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Six years of rising stock prices

Is the rally about to come to an end?

Prices on the stock markets have been going up since 2009. Such a long boom is rare. Will prices see an adjustment in 2016? Three experts tell us what they think.

teleboerse.de: The Dax rose by a further eight percent this year. Will it start to get dizzy at such heights, or can we look forward to another good year for shares in 2016?

Carsten Riehemann: We think that share prospects will remain favourable in 2016. The global economy is growing - albeit reticently - and interest rates are staying low. But investors need active management both when selecting individual titles and for share quota risk management. For us, one thing is clear: The fluctuations on the stock markets will stay, and might get even stronger.

Carsten Riehemann is Managing Shareholder at Vermögensverwaltung Albrecht, Kitta & Co.

Thomas Wukonigg: I take a similar view. Volatility is likely to increase. Nevertheless, in 2016, stock markets might rise to last year's peaks. We estimate the bandwidth of the Dax to be between 9,200 and 12,300 points.

Thomas Wukonigg is e.g. responsible for portfolio management at Capital-Forum AG.

Uwe Günther: I disagree. 2016 is unlikely to be a good year for shares. The macroeconomic, valuation-related and political burdens are simply too numerous and significant for this to be possible. For instance, I think that the US market has an adjustment potential of significantly more than 20 percent. The Dax will also not get away entirely unscathed. We've seen this for six months now.

Uwe Günther is founding member and Managing Director of BPM - Berlin Portfolio Management GmbH. **www.berlin-pm.com**

The current VDax New implies significant, including negative, fluctuations. Where do you identify the possible slump?

Günther: We are already in an orientation phase for the new market valuation. We should not be fooled by the still high dividend returns and already significantly lower price-to-book value ratios. The lower investment and consumption rates across the world will put significant pressure on company profits.

Wukonigg: As I said: We believe that the Dax could fall down to 9,200 points. But the dividend return of three percent should have a dampening effect on the downward momentum.

Riehemann: We stopped long ago trying to fathom precisely what indexes will do in a year or at a specific point in time. Experience has shown that they will perform entirely differently anyway. For us, what is happening at this moment matters, especially as regards shares. We are currently assuming growing stock markets.

The higher rates in 2015 were driven primarily by expansive monetary policy. The Fed has now changed to increasing interest rates and the ECB most recently disappointed the markets because it did not stock up its bond purchases. Will cheap federal bank money no longer be around to drive prices in 2016?

Günther: The markets are undoubtedly experiencing what I call a "fake high". This was more than apparent based on the market reaction at the last ECB meeting. Unfortunately, a large part of share profits and returns are based on this very federal bank policy and on unsecured federal bank loans - not on higher revenues and company earnings.

Wukonigg: In Japan, China and the Eurozone, the federal banks will only be able to act as a driver again if they purchase additional bonds at a large scale. In the USA, the markets are expecting the Fed to take several steps regarding interest rates. If these are not taken because economic development stagnates, this could be a positive surprise for the markets.

Riehemann: What will keep is most busy is the fact that international monetary policy seems to be drifting apart. This will mean great potential for fluctuations: not only on stock and annuity markets, but also on foreign exchange markets.

What about the economy? The USA are already far advanced in their cycle and China is basically a huge question mark. Only Europe is speeding up. Will this be enough for the world economy to continue to grow?

Riehemann: In addition to Europe, we can especially expect China and other emerging economy to surprise us positively so that the global economy should continue to grow, albeit at moderate speed.

Wukonigg: I also think that estimates for China are likely to be too negative. Emerging economies like India, Argentina or Venezuela will also be able to provide positive impulses. The political atmosphere there is moving towards a greater market economy. In addition, there is the possibility that the sanctions against Iran and Russia might be lifted, since the latter is fighting against IS on the side of the West by now.

Günther: I see this very differently. The overall global real growth rates are likely to be disappointing. 2009 saw the weakest upturn since the War. And this was only carried by the historically unique measures taken by the federal banks. I don't currently see where an organic, sustainable further upturn would come from.

If company profits fail to increase further, all that is left is to increase the valuation for higher prices. Can we expect higher P/E ratios in 2016?

Riehemann: We definitely see potential for higher company profits - especially in Europe. Currently, social media are revolutionising the technology sector. In the pharma industry, new biotechnology companies are creating entirely new treatment methods. Robotics are also opening up entirely new opportunities for many companies. That suggests greater potential for profits. So P/E ratios need not necessarily go up further.

Wukonigg: Our interpretations are based around the idea of a higher valuation. As soon as there are fewer uncertainties again, investors will increasingly realise that there is no real alternative to shares. This will result in additional capital and higher valuations.

Günther: We have seen an increase in P/E ratios since at least 2012. In our opinion, prices - driven by the federal banks - might well show a greater increase than earnings. Since institutional investors have been shedding risky assets since February, prices are driven primarily by smaller investors and the federal banks.

Various voices have been heard to say that most recently, prices have only been driven by risk capital. Experience has shown that this is likely to be highly elusive, as become apparent at the start of December.

Wukonigg: It wasn't only loan-financed risky capital that entered the markets. Most recently, we above all saw the withdrawal of the petrodollar. Even the Norwegian federal fund supposedly reduced its share holding. When interest rates fall to a historic low, there is no alternative to shares.

Riehemann: We think that a lot generally depends on the investor's mindsets. That's largely because there is basically no more interest. In order to achieve positive returns at all, investors nowadays must use significant risky capital.

In addition to economic and valuation, there are also fundamental risks such as war with IS terrorists. Since the start of the noughties, there has been a crash every four years: 2000-2003, 2008-2009 and 2011. Are the stock markets gearing up for another crash in 2016?

Riehemann: Of course, geopolitical risks or other exogeneous shocks can create a crash on the currently nervous markets at any time. In the worst case, we will remove the risks from customer portfolios completely.

Wukonigg: There will be seven elections in Europe this year. Taken together with the possibility of Britain leaving the EU, this could result in lots of fluctuations and possibly severe setbacks for a time. But an actual crash is unlikely because valuation levels aren't very high.

Günther: Statistics by themselves are unlikely to be helpful, even though they are interesting. The main thing is to clearly distinguish between causes and triggers. For instance, a strong global economy based on stable finances is much less likely to be impacted by terrorist acts or natural disasters than an economic based on a giant debt bubble and flagging. Unfortunately, the latter is the case at the moment.

Bonds have become an interest rate risk and commodities such as gold have been disappointing for years. Is there no alternative to shares, in spite of all the risks?

Wukonigg: Definitely. But investors must diversify as widely as possible. Setbacks for individual stock can be vast by now. As was demonstrated most recently by Leoni, VW or Osram.

Günther: In the context of extremely low inflation, it can make more sense to hold good short-term bonds for a time, and in a crash, they might even stand up to risk comparisons relatively speaking. There is always an alternative.

Riehemann: We have added the investment class Total Return Investments to our portfolio management. This is able to generate positive earnings without the need for the stock and annuity markets to grow per se.

Crashes are most frequently triggered by so-called black swans, meaning unforeseeable events. What could be a black swan this year?

Riehemann: We find it difficult to speculate about black swans simply because, based on their definition, they are necessarily not yet known.

Wukonigg: There are several potential crises which could shake the financial markets in 2016: Too many interest rate steps in the USA, and a political move to the right because of the migrant crisis in Europe, i.e. the Front National, AFD, The True Finns, etc., and possibly Donald Trump as US president, could intensify geopolitical tensions. But strictly speaking, these aren't really black swans.

Günther: That's impossible to forecast. And if I could forecast it, it would cease to be a black swan!

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