"History doesn't repeat itself, but it often rhymes"…

There is no substantive evidence that the above quote was made by Mark Twain, but he did write a far more eloquent observation in a novel, entitled "The Gilded Age: A Tale of To-Day", he co-wrote in 1874;

History never repeats itself, but the kaleidoscopic combinations of the pictured present often seem to be constructed out of the broken fragments of antique legends.

Piecing through the ever more complex and voluminous data 140 years on is it still possible to get a hint of the future from fragments of the past; antique or otherwise. In the 21st Century investment cycles seem to come around faster than Lewis Hamilton. In the first 14 years we have had significant market peaks in 2000, 2007 and quite possibly 2014. Prior to that you have to go back firstly to 1987 and then 1974 then 1929. Things are speeding up!

But are we near a peak right now? I am indebted to the Elliot Wave Theorist (www.elliottwave.com) for some of the following clues. We have had something of a selloff in mid and small cap stocks already, both here and in the US. The Russell 2000 index of small cap shares saw its closing high back in March as did the FTSE 250 and Small Cap indices suggesting a meaningful switch from risk on to risk off, a pattern that occurred in 2007.

High yield debt (I still prefer the term "junk bonds") are starting to pull back from historically low yields. The Junk/Treasury price ratio is down more than 11% since its December 31st 2013 peak. The last time this ratio was down more than 11% while the S&P 500 was at an all-time high was in July 2007 and we know what happened in the bond markets after that…

A move out of riskier mid and small caps and perhaps a realisation that high yield is in fact junk is a warning sign that, at the very least, markets have got ahead of themselves. That this is a contrary opinion is something of an understatement as I am continually reminded! Bullish sentiment is rife. "Fund managers are aggressively positioning for a second half upturn in the global economy," says Market Watch. Citing the recent 51 day span without a single move of more than 1% one pundit suggested that the S&P is not over extended and may never pull back!

The yield on the Dow (2.09%) is now down to levels last seen in 2007 (2.06%). During the ensuing slump yields climbed to close on 5%. In 1929 the market peaked on a yield of 2.83%. Another valuation measure, Tobin's Q ratio divides the market value of corporate assets by their replacement costs. It is currently standing at the second highest extreme topped only by the TMT frenzy in 2000.

We also have an example of "tulip bulb mania" in the form of a stock with the appropriate name of CYNK Technology. It had no assets, no earnings, no revenue and a business plan based on the idea that "people should, and will, pay to get in touch with people." It jumped over 36,000% from a low of 6 cents to a high of $21.95 before crashing back to earth; all during the course of July this year. Tulip bulb mania in the 1630s managed gains of a mere 2880% for the "rare" Switzer varieties.

Previous peaks in 1929, 2000 and 2007 have seen a spike in the number of stories about income and wealth inequality, as markets inexorably rise and the rich get richer…And here in April Thomas Picketty launched his book "Capital in the 21st Century" all about…wealth inequality. Another market peak indicator is the increasing concern about bubble conditions. Janet Yellen at Yellen Capital – the new nickname for the Fed given that its burgeoning holdings of US Treasuries make it the world's biggest hedge fund - doesn't believe that the price / equity ratio (she probably meant price / earnings but then she is a theoretical economist…) is high, although she did say that certain biotech and social media stocks were overvalued. One is tempted to ask what she was twittering on about…and it seems that I just have…oh dear.

And finally now that he has moved on former Chairman Bernanke has suggested that "It's entirely possible that if you look at the world, you have slow growing advanced economies and that the rate of return is just going to be low." Well you certainly engineered a low rate for savers forcing them into just the kind of riskier assets that are now beginning to peak didn't you?

Mind out below…

Clive Hale –The View from the Bridge – August 3rd 2014

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