A Look At All-Time Highs (Other Than The S&P 500)
Don's Blog 2017.12.12

Chart 1 below is the all-time high to which one should be paying attention. It is named the Margin-adjusted CAPE by John Hussman. It builds on the work done by Robert Shiller which smooths earnings growth over a 10-year moving average basis, by adjusting for profit margins, which—like earnings—are cyclical. Nothings is fool-proof, however, in my opinion this is the single best indication of a market's valuation. It is at an all-time high. It could go higher, which it has already. However, at these levels, it's difficult to see how one can obtain anything close to "normal" annual returns of 8 to 10%. Based on historical numbers, 10-year annual returns should be -2%. Please also note chart 2 below, which is quite busy, but indicates both stocks and bonds are at extremely high valuations.

With the above in mind, let's take a look at the balance sheet, which is very important but not generally thought of when valuing a company, such as seen above. It's earnings, earnings, earnings. Profit and loss, not balance sheet. During the third quarter of 2017, total system borrowings expanded $1 trillion (non-financial debt). Total debt at 09/30/2017 was $68 trillion. This also is a new record. Of course, on the other hand, things such as household net worth expanded nicely. On 09/30/2017 this number was a record $97 trillion. So, what's to worry about? Debt is fixed, stocks and bond valuations are not. Plus, the fact that when things go south, creditors become bad partners. Household net-worth is now 498% of GDP, surpassing 378% in the first quarter of 2009, 478% the first quarter of 2007, and 435% the fourth quarter of 2009.

One last item: how is that health care system working for you? Please note charts 3 and 4. It is obvious the government is doing to our healthcare system exactly what it did to education. Do all these kinds of things lead one to value financial assets at all-time highs?

Chart 1

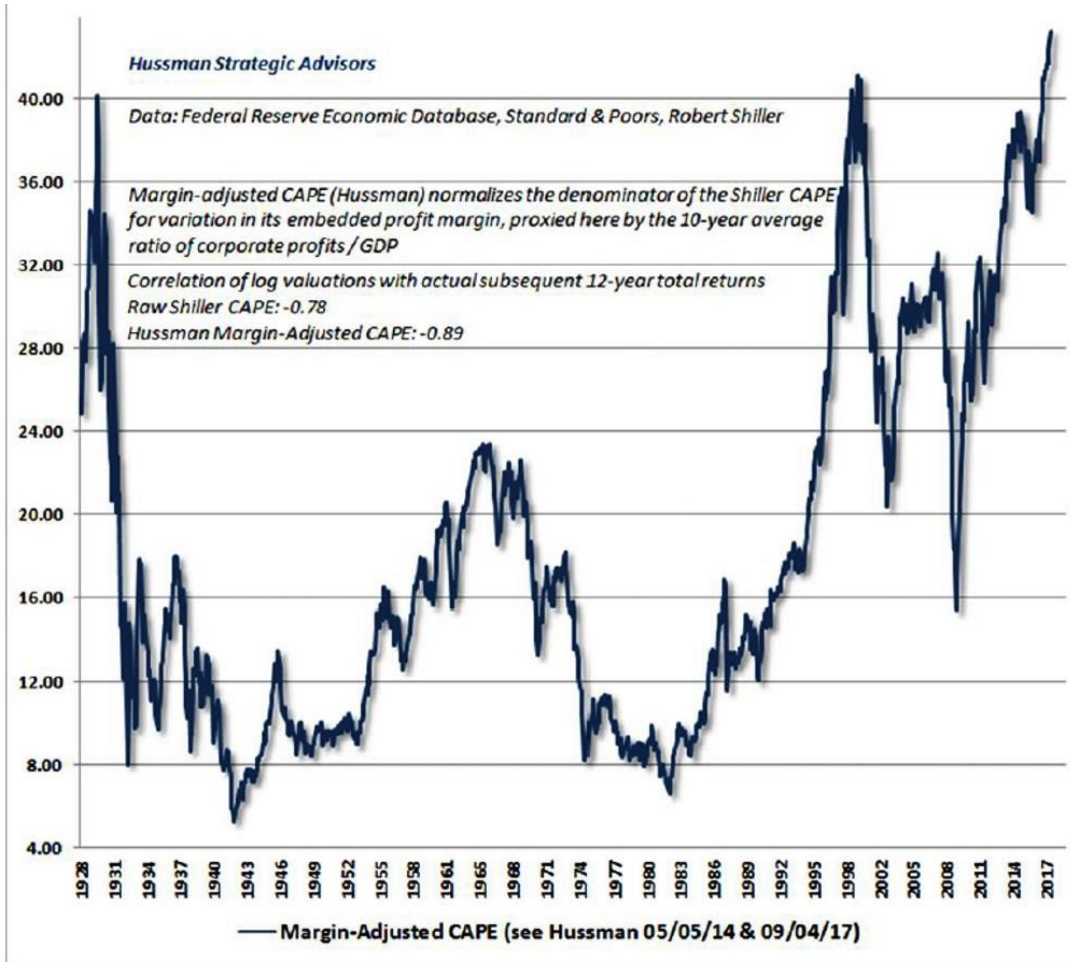
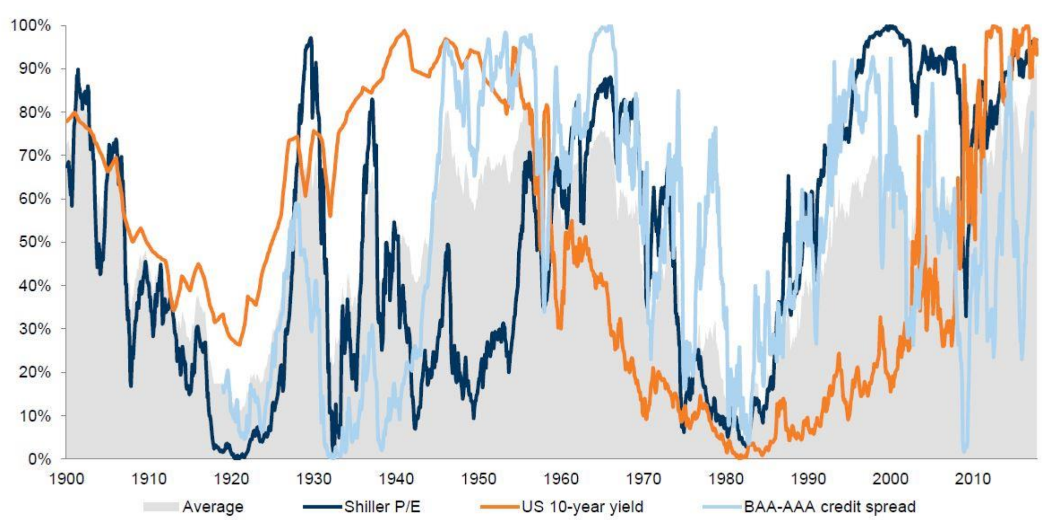


