EQUITIES: BUY; SELL; OR, HOLD ?

This is not the best time to be aggressively buying into equities – anywhere in the world.

This is **TARGET**'s opinion, only, but it is based upon a number of very basic truths, many of which are only too often overlooked by quite a number of people.

In a bullish market, investors and speculators get carried away by their own greed: The buying frenzy is whipped up in similar fashion to hungry sharks, targeting in on a school of fish.

Over-generalisations in a bullish market become rampant, with people, making all kinds of comparisons between this bull market and that bull market, this new **I**nitial **P**ublic **O**ffering (IPO) and that new Initial Public Offering.

Of late, The Hang Seng Index, the key index of The Stock Exchange of Hongkong Ltd, has reached new highs on record daily levels of activity, ramped up by investor excitement at the spate of the IPOs of banks, owned and operated by the Government of the People's Republic of China (PRC).

Strip out the latest PRC, bank IPOs and one notes that daily volumes of activity fall back, markedly.

For some weeks, now, PRC banks and PRC infrastructural companies have dominated trading of the 10 most-active counters of the Main Board of The Stock Exchange of Hongkong Ltd.

The latest batch of PRC banks are not particularly good financial institutions and, in fact, their recent past histories leave a lot to be desired.

But they are ubiquitous in the Middle Kingdom.

The hype has been the thing for their successful flotations on the premier equity market of The Stock Exchange of Hongkong Ltd – little else.

Of course, few people will write such things because it is not in their best interests so to do.

TARGET (), however, feels compelled to tell it the way that it, really, is: These PRC banks are big and, because of their political clout in Beijing, they can throw their weight around in order to bring about that which is deemed to be in the best interests of the PRC State – sometimes, if not always, to the detriment of small bank customers, many of whom are quite ignorant of many things, including financial planning and investments.

As for the year-end figures of these banks, who really knows the truth of the situations?

One must rely on generosity and creative accounting, for the most part, in trying to analyse Profit and Loss Accounts and Consolidated Balance Sheets of some, if not all, of these banks.

But the investing public continues to rush out in order to buy into these large, PRC-domiciled banks which cannot print scrip quick enough to fill the demand.

In the mad dash to get a few thousand of these bank shares, investors completely disregard fundamentals.

In fact, **TARGET** would hazard a guess that very few Hongkong investors, putting in their cheques in order to buy a few share in these banks, even bother to crack open the prospectuses and, even if they do open these tomes, they are quite unlikely to be able to understand very much of that which they read.

TARGET's chief financial analyst does not bother to write up these banks because it is almost impossible to understand what is going on in them; and, this medium has never published public relations handouts, as do many other publications of the Hongkong Special Administrative Region (HKSAR) of the PRC.

The Hard Landing Is Coming

Aside from the euphoria for the scrip of PRC-domiciled banks, however, euphoria which will die as suddenly as it appeared, in all likelihood, there are many other reasons that make one think that equity markets, around the world, are due for a hard landing.

As **TARGET** has stated, many times in the past, the economy of the US is grinding to a halt.

Weekly, there is growing evidence of this (Please refer to last Monday's **TARGET** Intelligence Report, Volume VIII, Number 210).

One cannot, and should not, disregard the growing evidence of the malaise of the largest single economy of the world because economic growth, worldwide, productivity factors and inflation will not continue to be benign for much longer.

The penny for many investors will drop.

It is just a matter of when, not if.

Investors and their gurus often look at recent price levels of their quoted *'darlings'* and compare them with the same period of one year ago or even more than 2 years ago and, based on these comparisons, come to the conclusion that the share price is, still, very reasonable.

This, of course, can be very misleading as a method of determining whether or not the price of the scrip of this company or that company is within buying range.

Inflation, alone, causes share prices to rise and this, only too often, is not taken into account by the vast majority of investors.

Then, on viewing balance sheets of companies, one notes that many of them are stronger today than ever before.

Whenever there is a sharp sell-off on major equity markets and/or whenever there is a material downturn in an economy, one that could have residual effects, companies look to strengthen balance sheets in an effort to reduce future risk as much as possible.

Beware: One can be carried away by looking at strong balance sheets.

Then, again, one is told that the earnings of a company for this quarter or that quarter, this year or that year, are likely to be a great deal higher than the earnings of the previous quarter/year.

One hears only too often: Get in, now, while the going is good!

Again, inflationary factors often causes corporate earnings to grow.

However, the question should be raised as to whether or not the earnings of a company are rising in line with the growth of business, not just a figure on the Bottom Line, one which may be related, solely, to inflation or the ability of management to raise prices for its products.

As for employing the concept of the familiar Price-Earnings Ratio, which may indicate that the scrip of a company is cheaper, today, than it was at this time, one year ago, or even 2 years ago, this method of ascertaining whether or not a company's shares are within buying range is flawed, too.

If the scrip of a company, during a bull market, was terribly expensive when the Price-Earnings Ratio was standing at, say, 25 times, at today's calculation of a Price-Earnings Ratio of 10 times, it may not mean very much.

Because, all things considered, today's share price may well be outrageously too expensive – even by the standards of the last bull market.

The key to determining a fair valuation of a company's scrip is to be able to readjust it for cyclical periods in order to make logical comparisons.

One should not just look at absolute figures, only.

Interestingly enough, over the past 5 years, it appears that there have been little material changes in Price-Earnings Ratios of most of the blue chips, listed on The New York Stock Exchange.

That being said, then, it would appear that it is, after all, time to buy into this market.

Hold on, there!

If the price of equities, today, are standing at Price-Earnings Ratios equal to their respective Price-Earnings Ratios of 5 years ago – when prices were, also, hitting historic highs – then, if prices were too high 5 years ago, they must be too high, today, also.

If anything, to be entirely generous, share prices may well be standing at fair valuations, today, but not, necessarily, based on tomorrow's earnings' potential, all things considered.

So, if that dollar in your pocket is burning a hole in the lining of your pants and you feel that you must invest in stocks and shares, it seems reasonable to this medium to be tame in making any new financial commitments.

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