Forbe's Magazine's Portfolio Strategy columnist and Fisher Investments chief executive Ken Fisher dismisses the naysayers and explains why he believes US stocks will rise 7% – and maybe much more – annually over the next decade

Stocks will just keep rising

Where will the S&P 500 index be 10 years from now? First, no one knows. Second it's important because the US is half the world's stockmarket – its vector impacts everyone else. Third, as you've read, pundits commonly speculate a 0% return this decade. My guess? US stocks will exceed 7% annually through 2014. Maybe much more. Why?

As I say, no one knows where stocks will be 10 years from now. Those who tell you they do are saying more about what they don't know about markets than what they do know. Prices derive from supply and demand for equities – something we don't like to think about.

Our information processors came from our far-distant ancestors and work like theirs did. We contemplate earnings, interest rates, politics, valuations and the like (instead of supply and demand), the way they thought about wind, rain, lightening and the neighbouring tribes when contemplating the hunt. No one among us wakes daily gleeful to contemplate another opportunity to envisage supply and demand for equities.

This is critical but understood very little – demand is more powerful than supply in setting short-term pricing but, long term, supply is almost infinitely more forceful on prices. Supply is constrained in the short term by the regulatory gauntlet through which it must pass. Demand flows freely being solely our eagerness to own or not own stocks.

But, in the long term, supply vacillates infinitely to overcome variances in raw capital costs between varying equity categories. Another way to say that is, correctly calculated, all major equity categories have similar long-term returns where their small differences are random.

To envisage supply, contemplate the US. In the last two decades stocks returned 15% a year. But the US's stocks grew in value by 10% more. How can that be? The difference is newly-created stock. Had there been less stock created, existing ones would have returned more. Had there been more new stock, returns would have been lower.

The problem is, we have no capital markets know-how today allowing us now to foresee supply shifts for securities seven to 10 years out and yet that is what drives where returns will end the decade. This is why anyone who tells you where stocks will be then is telling you what they don't know. I cite my September 2003 column on why academic attempts at calculating an "equity risk premium" are less than useful for forecasting.

Why then do I guess stocks may exceed 7% annually? Ultimately, stocks compete for capital against bonds. The bonds they compete against are low-grade corporates. Think of where both sit on a balance sheet – next to each other because they belong together.

Then, envisage the US's Baa corporate bond rate at any point in history. Look at stocks then over the next 10 years. Stocks have beaten the initial Baa rate in more than 75% of all rolling 10-year periods in history and the times they didn't were mostly long ago.

The last? The 10 years starting 1981 with the Baa rate at 16.75%. But if you went to 1980 or 1982 stocks won. Some 10-year periods stocks won by a little. Others by a lot. But they won most times because in theory they should have. Having had a long global bear market from early 2000 through to 2002, my guess is we are not now in a period where bonds win. Hence I am about 75% certain stocks beat the current 6.2% Baa rate by at least a little.

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I'm more certain 2004 is a happy year. So buy stocks like Dutch-based insurer Aegon, a good firm yet relatively cheap compared to global peers at 10 times 2004 earnings. With cyclical winds behind it the group should surprise favourably.

Canada's Masonite Corporation offers clever opportunities in luxury consumer durables in an expansion. Masonite is the world's leader in residential front doors, which research shows do well in a sustained housing boom. People's egos are in their doors.

Finally, the same cyclical trend will help gaming stocks and two that have lagged their peers in the market but lead in the real world are the US's Caesar's Entertainment and Harrah's Entertainment. Between the two you've pretty well covered your gambling bets.

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