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# Big Money Poll: The Bull Will Be Right Back

By JACK WILLOUGHBY | MORE ARTICLES BY AUTHOR

America's money managers say stocks will resume their climb after a short but needed time out, according to our latest Big Money Poll.

It's going to take a lot more than the past month's 5%-plus selloff in stocks for America's money managers to change their upbeat tune. That's what they've been telling Barron's in the past two weeks, ever since 59% of participants in our latest Big Money poll said they were bullish or very bullish about the outlook for U.S. stocks through the middle of 2015. That's up from 56% in our spring survey, but below last fall's bullish reading of 68%.

The nation's professional investors aren't blind to the alarming developments that have tripped up the market in recent weeks, including evidence of slowing economic growth in key parts of the world, spreading violence in the Middle East, and even a possible Ebola pandemic. They are also worried about a coming change in Federal Reserve policy after years of falling interest rates, which provided a huge tail wind for stocks and other risk assets.

Scott Pollack for Barron's

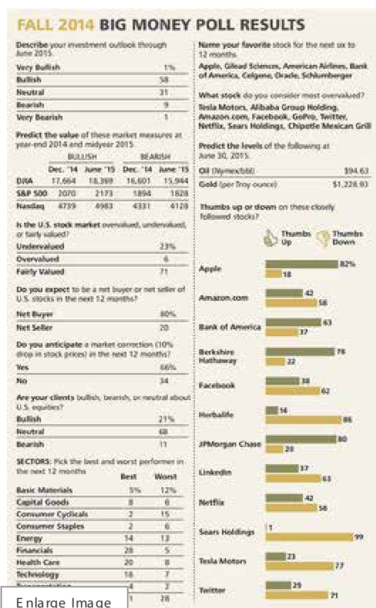
Equities will outperform other assets in the next 12 months, and U.S. shares will do best. The Big Money managers expect financials, health care, and tech stocks to lead the market higher.

Indeed, two-thirds of Big Money managers noted in our survey that they expect a correction, defined as a 10% drop in share prices, within the next 12 months. Whether smart or simply lucky, they're suddenly looking prescient.

Still, the pros expect decent growth in corporate earnings and moderate equity valuations

to put a floor under the market. They believe the bull market that began in 2009 will resume after an unpleasant but arguably healthy time-out.

BASED ON THEIR mean forecasts in the Big Money poll, the bulls see the Dow Jones industrials topping 18,360 by the middle of 2015, and the Standard & Poor's 500 index hitting 2173. While their targets, which imply a gain of about 12% for the Dow and 15% for the S&P 500, might seem aggressive after last week's rout, their commitment to U.S. equities remains intact.



FALL 2014 BIG MONEY POLL RESULTS

**Describe** your investment outlook through June 2015.

| | |
|---|---|
| Very Bullish | 1% |
| Bullish | 58 |
| Neutral | 31 |
| Bearish | 9 |
| Very Bearish | 1 |

**Predict the value** of these market measures at year-end 2014 and midyear 2015.

| | BULLISH | | BEARISH | |
|---|---|---|---|---|
| | Dec. '14 | June '15 | Dec. '14 | June '15 |
| DJIA | 17,664 | 18,369 | 16,601 | 15,944 |
| S&P 500 | 2070 | 2173 | 1894 | 1828 |
| Nasdaq | 4739 | 4983 | 4331 | 4128 |

**Is the U.S. stock market** overvalued, undervalued, or fairly valued?

| | |
|---|---|
| Undervalued | 23% |
| Overvalued | 6 |
| Fairly Valued | 71 |

**Do you expect** to be a net buyer or net seller of U.S. stocks in the next 12 months?

| | |
|---|---|
| Net Buyer | 80% |
| Net Seller | 20 |

**Do you anticipate** a market correction (10% drop in stock prices) in the next 12 months?

| | |
|---|---|
| Yes | 66% |
| No | 34 |

**Are your clients** bullish, bearish, or neutral about U.S. equities?

| | |
|---|---|
| Bullish | 21% |
| Neutral | 68 |
| Bearish | 11 |

**SECTORS:** Pick the best and worst performer in the next 12 months

| | Best | Worst |
|---|---|---|
| Basic Materials | 5% | 12% |
| Capital Goods | 8 | 6 |
| Consumer Cyclicals | 2 | 15 |
| Consumer Staples | 2 | 6 |
| Energy | 14 | 13 |
| Financials | 28 | 5 |
| Health Care | 20 | 8 |
| Technology | 16 | 7 |
| [illegible] | 4 | 2 |
| [illegible] | 1 | 28 |

