thenavigator

Autumn 2024

Back to the future

I remember the 1990s as if it were yesterday. It was the post-Cold War decade, marked by the rise of the USA as the sole superpower. This period also saw the first screenings of the TV series *Friends* and the movie franchise *Wayne`s World*. After a slow start in the early ‘90s, markets certainly did party on.

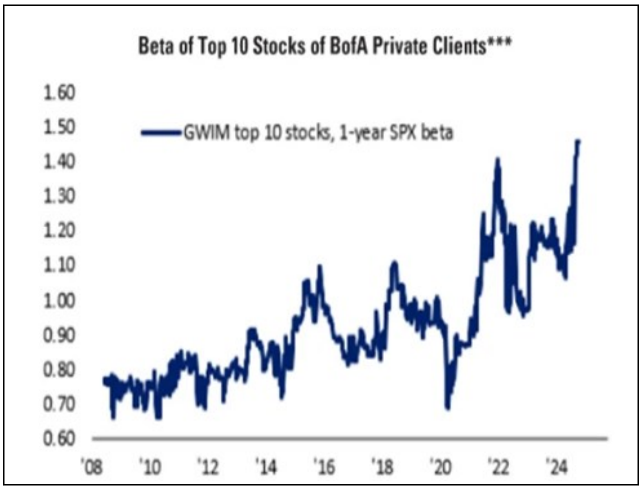
It was the era when many City traders were awarded large cash bonuses, with some setting up restaurants to explore their creative talents. We also saw the rise of two new demographic subsets – the yuppies and the dinkies (dual income no kids) – who often had matching BMWs or, if they were really successful, matching Porsche 911s. It was also the era of power dressing for both men and women, who often spent over £50,000 on lunches at the best restaurants.

Of course, much of this joie de vivre came from stock market investments, mainly in bubble stocks. Whenever extra money was needed, it was taken from the portfolio, which seemed to miraculously increase in value every day. Life seemed like a dream but, in hindsight, it was a mirage.

By late 1999, despite being ever the optimist, I really felt that things had got out of hand and issued words of caution to my colleagues. Of course, given the easy gains they were making on a regular basis, these words either fell on deaf ears or were met with ridicule and comments that I was out of touch with the new era.

It was also during this period that famous hedge fund managers such as Julian Robertson were forced to close their funds and turn them into family offices due to vast redemptions, as their performance temporarily failed to keep up with the market.

In addition, there were various uncomplimentary articles speculating that Warren Buffett was too old, had lost his touch and was unable to adapt to the new paradigm that was unfolding in front of us.



Source: Beta of Top 10 Stocks of BofA Private Clients, 2008-2024, chart by Richard Bernstein Advisors LLC

The early 2000s were pretty bleak and not much fun. I blamed this on the overhyping of the millennium, which could only disappoint given the ludicrous build-up. I also clearly remember the very uncomfortable conversations my colleagues on the discretionary portfolio management team were having with their clients, trying to explain how their substantial portfolios had seemingly evaporated into thin air overnight.

Decades later, with hindsight, it is easy to see that I was living through my first ever financial bubble. It has been said that financial markets enter periods of euphoria or bubbles every 20 years or so. Part of the rationale for this is that it gives time for investors involved in the previous bubble to nurse their wounds – which are always deep –

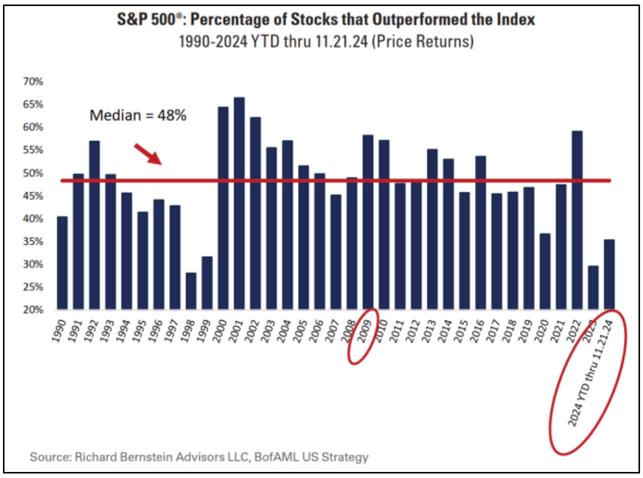
and to experience some amnesia. It also allows time for a new generation of investors to emerge who, of course, always know better and are much more au fait with the latest technology that will change everything.

