EQUITY

US Equity Market: Are Things as Good as They'll Get?

November 01, 2018

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The US equity market's ascent paused in October as investors digested rising rates, slowing global growth and the persistent question: "Are things as good as they'll get?" As many observers expect further turbulence ahead, Franklin Equity Group's Grant Bowers shares his view on US equities, the economy, and how to stay focused on long-term investing in a volatile market.

The US bull market continues to confound fears of its demise.

While we've seen some wobbles in October, we don't see a reason to believe the market will be thrown off course. But the longer the bull run lasts, the more investors are asking: "Are things as good as they'll get?"

Two Pillars for Optimism

On a macro level, we remain optimistic in our US market outlook. Looking at what drives US companies and the economy in general, we see two main pillars: corporations and consumers. Both remain healthy, in our view.

US corporations continue to generate earnings growth rates above global peers, while domestically, unemployment is low, consumer confidence is high, and wages are starting to increase. We don't see the selloff in equities at the end of October as being a precursor to a larger economic recession but more of a recalibration as the market assesses the changing global landscape.

With the recent selloff, valuations have come down and, in our view, are at a level that accurately reflects the investment environment. Strong earnings, coupled with the pricing pullback earlier this year, suggests to us that things don't look too bad on a price-to-earnings ratio.[1]

US economic growth, profit margins and stock returns are still well above global peers.

Inflation is creeping up in the United States, but appears relatively anchored. Growth has been robust but not too fast. In our view, there are no signs of the credit imbalances or excesses that often lead to overheating.

How We Approach the Ageing Bull Market

For us, investing in an ageing bull market like we are in today isn't that much different than any other time. We remain focused on building a portfolio of stocks that we believe should be poised to benefit from multi-year secular growth themes or innovation.

We take a long-term view and leverage our bottom-up research to identify businesses that have dominant brands or franchises with high-quality management teams and healthy financial returns.

Consequently, our analysis encompasses more than just the current cycle; we consider a potential investment's outlook for the next 5-10 years.

As long-term investors, we are always trying to block out the short-term market noise and identify sectors and companies that are benefitting from large multi-year growth trends.

We look for secular growth stories that are disrupting incumbent businesses and are addressing the major needs of tomorrow.

Seeking Out Disruption and Innovation

We really want to hone in on the changes that are occurring today that will impact the world tomorrow. Often these growth trends are driven by disruptive technologies, innovation, changing consumer habits or demographic shifts.

This includes things like demographics, digitisation—including e-commerce and the cloud—as well as artificial intelligence.

There is likely to be a tremendous amount of change taking place in the technology and health care sectors in particular over the next few years.

Our Positive Outlook for Technology and Health Care

In the technology sector, the outlook for spending remains strong as many companies have realised that investments in technology improvements are required to remain competitive in the global marketplace.

New software, factory automation and data analytics can all improve productivity and lower the cost of production for companies, keeping them ahead of their competitors.

Cybersecurity, software as a service (SaaS), cloud computing, digital payments, mobility and smart devices are just some of the technological areas that have sparked our interest.

Similarly, we continue to look favourably on the long-term outlook for the health care sector. We expect an ageing population globally to drive increased consumption of health care services and demand for improved treatments and cures.

This demographic tailwind, combined with innovation in drug development and medical technology, is creating numerous potential investment opportunities as well.

Overall, our long-term outlook for both technology and health care companies remains positive. While both sectors have traditionally experienced bouts of short-term volatility, those have often created attractive buying opportunities for many investors.

To hear more from Grant Bowers on the US market, including his thoughts on the three biggest risks and the growth versus value debate, check out this episode of our Talking Markets podcast.

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What Are the Risks?

All investments involve risks, including possible loss of principal. The value of investments can go down as well as up, and investors may not get back the full amount invested. Stock prices fluctuate, sometimes rapidly and dramatically, due to factors affecting individual companies, particular industries or sectors, or general market conditions. Investing in fast-growing industries, including the technology sector (which has historically been volatile) could result in increased price fluctuation, especially over the short term, due to the rapid pace of product change and development and changes in government regulation of companies emphasizing scientific or technological advancement. Value securities may not increase in price as anticipated or may decline further in value. Growth stock prices reflect projections of future earnings or revenues, and can, therefore, fall dramatically if the company fails to meet those projections.

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1. The price-earnings (P/E) ratio is a valuation multiple defined as market price per share divided by annual earnings per share (EPS).

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