**Name your favorite** stock for the next six to 12 months.

Apple, Gilead Sciences, American Airlines, Bank of America, Celgene, Oracle, Schlumberger

**What stock** do you consider most overvalued?

Tesla Motors, Alibaba Group Holding, Amazon.com, Facebook, GoPro, Twitter, Netflix, Sears Holdings, Chipotle Mexican Grill

**Predict the levels** of the following at June 30, 2015.

| | |
|---|---|
| Oil (Nymex/bbl) | $94.63 |
| Gold (per Troy ounce) | $1,228.93 |

**Thumbs up or down** on these closely followed stocks?

| | Thumbs Up | Thumbs Down |
|---|---|---|
| Apple | 82% | 18 |
| Amazon.com | 42 | 58 |
| Bank of America | 63 | 37 |
| Berkshire Hathaway | 78 | 22 |
| Facebook | 38 | 62 |
| Herbalife | 14 | 86 |
| JPMorgan Chase | 80 | 20 |
| LinkedIn | 37 | 63 |
| Netflix | 42 | 58 |
| Sears Holdings | 1 | 99 |
| Tesla Motors | 23 | 77 |
| Twitter | 29 | 71 |

Enlarge Image

Andrew Slimmon, a senior portfolio manager at Morgan Stanley Global Investment, whose Chicago-based group manages $4.1 billion of equities, notes that Europe's economic troubles sparked a selloff in U.S. stocks in 2010 and in 2011, just as concerns about another European recession are sending tremors through the market today. "The fear then was that contagion from Europe would cause a recession in the U.S.," Slimmon says. "It came at a time when the U.S. economy was more fragile. Afterward, the market came back strongly. This time, the U.S. economy is on stronger footing. The magnitude of the decline likely won't be as large, and the rebound could be greater."

To Joel Tillinghast, co-manager of the $46 billion Fidelity Low-Priced Stock fund, the allure of stocks seems obvious. Money-market funds pay holders little to nothing, whereas stocks with decent dividends pay enough to compete with bonds—and offer the possibility of capital gains. The economics are particularly compelling given five or 10 years of compounding. "People will gradually realize that equities are a superior alternative," he says.

U.S. equities are especially attractive, Tillinghast adds. "Numerical predictions will either be right or wrong," he says. "I'd urge people to consider that the greatest growth opportunities come from American-centric industries, and that interest rates aren't going up. People are freaked out now, but fantastic opportunities have been created by the fact that America is less dependent on imported oil, and is a leader in biotechnology and social media. America has one of the strongest economies in the world."

Many biotech and social-media shares reside on the Nasdaq, and disproportionately influence the value of the Nasdaq Composite. The Nasdaq has slid 7% since Sept. 2, to a recent 4258, but our bullish respondents are enthusiastic about its prospects. They see a near-20% recovery in the offing that could leave the index near 5000 by the middle of next year.

"People see upside [in the Nasdaq] because they see the pace of innovation in Silicon Valley and biotechnology, even though valuations are starting from a higher price," says Christopher Ailman, chief investment officer of the California State Teachers' Retirement System, or CalSTRS, which oversees $186.4 billion.

As for the broader market, Ailman says, "This may indeed be the 10% correction I was anticipating. But we will have a discussion tomorrow and likely talk about buying opportunities, not selling, because the fundamentals of the economy haven't changed. The GDP [gross domestic product] forecast still has a nice, positive trend. Corporate earnings aren't growing as fast as in the past, but they are still growing."

