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Obama Stock Advance Persists on Money Fund Hoarding (Update3)

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By Lynn Thomasson and Michael Tsang



Sept. 28 (Bloomberg) -- Americans holding \$3.5 trillion in **cash** are giving money managers increasing confidence that the stock market rally under President **Barack Obama** will continue through the end of the year.

Even after reducing money-market accounts by 11 percent this year, investors have cash equal to 73 percent of **Standard & Poor's 500 Index** companies' **net assets**, according to data compiled by the Investment Company Institute and Bloomberg. At the peak of the bull market in 2007, the measure of buying power was 62 percent.

The S&P 500 has climbed 57 percent since March 9 as the U.S. government and Federal Reserve lent, spent or guaranteed \$11.6 trillion and the central bank held interest rates near zero to fight the longest recession in seven decades. Now, the benchmark gauge for U.S. equities may extend the advance as investors who kept their money in cash become convinced the gains will last, said **Jack Ablin**, who helps oversee \$60 billion as chief investment officer at Harris Private Bank in Chicago.

"There's an enormous stockpile of liquidity on the sidelines," Ablin said in a telephone interview on Sept. 23. "The reinvestment of cash could help fuel the market."

No new president since **Franklin Roosevelt** has seen a bigger rally than Obama. The S&P 500 climbed 32 percent since he was sworn in as economists lifted estimates for third-quarter growth almost sixfold to 2.9 percent. Forecasts for next year's gross domestic product rose to 2.4 percent from an average estimate of 2.1 percent on Inauguration Day, according to Bloomberg data.

Saving Money

Investors placed \$1.45 trillion in U.S. money-market funds in **2007 and 2008** during the worst financial crisis since the Great Depression, based on data from Washington-based ICI. The amount has dropped \$439.5 billion since reaching a record \$3.92 trillion in the week ended Jan. 14.

A broader measure of **reserves** that includes cash, bank deposits and money-market funds has climbed to \$9.55 trillion this month, based on data compiled by the Fed. That's enough to buy all of the companies in the **S&P 500**, which have a combined market value of \$9.39 trillion, Bloomberg data show. Since 1999, so-called money at zero maturity has on average accounted for 62 percent of the stock index's worth.

"There is a wall of cash," said **Yves Carpentier**, a Paris-based manager at Cap West, who oversees \$118 million in three U.S. stock funds that have gained more than 32 percent this year, beating at least 87 percent of their competitors. "Stocks will be the investment of choice in the coming months."

Never Before

The S&P 500 plunged 38 percent last year, the biggest drop since 1937, as crashing real-estate prices spurred \$1.6 trillion in writedowns and credit losses at global financial companies and led to the most bank failures since the savings-and-loan crisis of the early 1990s. Before the collapse of

New York-based Lehman Brothers Holdings Inc. last year, the amount of cash never exceeded the value of U.S. equities.

The S&P 500 rose 1.8 percent today, the most in five weeks, as takeovers in the drug and technology industries added to evidence that mergers and acquisitions are rebounding from the slowest pace in six years.

Stocks rebounded this year, trimming the S&P 500's decline since its Oct. 9, 2007, record to 32 percent, as the U.S. government pumped cash into the country's largest lenders and the economy stabilized. More than 72 percent of S&P 500 companies **beat** analysts' second-quarter earnings estimates.

Stock Inflows

Investors are returning to stocks faster than in the last bull market. They've added \$15.8 billion to domestic-equity funds since March, compared with outflows of \$18.6 billion during the first five months of the bull market that began in October 2002, data from ICI shows.

Should inflation exceed returns on money-market accounts, that may cause more investors to buy equities. The 100 largest taxable U.S. funds returned an annualized 0.12 percent during the past week, according to **data** compiled by Westborough, Massachusetts-based Crane Data LLC.

The Fed said on Sept. 23 that it anticipates keeping the benchmark interest **rate** "exceptionally low" for an "extended time." Labor Department reports this month showed prices of goods imported into the U.S. **tumbled** 15 percent in August from a year earlier and consumer prices dropped 1.5 percent.

