always equal future returns. In other words, should interest rates continue to soar, they could trigger sell-offs that buck historical trends.

Whether that stock market cycle hypothesis does hold water or otherwise, one thing for sure is that intermittent market shocks and swings (e.g. currently market is down due to trade tensions between US and China) is inevitable.

While a gung-ho investor relishes the thrill of betting his last penny on a strong upward trajectory till a more obvious tell-tale sign of a crash looms, investors with low risk appetites would have already commenced their 'market descent' measure, particularly by exiting their holdings of speculative stocks while maintaining (or even increasing) their holding of high dividend-yielding counters.

Whatever the case is, nothing beats having a versatile back-up plan at all times, for even in the most bearish of markets a genius investor is still capable of pouncing on the slightest opportunity in sight to reap handsome gains.

In essence, the science of technical analysis (or fundamental analysis) has to be streamlined with investment psychology given economic cycles, market exuberance and stock market swings are many a time heavily linked to human psychology of greed and fear. While there are painful market crashes, investors tend to have short-term memories – deliberately or otherwise.

Soon, greed will step in and wash away memories of past crashes, while pushing investors to drive the economy and stock markets into fragile bubbles once more. And the cycle repeats itself endlessly.

Ismitz Matthew De Alwis is the CEO of Kenanga Investors Bhd and president of the Financial Association of Malaysia