THE BULLS' CAMP has drawn modestly this fall from the undecided, as 31% of managers now say they are neutral about stocks, down from 35% in the spring. The bears' ranks are essentially unchanged at about 9%.

Notwithstanding the bullish tilt of our poll, 71% of Big Money managers consider the market fairly valued—or at least they did when the survey was e-mailed a few weeks ago and the Dow was closer to 17,200 than today's 16,380. But this is less of a contradiction than it might seem. "Historically, markets don't stop at fair value, but go past it," says

Robert Lutts, president and chief investment officer of Cabot Wealth Management in Salem, Mass., which oversees $550 million. “Prices are getting up there, but we have none of the excesses that marked the top of previous markets.”

Lutts thinks worries about a rate hike have been exaggerated, while the benefits of falling energy prices have been ignored. Crude oil prices have fallen more than 20% since mid-July, to a recent $83.02 per barrel, while gas prices have slipped below $3.30 a gallon at the pump.

“People don’t appreciate how much of a plus they get from lower oil and gas prices,” he says. “It’s like a tax reduction.”

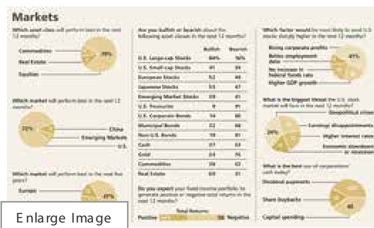
Charles Lemonides, founder of ValueWorks, a New York hedge fund with $250 million under management, agrees. He predicts the price of oil will drop to $75 a barrel by mid-2015, spurring further reductions in gasoline prices and putting more money into consumers’ wallets. Nor did he see signs, before the market’s recent tumble, of the euphoria that typically signals a bull market’s end is near. Many stocks were “quietly” correcting while the averages marched higher, he notes. “The froth just isn’t the same as at previous peaks,” Lemonides says. “I’m more inclined to be buying today than I was six months ago.”

Chances are he won’t be alone. Eighty percent of Big Money respondents say they expect to be net buyers of stocks in the next 12 months; just 20% expect to be sellers.

PROFESSIONAL INVESTORS are more bullish these days than the people whose money they manage. Nearly 70% of Big Money managers say their clients are neutral about U.S. equities, compared with just 21% who claim their clients are bullish.

The managers regard geopolitical crises, earnings disappointments, higher interest rates, and a more sluggish economy as the biggest threats facing U.S. stocks in coming months. In the plus column, they cite rising corporate profits, higher GDP growth, better employment news, and any decision by the Fed not to raise short-term interest rates as the factors most likely to get stocks back on track.

More corporate merger and acquisition activity, a pickup in China’s economy, and steps toward U.S. tax reform also could light a fire under share prices, they say.




Despite the challenges ahead, or perhaps because of them, 70% of Big Money managers expect equities to outperform other asset classes in the next 12 months.

A distant 9% think that either real estate or commodities will be the safest haven. Looking out five years, 80% of managers favor equities, something to remember as you’re surveying the wreckage after last week’s storm.

More than 70% of Big Money respondents expect the U.S. to be the best-performing market in the coming year, but only 30% see America dominating equity markets in five years. Emerging markets could be ascendant again, as a rising middle class in developing countries controls a greater share of the world’s wealth. The global market has changed “dramatically” since 2008, says Joseph Parnes, founder of Technomart Investment Advisors in Towson, Md., who cites new sources of wealth emerging in Asia.

Even so, 84% of poll respondents say they’re bullish on large-cap U.S. stocks in the near term, while 94% say they’re bullish over a five-year horizon. U.S. small-caps also could win more fans as they start to recover. Joseph Ray, president of Dallas-based Gerald L. Ray & Associates, which manages $700 million, calls the U.S. “the best house in a bad neighborhood.” U.S. companies, he notes, have strong balance sheets and plenty of cash, and ample opportunities to grow by doing deals.