As the secular bull market in US stocks reaches its 16th year, the S&P500 has achieved its 53rd record high of the year, while bitcoin has reached the USD 100,000 mark. While these milestones reflect significant market enthusiasm, they also raise important questions about sustainability in certain market areas. Overvaluation and increased volatility may pose meaningful risks, and investors should carefully consider these dynamics when navigating current market conditions. We believe investors in certain parts of the market should be afraid – very afraid.

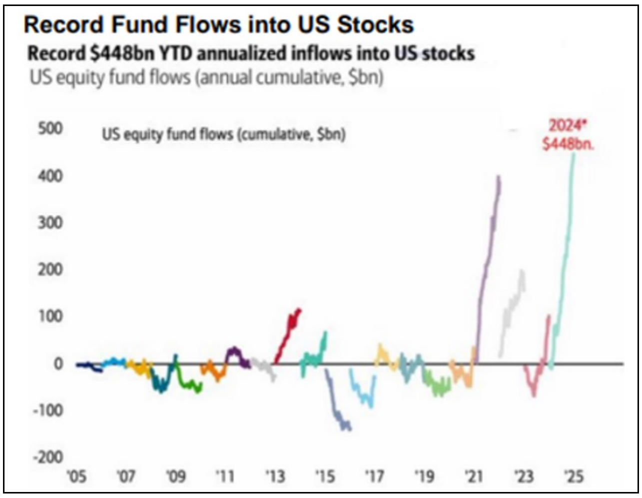
An alternative Christmas tale

As we approach the traditional year-end festive season, we feel rather like Ebenezer Scrooge crying out "Bah, humbug!"

As investors gorge on their daily market gains without even a "Please, sir, can I have some more?" (*Oliver Twist*), we see other similarities between Dickens' novels and Victorian society. Many of those who are chasing things at the moment are likely to end up in the Victorian equivalent of the poorhouse.



Source: S&P 500: Percentage of Stocks that Outperformed the Index, 1990-2024 YTD (Price Returns), chart by Richard Bernstein Advisors LLC



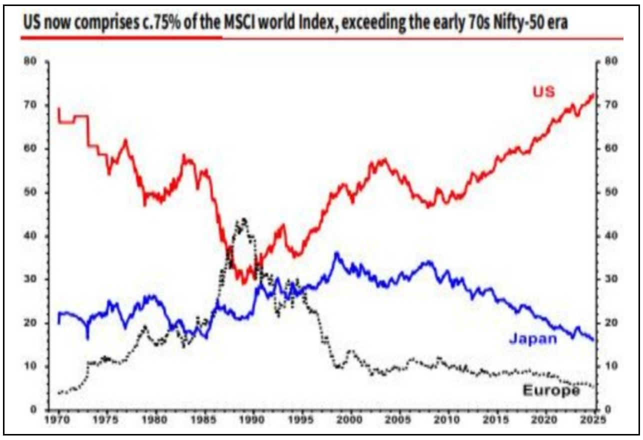
Source: BofA Global Investment Strategy, US Equity Fund Flows (annual cumulative, $ bn), 2005-2024, chart by Richard Bernstein Advisors LLC

Nobody really knows the exact cause of the market crash of 1929, but many feel that one of the major reasons was a reckless overconfidence on the part of investors, which led to an asset bubble that eventually burst, as is the fate of all bubbles.

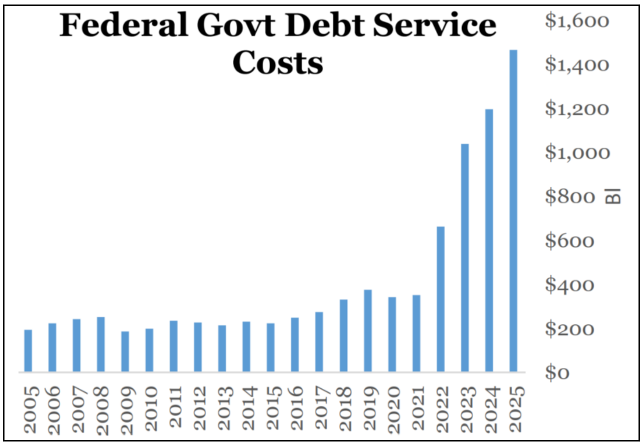
I believe that I am witnessing the second large asset bubble of my career; I desperately hope to witness a couple more before I hang up my boots. We are, I believe, close to the point in time where we will see the end of the secular bull market in US stocks that began 16 years ago.

In 2009, investor caution was reflected in stock ownership levels at just 39% and an average beta of 0.75. Today, stock ownership has surged to 63% and the average beta has climbed to 1.45, signalling a notable shift towards higher-risk exposure.

