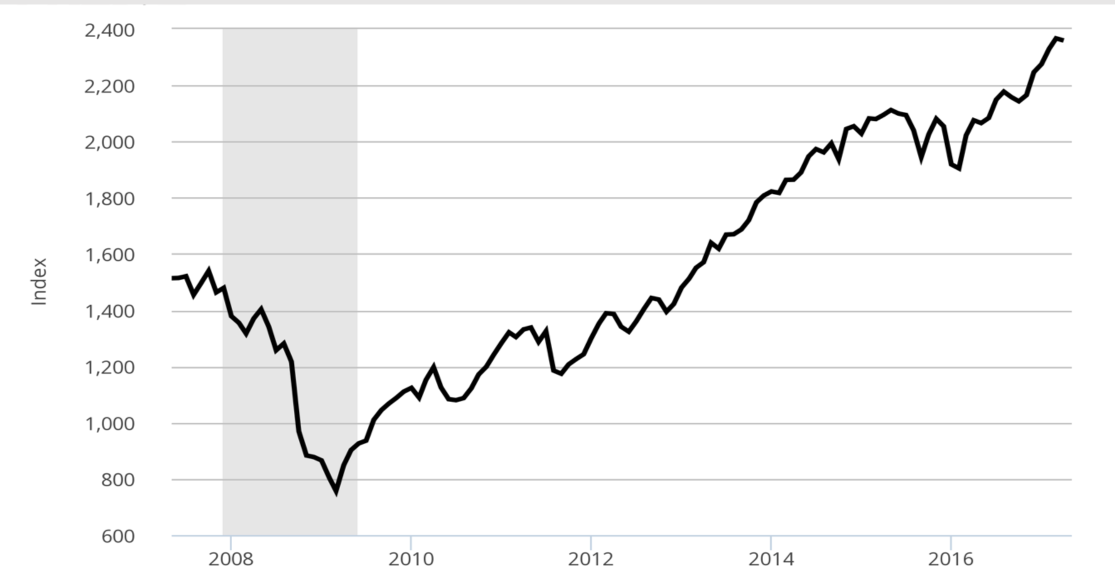
Gráfico da Semana

Is the U.S. stock market ready to pop?



Source: S&P Dow Jones Indices LLC

After a sharp fall during the recession in the wake of the financial market crisis of 2008 (see shaded area in the graph above), the U.S. stock market has made a turn-around in 2009. Since then equities have performed a rally that lifted the Standard & Poor's index of 500 stocks quoted on the New York Stock Exchange from below 800 up to 2399 index points on May 5, 2017. Yet while the stock market's valuation has tripled over the past couple of years, the U.S. economy in terms of its real gross domestic product has risen by less than 20 percent and in nominal terms about 25 percent in the past seven years.

Over the long run, stocks correlate with economic growth. There are, however, occasionally stretches of time when stocks outperform or underperform the real economy by considerable margins. Currently, so it seems, stock market valuation are well ahead of the real economy. Empirical evidence shows that market correction take place neither smoothly nor moderately, but the excess to the upside is followed by an excess to the downside and vice versa.

Are there reasons to believe that a stock market correction is imminent and that such a correction would bring down valuations considerably? Such a question asks for the determinants that have brought about the current high valuations.

One indisputable reason for the elevated valuations of the stocks in the United States is the policy of the so-called "quantitative easing" that made the U.S. central bank (FED) to increase the monetary base from below one trillion to almost four and a half trillion U.S. dollars. Concurrently, the FED has brought down the policy interest rate (Federal Funds Rate) from five percent in 2007 to 0.5 percent in 2009. It was not until towards the end of 2016 that the central bank began to raise the rate in a couple of small steps to the present level of one percent, which is still extremely low.

Interest rates at such a low level have not only led to a frenzy "search for yield". These low rates have also provoked companies to use their excess liquidity for stock buy-backs. Both policies are about to end and thus a correction of the stock market seems inevitable.

cafécdados: *Postado por Antony Peter Muller em 08/05/2017*