The managers are split on the near-term prospects for Europe and Japan, but nearly 60% favor emerging markets. They expect to develop more enthusiasm for foreign markets in the years ahead. They like cash more than they did last spring, at 37% bulls versus 21%, but gold doesn’t glitter for them. Only 24% of poll respondents are bullish on the 12-month outlook for bullion, although 38% favor gold over five years.

FINANCIAL STOCKS are the managers’ favorites these days, with 28% expecting them

to lead the market in coming months. Rick Seto, managing director at Pasadena, Calif.–based Flaherty & Crumrine, which oversees $5 billion, gives thumbs up to **Bank of America** (BAC), whose litigation overhang, he says, has largely passed. BofA trades for $16.21, or about 0.8 times book value, versus a peer-group average of 1.2 times book. He thinks the stock could rally to $21 or so in the next 12 months as the U.S. economy continues to recover.

Health care and tech stocks also could lead the market, according to poll respondents. Utilities have the poorest prospects, in their view, followed by consumer-cyclical shares.

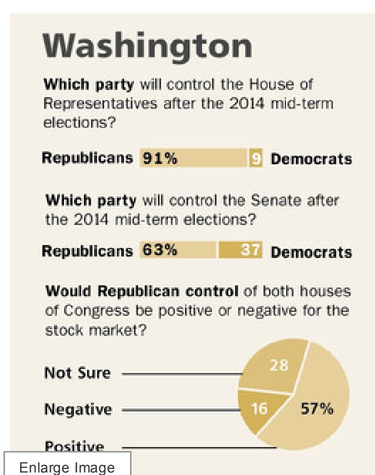
As for individual stocks, **Apple** (AAPL) remains a hands-down favorite of the Big Money men and women. Some have been seduced by the company's groundbreaking products—Apple recently unveiled a watch, a mobile-payment system, a new generation of iPhones, and new iPads and iMacs—and some, by the low valuation of the shares. At a recent $97.67, Apple fetches a mere 10 times estimated 2015 earnings of $7.33 a share, after stripping out the $28-a-share of cash on the company's balance sheet.

**Schlumberger** (SLB), the Houston-based oil-services leader, is another Big Money pick (and the subject of a positive cover story, "**Right on Target**," in the Aug. 18 issue of *Barron's*). The stock has been hammered since June, falling 20% to $93.97. It trades today for 14.6 times next year's expected earnings of $6.64 a share, and sports a dividend yield of 1.65%. Analysts are forecasting an 18% rise in 2015 earnings per share. Slimmon, the Morgan Stanley manager, expects oil-services companies such as Schlumberger to be early beneficiaries of the next upswing in oil prices.

The Big Money managers also espy plenty of overvalued issues, prominently including electric-car maker **Tesla Motors** (TSLA), **Amazon.com** (AMZN), and **Alibaba Group Holding** (BABA), the Chinese mobile-commerce giant whose shares went public last month in the largest new-issue offering in history. The deal priced at $68 per American depository receipt and the stock opened at $92.70. The ADRs were changing hands late last week at around $88, or 37 times future earnings.

The managers likewise said they consider **Netflix** (NFLX) overvalued. The stock plunged $86.89, or 19%, Thursday, to $361.70, after the video-streaming company reported disappointing third-quarter subscriber growth.

**THE BIG MONEY POLL** is conducted twice a year, in the spring and fall, with the help of Beta Research in Syosset, N.Y. The latest survey drew responses from 145 portfolio managers from across the country, representing some of the largest investment companies in America and many smaller firms. *Barron's* has been conducting Big Money for more than 20 years to get professional investors' read on the financial markets and the economy.




Even the Big Money bears are looking somewhat bullish after stocks' latest slide. Their mean bearish forecast put the Dow at 16,600 by year end and 15,900 by June 30, 2015. But numerical predictions, again, don't come close to reflecting their concerns or downbeat market perspective.