While this trend may suggest growing confidence in markets, it also underscores the potential for increased portfolio volatility and sensitivity to market corrections. Investors should remain mindful of the risks associated with elevated beta and higher equity allocations as part of their broader investment strategy.

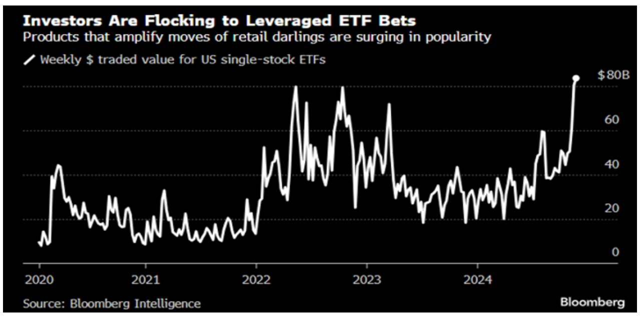


Source: Datastream; US now comprises c.75% of the MSCI world Index, exceeding the early 70s Nifty-50 era, 1970-2024, chart extracted from The Bear Traps Report With Larry McDonald, dated November 24, 2024

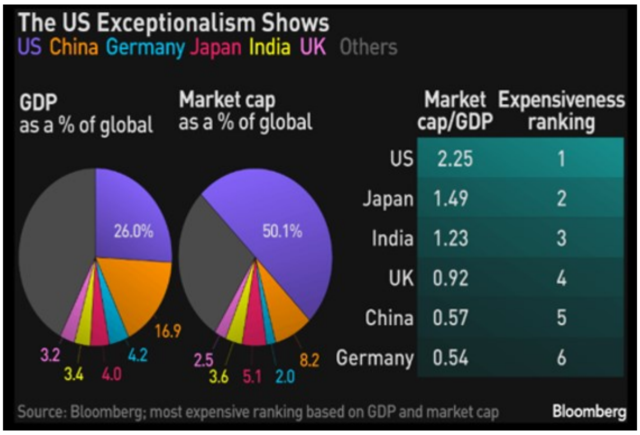


Source: Datastream; Federal Govt Debt Service Costs, 2005-2024, chart extracted from The Bear Traps Report With Larry McDonald, dated November 24, 2024

The US deficit is already a problem but is only likely to get worse with tax cut giveaways.

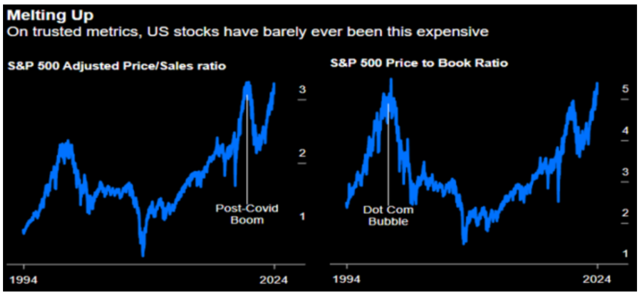


Source: Weekly $ traded value for US single-stock ETFs, 2020-2024, chart by Bloomberg



Source: Most expensive ranking based on GDP and market cap, 2024, chart by Bloomberg

Leverage is one of the key themes of every asset bubble. Rational valuation measures, such as the Buffett indicator (the size of the stock market compared to a country's GDP), are flashing bright red. It therefore comes as no surprise that Mr Buffett holds his largest cash pile ever and is too scared to even buy back his own stock!

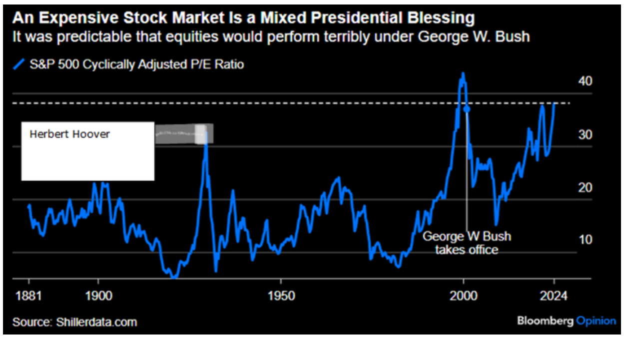


Source: S&P500 Adjusted Prices/Sales ratio, 1994-2024; and S&P500 Price to Book Ratio, 1994-2024; charts by Bloomberg

While inflation in the US has been edging down, recent developments such as blanket tariffs, tightening immigration and tax cuts are all inflationary. This is without taking into account recent pay developments – Boeing machinists and dock workers just received a multi-year payout deal averaging nearly 9% per annum.