"Many of the fund managers I talk to that have missed this rally or underplayed this rally are sitting with way too much cash," said **Jeffrey Saut**, chief investment strategist at Raymond James & Associates in St. Petersburg, Florida, which manages \$214 billion.

Rising Concern

Yields on U.S. inflation-protected debt show increasing concern about consumer prices eroding the value of fixed payments. The **difference** in rates on 10-year notes and Treasury Inflation Protected Securities, or TIPS, which reflects the outlook among traders for consumer prices over the life of the securities, is 1.75 percentage points. That's up from minus 0.02 points in November, though below the average of 2.06 points during the past decade, data compiled by Bloomberg show.

John Paulson, the New York-based hedge-fund manager who earned \$2.5 billion in 2008 betting against a recovery in U.S. housing, and **Warren Buffett**, the world's second-richest person, still expect inflation to climb.

Paulson & Co.'s biggest holding is the **SPDR Gold Trust** that buys bullion. Buffett, chairman and chief executive officer of Omaha, Nebraska-based Berkshire Hathaway Inc., said in June that government spending to ease the financial crisis may increase inflation.

Bigger Returns

"Stocks can easily go higher," **Marc Faber**, publisher of the Gloom, Boom & Doom report, said in a Sept. 22 Bloomberg Television interview from New York. "If you print the money, they can go anywhere."

While the S&P 500 is valued at the **highest level** since 2004 based on reported operating earnings from the past year, **Jeffrey Coons** at Manning & Napier Advisors Inc. says the index is still cheap relative to the net assets and sales of its companies.

The index trades for 2.18 times **book value**, or assets minus liabilities, 33 percent below its 15-year average, data compiled by Bloomberg show. The S&P 500 was never valued below 2 times net assets until the collapse of Lehman, data starting in 1994 show. The index fetches 1.15 times sales, 22 percent less than its average since 1993.

"Nobody, nobody, nobody knows what the E is in P/E coming off a severe recession," said Coons, co-director of research at **Manning & Napier**, which oversees \$21 billion in Fairport, New York. "One of the best measures in an environment like today is price-to-sales," he added. "When we look at the stocks in our portfolio, the valuations of stocks in it, a lot are 25 percent to 30 percent away from

their fair values.”

‘Not Getting Worse’

Stock gains will be limited should the economic recovery stall, according to **Eric Cinnamond**, manager of the \$239 million **Intrepid Small Cap Fund** that has gained 32 percent this year.

“Things have stabilized and are not getting worse, but they’re not necessarily getting better,” said Cinnamond, who has 18 percent of his assets in cash. “We’re actually getting more defensive.”

Sales of existing U.S. homes unexpectedly fell last month for the first time since March, according to a Sept. 24 report from the National Association of Realtors. The global economic recovery will probably be “sluggish,” International Monetary Fund Managing Director **Dominique Strauss-Kahn** said in an interview in Washington before last week’s Group of 20 nations summit.

Long-Term Earnings

Price-to-earnings ratios using a decade of **data** show stocks aren’t cheap. Equities trade for about 19 times profit, above the 16.3 average for the past 128 years, according to Yale University’s **Robert Shiller**. The professor uses 10 years of earnings to smooth out short-term fluctuations.

The MSCI World Index of stocks in 23 developed nations has **returned** 18 percent this quarter including the reinvested dividends of its 1,660 companies. Treasuries have gained 1.9 percent, according to Merrill Lynch & Co. Oil has slipped 4.4 percent in New York, while the Reuters/Jefferies CRB Index of 19 industrial and agricultural commodities added 0.8 percent.

Higher valuations reflect greater confidence among investors that the economy will rebound and spur a revival in earnings growth and consumer spending, according to **James Paulsen**, chief investment strategist at Wells Capital Management in Minneapolis, which oversees \$375 billion. Combined with the amount of cash still available to buy shares, Paulsen says equities are a good bet.

“There’s a huge amount of dry powder on the sidelines that could become a big catalyst for both the economy and the stock market,” Paulsen said. “As confidence grows in the sustainability of this recovery, more cash is going to find itself into economic or investment pursuits. Considerable buying power could be reallocated into stocks.”

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