Marc Heilweil, founder of Spectrum Advisory Services, an Atlanta manager with $530 million in assets, had the lowest forecast in our fall survey. He expected the Dow to trade around 16,500 at year end, but plummet to 13,000 by mid-2015. "The earnings growth hasn't been there," Heilweil says. "Consumer-spending patterns aren't ready to turn. And corporations increasingly are run on a financial basis, with an emphasis on buying back stock instead of spending to grow."

Based on our poll, others agree. Forty percent of Big Money managers think capital spending is the best use of corporate cash today, while 42% favor dividend payments. Only 18% believe companies are spending most wisely when they buy back shares, although lower stock prices could make buybacks more attractive for a while.

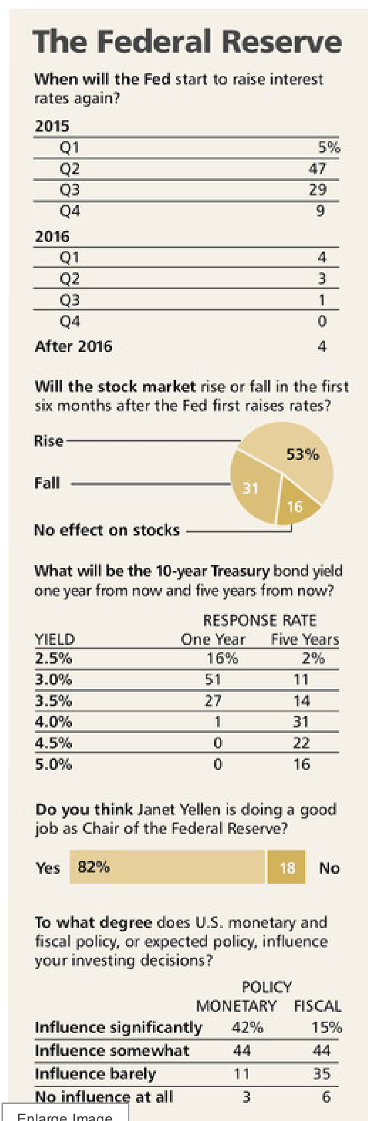
Guy Scott, a portfolio manager at Janus International Equity Fund, a $1 billion-in-assets manager in Denver, also has been bearish of late. “The U.S. market is overvalued,” he said recently. “The S&P 500 has risen for five years in a row. Very rarely does it go up a sixth consecutive year. Also, China’s economy is slowing. The risk is that it slows more than people expect.”

Scott pegged the Dow’s year-end close at 16,300, although he expects stock prices to rise in the first half of 2015.

**IF MOST BIG MONEY** managers are bullish to neutral on stocks, they are overwhelmingly bearish on bonds—for the next 12 months and five years. Consider this 12-month tally: 91% are bearish on Treasuries; 86%, on U.S. corporate bonds; 81%, on non-U.S. bonds; and 68% on tax-free municipals. Only 3.5% of managers expect bonds to be the best-performing asset class in the next 12 months, which probably says more about their hostile view of equities.

Don’t write off bonds altogether, however, as 44% of managers expect their fixed-income portfolios to generate positive returns in the next year. The bond market continues to confound, as its safe-haven status is buoying prices and depressing yields even further. The yield on 10-year Treasuries slipped below 2% last Wednesday, before ending the week at 2.22%.

“Have any predictions proved more consistently wrong than the prediction since 2012 that interest rates would rise?” asks Peter Scholtz, founder of Scholtz & Co., a $140 million asset manager in Norwalk, Conn.



## The Federal Reserve

**When will the Fed** start to raise interest rates again?

| | |
|---|---|
| **2015** | |
| Q1 | 5% |
| Q2 | 47 |
| Q3 | 29 |
| Q4 | 9 |
| **2016** | |
| Q1 | 4 |
| Q2 | 3 |
| Q3 | 1 |
| Q4 | 0 |
| **After 2016** | 4 |

