



MELLON ON THE MARKETS

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By Jim Mellon

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Happy New Year to all you Master Investors out there! The start of the New Year has been good for those of us fundamentally worried about stretched valuations and a cloudy outlook.

China's ructions have caused some steep falls in most markets. It is worth noting that if January is a down month, typically the rest of the year is also down. Now that is a little bit of hocus pocus of course, because superstitious analysis of historical data is not a way to wealth. Except sometimes these sorts of predictions are self-fulfilling.

Most importantly, **there isn't any particular reason that most markets should rise, but there are plenty of reasons to suggest that they should fall or tread water.** The most important of these are: a) in Europe and the US, there is likely to be a deceleration or even fall (in the US) in earnings; b) this leaves valuations at stretched levels on any measure that you care to apply; c) dividends will come under pressure as companies, particularly in energy and mining, find debt service levels untenable (which is already happening in some cases); and d) currency volatility will cause earnings surprises on the downside to be exaggerated.

Last year worked out pretty well for us. The Swiss Franc (two tea bags) fell, the Euro fell, then rallied, the yen was neutral, Japan was up about 13%, the US market fell by 1% (with almost all of its gains concentrated in a few tech stocks, and 490 stocks in the S&P 500 falling), and the FTSE fell by about 8%. European stock gains were wiped out by the fall in the currency.

So far, so good. Gold and silver weren't great, but the call to generally avoid emerging markets worked.

Now, for 2016 here are my predictions:

1. The US market falls further. Perhaps 5-10%. The crazy valuations of tech IPOs meet their day of reckoning. Some large biotechs that got beaten up in the last year, like Gilead or Biogen, recover sharply, but most biotech is blah. Agriculture stocks do well (think John Deere, Monsanto and Syngenta) as agricultural prices recover.
2. The UK does OK, as sterling falls somewhat against the dollar and further against the Euro.
3. The Italian and French debt crises-in-the-making become apparent to a wider audience than me. And yields on all Euro bonds go up – i.e. prices go down.
4. European stocks tread water.

5. Japan, spurred by rising ROE, buybacks and improved corporate governance, continues to be the world's best performing market. Nikkei has 22,000 at least written on it. My picks include Fanuc, Hitachi, Mitsubishi Heavy and Honda.
6. China produces a modest positive return.
7. Vietnam is the world's best performing market, followed by Argentina and Brazil.
8. Russia continues to disappoint.
9. Africa stalls further and the idea of a growth miracle is debunked.
10. US treasury yields on 10 year bonds rise to 2.7%.
11. The Swiss franc falls further.
12. The Japanese yen strengthens to 110 -115 against the US dollar.
13. The AUD falls to 69 cents (I am resuming my bearish tack here).
14. The CAD rises to 1.29 against the US; the SEK is a buy (Swedish Krone).
15. Hilary Clinton wins the US election.
16. Brexit is close, but the muppets will vote to stay in (a very stupid move in my view!).
17. Gold and silver will outperform.
18. My favourite big company stocks that I can talk about, apart from the ones above, will be Rio, Peugeot, Amgen, and the JNUG ETF.
19. 12,000 people will register for the greatest investment show on earth, Master Investor on 23rd April 2016.
20. There will be a move to bail-in failing banks in the Eurozone – Portugal first, then Italy. This will dent Europe's economic recovery.
21. The migrant crisis will result in an effective closing of borders (destruction of Schengen).
22. Saudi Arabia will move closer to bankruptcy.
23. Corn, copper and lithium will be the best non-precious commodities to invest in. Iron ore will be flat.
24. Merkel will be ousted.
25. The Queen will abdicate.

So there you have it. And of course, I will be back with a lot of new forecasts/recommendations at the Master Investor show. I really hope you get your tickets early; there has been overwhelming demand for them – and I would love to see everyone there.

Happy Hunting!!

Jim Mellon

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