Infomail
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Pessimists are Getting Desperate

"I can calculate the movement of the stars, but not the madness of men"

Sir Isaac Newton
(After losing a fortune in the South Sea Bubble)

In case one has not noticed, there has been a surge in market forecasts lately claiming the recent run in the equity markets has resulted in a stock market "bubble." There are articles and commentary all over which have used the word "bubble." The fear, of course, is that when the euphoria ends, prices will fall resulting in significant losses for investors who don't bail out first.

Probably the best method to determine where there is a bubble would be to simply look at past performance and measure how far in excess of the long term averages it has been. For example:

- Gold experienced a 10 year run which began in 1971 where it returned 32% per year.
- US Small Caps earned 27% annualized in the decade ending in 1984
- Japanese stocks produced over 28% annualized in the 1980's

All these results were well above long term averages and obviously unsustainable, and eventually, nature takes its course as they say and everything "reverts back to the mean."

Looking at today's data, I see a different picture:

	Nov 03-Oct 13	1928-2002	Difference
US Total Stock Index	7.9%	9.6%	-1.7%
Equity Asset Mix	10.3%	11.9%	-1.6%
Balanced Asset Class Mix	8.7%	10.3%	-1.6%

(Using Historical Annualized Returns [1928 to 2013])

Warren Buffet once said something to the effect that forecasts say more about the person making them than the actual claim itself. So the same can be said for the bubble predicting when markets will rise or fall.

The bad news headlines which seem to have dominated the past 6 years appear to be in the rear view mirror now. So now that it seems most news is good news, the pessimists figure it's time for a large drop……but they've been saying that for 6 months now. Remember "sell in May and go away?"

So since markets have not experienced a 10% pullback in about a year and a half, logically then, every day that goes by would mean we are a day closer to some sort of slide.

But I would hazard to guess any pullbacks for the time being will remain short in duration and shallow in depth. Even with the Fed on the verge of tapering (some rumours say maybe even this week), in my experience the first knee jerk reaction downward to Fed actions is generally a strong buying opportunity.

Financial markets have been discounting the tapering for months and were actually all set for it back in September, and whether it happens in December or March, that's less important than the reality that the US and global economy is recovering.

Payroll numbers get better, housing numbers are improving, auto sales are at their best since 2007 and the markets continue to make new highs. Despite Keynesians proclaiming the partial government shutdown and Sequester were supposed to hurt the economy, they've been anything but. Imagine, what would happen if the US really down sized big government?

Sure lately stocks are looking tired, as if looking for a place to relax. Pullbacks are normal and part of investing. Real people trying to simply fund a comfortable retirement have been investing, and they've been rewarded. Many investors have simply underperformed because they've been on the sidelines or simply too conservative.

As for the current state of the global equity markets, things appear to be pretty normal. Recent returns (the last 10 years) have been about what we'd expect. But given the drubbing investors took in 2008-09, it is normal to expect above average returns……and I believe more are on their way.

Stay tuned,

Vito Finucci
Vice President and Director
Investment Advisor

P.S. This will be the last Infomail for 2013. Thank you to everyone for the comments, emails and feedback in the past year. I'd like to wish all readers a very Merry Christmas and Holiday Season from all of us here at RBC Dominion Securities.