US equities still place to be for growth

But remember it was the eye of the storm that got us all into trouble to begin with.

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This month marks 11 years since the start of the global financial crisis (as marked by the collapse of Bear Stearns). Since then the US's bellwether S&P 500 index has annualised a total return of almost one third greater than any comparative sharemarket.

Ironically, being the eye of the 2009 storm, the US financial markets engine has demonstrated its ability not only to rock global financial stability but also stimulate it like no other centralised markets system in human history.

At its lowest point in March of 2009, the S&P 500 fell 57 per cent, touching an intra-day low of 666.

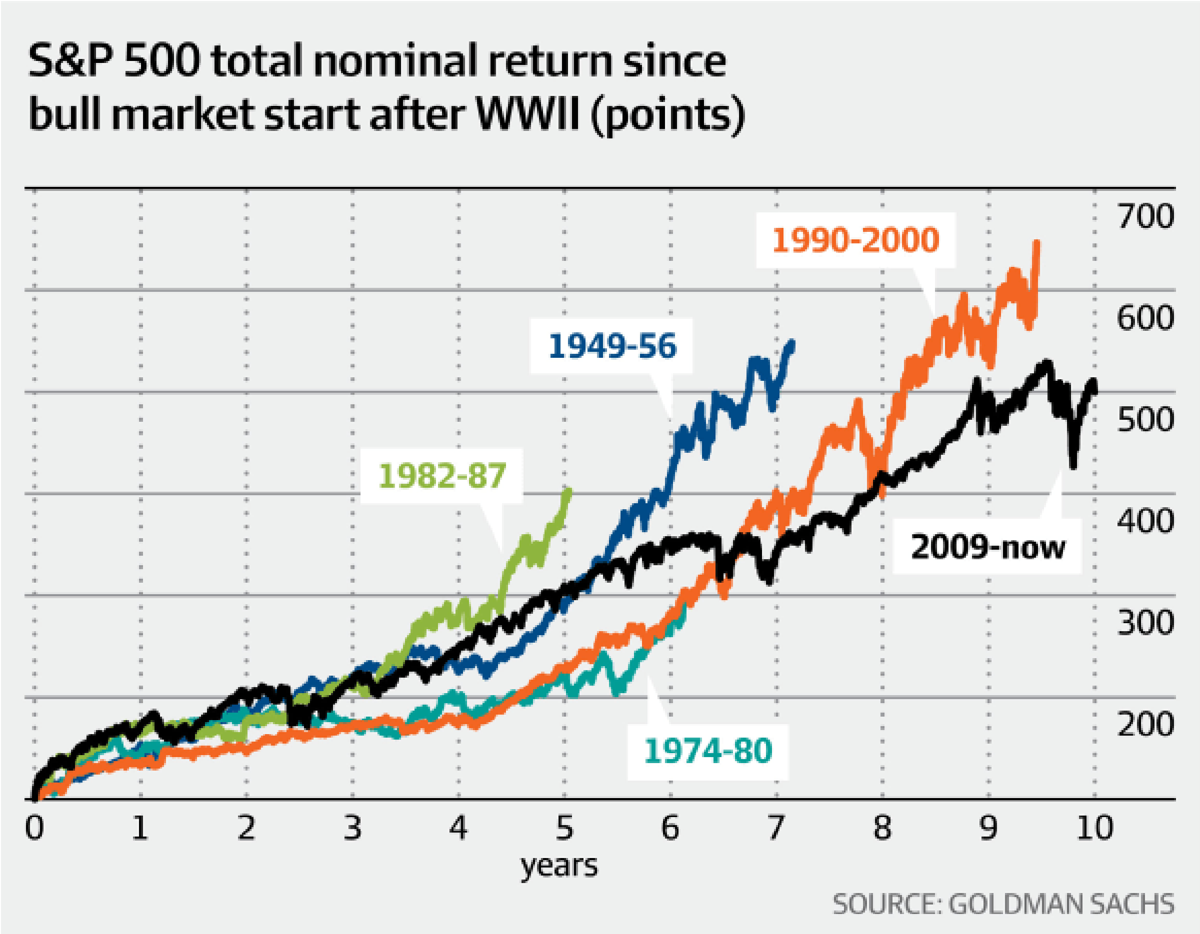
By contrast, in Europe, the bellwether pan-European exchange, the STOXX 600, fell 61 per cent but since then has recovered with an annualised 13 per cent. This has been driven largely by returns elevated by higher valuations, with much thanks going to the European Central Bank (ECB).

Comparatively the S&P 500, the strongest of the major global markets, has delivered an 11-year annualised total return of 18 per cent, three-quarters of which has come from earnings growth which is materially different than the European experience stoked by monetary stimulus alone.

US monetary policy tightening is over, at least for now. Although this is not much of a surprise, guidance from the Federal Open Market Committee (FOMC) is broadly positive for just about everything except US dollar hard cash and especially for US equities and real assets.

The strong returns in equity markets have come despite relatively weak economic activity, particularly in nominal terms.

But modest economic growth belies what has already been an unusually long economic cycle. Despite the growth concerns that dominated the fourth quarter of 2018, this US summer the economy entered its longest economic expansion for nearly 150 years.



Australian ultra high net worth global investors have been conditioned to read the proverbial tea leaves in patterns of sectors and not aggregates, as this typically flagged upswings and pullbacks throughout the roaring 1980s and mid to late 1990s.

As such, they've witnessed the S&P 500 up 12 per cent year-to-date and the industrial-heavy Russell 2000 index up 17 per cent. A look under the hood confirms this optimistic atmosphere, with cyclical sectors like industrials (up 20 per cent) and technology (up 15 per cent), leading the S&P 500 higher. The traditional safe havens of utilities and healthcare increased by only 6 per cent and 5 per cent respectively.

Corporate profits

But the irresistible US story goes beyond price action alone. Unlike Europe (or Australia for that matter), it is also apparent in US corporate profits.

Take the industrials sector, for instance. Changes in expectations for future earnings (earnings revisions) seem to have bottomed after collapsing in the second half of 2018.

It is hard to make a bearish case when one of the most cyclically levered sectors is experiencing positive revisions.

Of course, with the potential of valuations spiking suddenly, US corporate returns will be more dependent on earnings and dividend growth than at any time since the nadir of the GFC.

This would mark an important departure from the trend of the past decade, where returns have been driven more by an unusually large valuation expansion and less by earnings relative to previous cycles.

Since the GFC, the valuation component of US returns has been nearly 40 per cent for the world as a whole and roughly 30 per cent in the United States, where profit growth has been much stronger.

Concentration worry

Also – unlike previous cycles, which Australian UHNW global investors cut their teeth on – this post-crisis cycle has lead to just 10 US companies contributing half of the entire S&P 500's margin increases since April 2009.

Referred to in institutional circles as the "momentum" factor, this helps explain the catastrophic collapse of global multi-strategy hedge funds in the US spring of 2016 and the elevation of one US tech constituent, Apple Inc. [AAPL:US], also at the heart of the recent US-Sino trade fracas.

For Australian global investors, the FOMC's pause allows long-term holders to continue to reduce risk on strength, particularly in relatively accessible international markets such as the US.

The US equity market remains the place for investors to find fast-growing companies and buoyant listed valuations. But remember it was the eye of the storm that got us all into trouble to begin with.

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