



Portfolio strategy: Ken Fisher

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continues to see beauty in the current market and notes that things are changing from bearish to bullish

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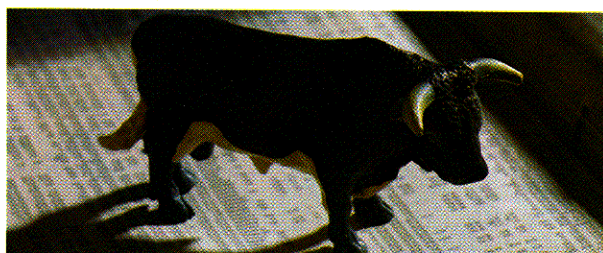
All the unrecognised beauty is very bullish

Last month I listed six ways in which this world is more beautiful than any you will see for a very, very long time. Let me continue to count the ways I see beauty in a world where most folks see grey.

Number seven – as the market rises, short-selling hits steady and all-time records, in dollars or percentages. Particularly impressive is that short-selling rises as the market does, which is evidence that the rally is seen with increased scepticism – exactly how a new bull market is supposed to operate. Every one of those short sales must eventually be bought back. Short-selling depresses prices now, borrowing future demand for stocks that must be repaid – and enhancing future returns. And that is beautiful.

Eighth, a little-noted shift is that insider transactions swung wildly from bearish to bullish. Throughout the bear market, corporate insiders sold about four shares for every one they bought. Normally, they sell about two shares for every one they buy. Starting in July they started buying two for every one they sold. Big shift. Rare. Very bullish. Very beautiful.

Ninth, in July US mutual fund outflows hit all-time records – a classic bear market bottom symptom, classic capitulation. They pulled \$50bn (£32bn) out of equity funds, representing 1.7% of total fund values. That is the second-biggest month ever, only surpassed in October 1987. But the three-month total to that point, of 2.5%, is an all-time three-month record. All-time records are beautiful.



Tenth, long bond prices rise. In early bull markets, long bonds must do well. It is the fertile soil from which the bull market seed grows. Think it through. Most folks wrongly fret over the market's price/earnings ratio (P/E) which, as I detailed in August, isn't productive in predicting market direction. You're not even supposed to think about price/earnings ratios. In finance theory, you're to invert the P/E into an E/P, known as the earnings yield, an interest rate-like percentage comparable to interest rates.


A P/E of 12, for example, is an E/P of one divided by 12 or 8.3%, comparing nicely to fixed income alternatives, particularly if earnings rise in the next decade whereas bond returns stay fixed. Remember, the market discounts the future earnings stream of businesses against interest rates – that's its job. The long-term earnings from owning businesses must compete in the long term with the income stream from long-term bonds. Hence, when bond prices rise and long-term rates fall, the hurdle against which business ownership must compete just fell. Again, beautiful.

Also of course, old pricing is beautiful. Boise Cascade sells right where it

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did in the late-1980s. This leading US paper and forest products firm owns 2.4 million acres of land worth, on average, about \$1,300 per acre. Its land alone, less all corporate liabilities, has a residual value of \$21 per share. If the stock is \$27, you pay only \$6 more per share or \$325m for profitable operations with \$7.3bn of annual revenue. It's market capitalisation is only 20% of annual revenue and it pays a 2.2% dividend yield. Dirt cheap.

Borders Group is America's number one shopping mall book retailer. In the 1990s dot.com frenzy, folks fretted "clicks" would be the end of "bricks", particularly with successes like Amazon. Hence, Borders' stock languished. Then, too, the economic downturn stalled growth. But the prime lessons of recent years include that clicks and bricks largely go together. Borders' position remains strong and, as the economy picks up, so will Borders' growth. The stock is cheap too at 50% of annual revenue, 14 times earnings and five times cashflow.

As the market rises so will the major brokers and investment banks. Well-situated is powerhouse Credit Suisse. The non-US market, as I mentioned last month, best depicted by Morgan Stanley's EAFE index, sells at 1989 prices in dollars, sterling or local currency. It is here that Credit Suisse is particularly strong. And very cheap. It sells at exactly book value, 50% of annual revenue, eight times earnings and has a hefty 5% dividend yield. Hard to beat that. 

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