I really struggle to see how the magic 2% inflation target will be reached, and it is more likely that the US economy has inflation running at 3.5-5%. This in turn means that longer-dated US bond yields are seriously mispriced and that the 10-year yield could easily move to 5% or more.

While we are in the midst of US election euphoria, it should be remembered that sometimes you're just dealt a bum hand.



Source: S&P500 Cyclically Adjusted P/E Ratio, 1881-2024, Shillerdata.com; chart by Bloomberg

We remain unfashionably underweight in US equities, especially the most popular names. Meanwhile, we remain overweight in cash and short-dated quality bonds.

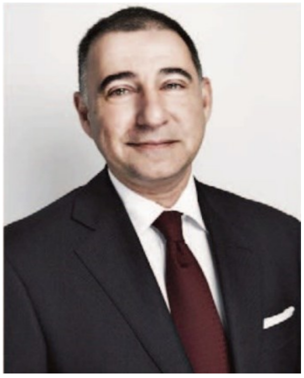
There are still opportunities within the equity space in less fashionable markets like Asia and Europe, including China and the UK. The question we always ask ourselves before investing in an area that we believe is mispriced is: why is it so, are the problems temporary, and what is the timeline?

Some of the best value we can find is in the auto and parts sector, where some segments of the industry may have underestimated the demand for electric vehicles.

However, this in the process of being addressed, and with the average age of a car in Europe and the US coming in at 13 years plus, the demand is there if the right products are available.

From a country perspective, we find potential investment opportunities in the UK, which we attribute to recent political changes and market reactions. France, which is going through a political crisis – although the average French household is saving 18% of its income – offers us a plethora of opportunities.

We are convinced that this is the right course of action, not just to preserve your wealth but also to enhance it in the years ahead.



The Navigator has been written by:
Peter Ahluwalia
Chief Investment Officer

Disclaimer

Important Information

The information in this material has been approved by swisspartners Advisors Ltd. ("swisspartners Advisors"). As a firm providing discretionary asset management services, swisspartners Advisors is authorized under the Swiss Financial Market Supervisory Authority ("FINMA") as portfolio manager and registered under the U.S. Investment Advisers Act of 1940 with the U.S. Securities and Exchange Commission ("SEC") as an investment advisor. Nothing in this material is a recommendation that you purchase, sell, subscribe or hold, or an offer or solicitation of a purchase or sale of any security, futures, options, other financial instruments or other investment, that you pursue any investment style or strategy or buy any other product or service. The value of, and income from, your investments may vary because of several risk factors, including but not limited to market, interest rate, credit, prepayment, liquidity, volatility and currency risks as well as other circumstances such as changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. This list is not exhaustive and you are strongly encouraged to consult with a qualified legal, tax and financial advisor before making any investment decision. Investors assume all risk and some or all of the amount invested may be lost.

This material does not take into consideration the specific investment objectives, financial situation or particular needs of any person that enters into a relationship with swisspartners Advisors. Nothing in this material is or is intended to be investment, accounting, tax or legal advice. You should consult with your own advisors concerning such matters. swisspartners Advisors does not provide legal, tax or accounting advice. The information contained herein was obtained from sources believed to be reliable. Although reasonable care was taken in gathering the information and formulating the opinions contained herein, swisspartners Advisors does not make any representation whatsoever as to its accuracy or completeness and accepts no liability for any loss arising from the use of this material. The information, opinions and estimates expressed herein reflect a judgment as of its original publication date and are subject to change without notice. No representation or warranty, expressed or implied, is made by swisspartners Advisors regarding future performance. The value and income of any securities or financial instruments can go up as well as down. The market value of securities or financial instruments may be affected by several circumstances, including among others, changes in economic, financial or political factors, time to maturity, market conditions and volatility, or the credit quality of any issuer or reference issuer. Foreign currency rates may have a positive or adverse effect on the value of any investment. Investors assume all risk and some or all of the amount invested may be lost. This material is not directed to, or intended for distribution to or use by, any person or entity that is a citizen or resident of, or located in, any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or subject swisspartners Advisors to any registration requirement.

IRS Circular 230 Disclosure: swisspartners Advisors and its affiliates do not provide legal or tax advice. Accordingly, any tax-related discussion contained herein (including any attachments) is not intended or written to be used, and cannot be used, in connection with promoting, marketing or recommending to any person any transaction or matter addressed herein or for the purpose of avoiding U.S. tax-related penalties.

For more information, please visit our website at www.swisspartners-advisors.com |