Chart 2

Exhibit 12: Valuation frustration - both bonds and equities appear expensive
Valuation percentile (since 1871 for S&P 500 & US 10-year yields, 1919 for BAA spreads)



Source: Shiller, Goldman Sachs Global Investment Research

Chart 3

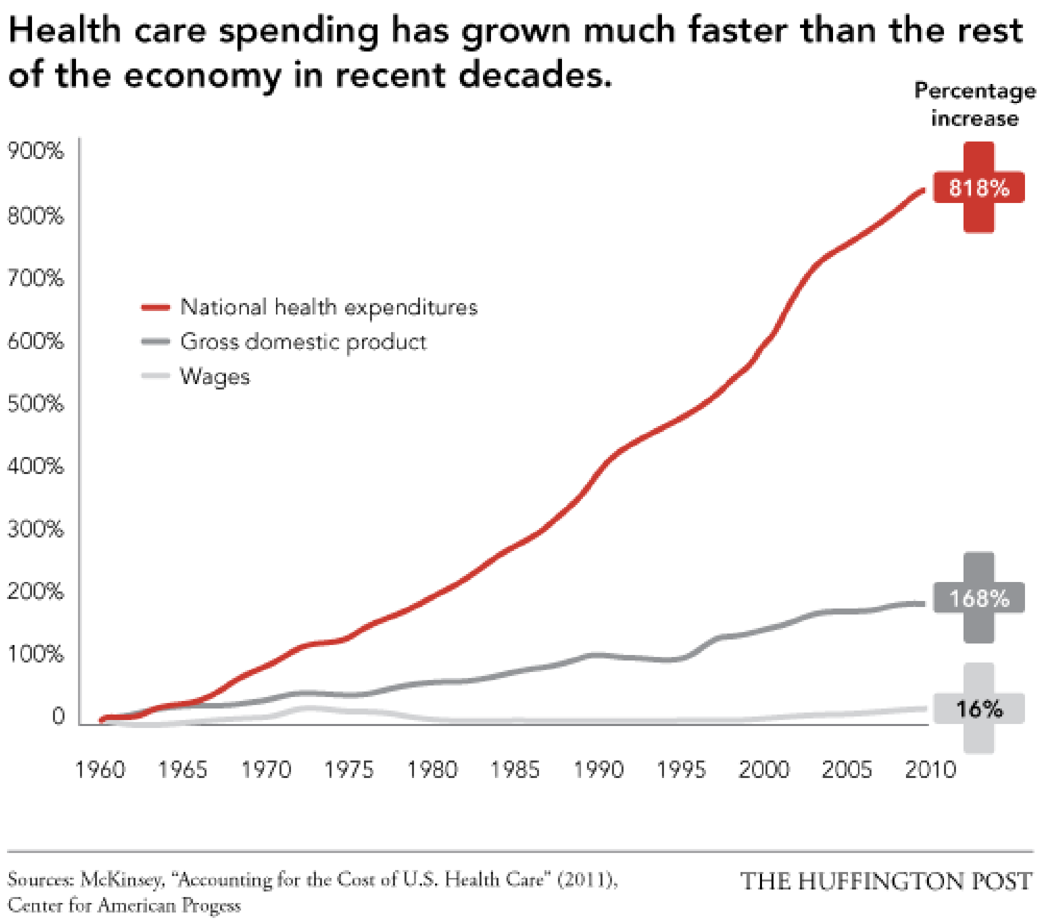


Chart 4