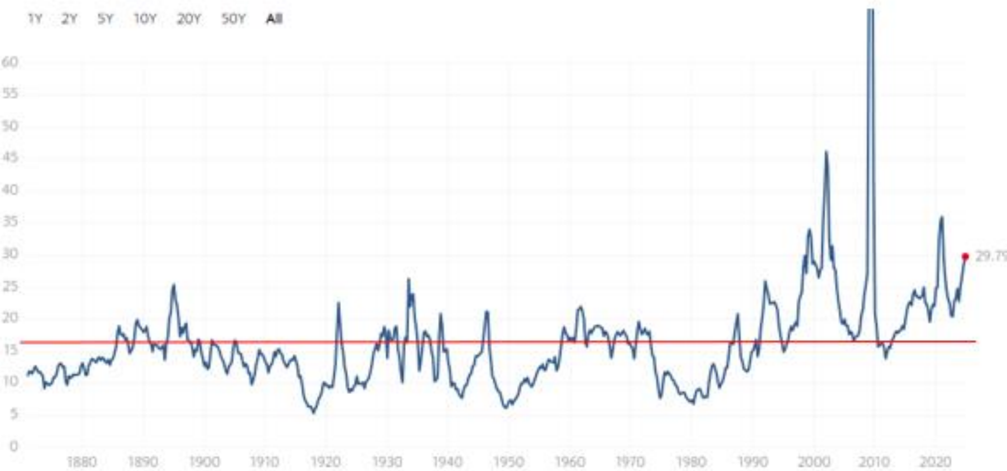
“ANTICIPATION”

November 2024

By Brahm Satov

On November 5th we have an election in the United States. At this time, it appears as if both Democrats and Republicans are anticipating a win. And the stock markets seem to also be anticipating a clear winner. I’m not so sure that we will have clarity immediately following the election, especially if it is close, as the polls anticipate. I cannot recall another time in history where Canadians were so concerned with a US election, perhaps rightly so, we shall see. Either way, uncertainty is usually not stock market friendly. “We can never know about the days to come, but we think about them anyway.” (Carly Simon, Anticipation) or as my mom used to say, “we don’t really know what tomorrow brings”, and that is why I like mathematics. We know that it makes sense to buy stocks when they are cheap and sell them when they are expensive. We also can learn from others that have risen before us and take heed to their advice: “Be Fearful When Others Are Greedy and Greedy When Others Are Fearful” (Warren Buffett).

The S&P500, (A U.S. stock market index tracking the stock performance of 500 of the largest companies) is trading at a price/earnings multiple of almost 30x, the mean is approximately 16x, by most metrics anything over 20x is deemed expensive. When the stock markets are trading at less than 15x, they are usually considered undervalued. Some have called this another bubble, the AI bubble, similar to the tech bubble or dot.com bubble. (P/E or price/earnings multiple, is price of a stock divided by earnings per share, in general the lower the P/E multiple the better the value).



Source: https://www.multpl.com/s-p-500-pe-ratio

While most investors are tempted to buy into the stock market euphoria, professional investors like Warren Buffett are raising record amounts of cash. According to Barron's, "Berkshire Hathaway has raised over $100 Billion this year and could be sitting on approximately $300B by year end". This could be that according to an indicator, aptly named, the Buffett Indicator, the current ratio of 209% which is 2.2 standard deviations above the historical trend line. In other words, the markets are expensive and overvalued, perhaps he is anticipating better value in the future.

Buffett Indicator

Source: A Sarna Offthecharts.substack.com

The more expensive the stock markets get, the lower the expected future return. This is just how the math of the stock markets work, all stock markets. We have seen a significant rise in the pricing of the US equity markets, but earnings have risen much more slowly, as such the P/E multiple has expanded, some have described this as a bubble. For those of us who have lived through bubbles before, we know that when they ultimately burst, it can be uncomfortable to say the least.

For many, it may seem like a tale of two economies, for the wealthy, they may be thinking, "what slowdown, I don't see it" but for those that do not fit into that category, they may be saying, "things have been tough for a while, given higher costs and that salaries have not kept pace, or their businesses have slowed". Some economists have called what they are seeing, pockets of weakness. I recall before the 2007 financial crises; economists were also calling it pockets of weakness. Given that most are anticipating a soft landing, I would remind readers about Bob Farrell's 10 market Rules (Bob was a legend on Wall Street, and a pioneer of technical analysis. He was the Chief Market Analyst at Merrill Lynch and well-known for his 10 market rules that never go out of fashion) and specifically, rule number 9, 'When all the experts and forecasts agree-something else is going to happen". Keep in mind that from my vantage point, the data is still not pointing to a soft landing and yet the markets have largely already priced it in, anticipation…

Thank you for taking the time to read this, please feel free to e-mail me any feedback or comments.

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