**Will the stock market** rise or fall in the first six months after the Fed first raises rates?



**What will be the 10-year Treasury** bond yield one year from now and five years from now?

| YIELD | RESPONSE RATE One Year | Five Years |
|---|---|---|
| **2.5%** | 16% | 2% |
| **3.0%** | 51 | 11 |
| **3.5%** | 27 | 14 |
| **4.0%** | 1 | 31 |
| **4.5%** | 0 | 22 |
| **5.0%** | 0 | 16 |

**Do you think** Janet Yellen is doing a good job as Chair of the Federal Reserve?



**To what degree** does U.S. monetary and fiscal policy, or expected policy, influence your investing decisions?

| | POLICY MONETARY | FISCAL |
|---|---|---|
| **Influence significantly** | 42% | 15% |
| **Influence somewhat** | 44 | 44 |
| **Influence barely** | 11 | 35 |
| **No influence at all** | 3 | 6 |

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The Federal Reserve is scheduled to end its third and final round of quantitative easing, or bond buying, this month, provoking further anxiety among investors. QE and other strategies have kept interest rates at near-zero levels for the past few years, to allow the economy and banking sector to recover from the 2007-’09 financial crisis and recession. The central bank isn’t expected to start lifting the federal-funds rate, to which other rates are tied, until sometime next year.

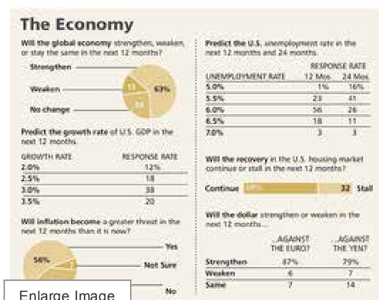
Seventy-six percent of Big Money respondents look for the Fed to act in the second or third quarter of 2015, although 8% don’t see a rate hike coming until sometime in 2016. Four percent predict it will occur even later than that.

Weakness in the rest of the world might buoy the U.S. stock market as this year winds down, says Donald Sazdanoff, founder of Sovereign Asset Management in Mansfield, Ohio, with assets of $65 million. He predicts the Federal Reserve will raise rates with an eye to that weakness, doing so only gradually. “If the Fed raises rates next year, it will do so very slowly or incrementally so as not to disrupt the market,” he says.

By keeping short-term rates at 0.25%, the Fed is punishing savers and painting itself into a corner, Sazdanoff says. Federal Reserve Chair Janet Yellen will want to get short rates up, he argues, to be able to stimulate the economy when the next real recession hits. Otherwise, the Fed will be left without monetary tools, he says.

JUST OVER HALF of Big Money managers see 10-year Treasury yields sitting at 3% a year from now. Another 27% think yields will have climbed to 3.5%. Peering out five years, 70% see yields of 4% to 5%. But don't look for the stock market to swoon when interest rates finally start to rise. Fifty-three percent of managers anticipate stocks will advance in the six months after the Fed starts raising interest rates, while just 31% expect the market to weaken.

Fed Chair Yellen gets resounding applause from the Big Money crowd, in the form of an 82% approval rating. While her predecessor, Ben Bernanke, set upon a course of unprecedented monetary easing as the global banking system nearly collapsed, Yellen might have the more difficult job of mopping excess liquidity to avoid inflation. "She's trying hard to give clear guidance, while also allowing the Fed some flexibility, given the economic uncertainty," says CalSTRS' Ailman.

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THE GLOBAL ECONOMY, whose health was called into question broadly last week, looks pretty sound to our respondents, 63% of whom expect it to strengthen in coming months. "All things are in place for global growth to accelerate," says Robert Turner, chairman of Turner Investments, in Berwyn, Pa., which manages $2 billion. "The Japanese and European economies are getting better. We're also encouraged by the possibilities of an investor-friendly India."

The U.S. economy looks solid, too, with 58% of managers forecasting U.S. GDP growth of 3% to 3.5% in the next 12 months. "The public underestimates the trauma caused by the 2008 crisis," says Thomas Luddy, manager of the $10.5 billion J.P. Morgan U.S. Equity fund. "The economy is still recovering from it. That's why there is room for reasonable growth."

Most managers expect the U.S. unemployment rate to settle in the 5.5%-to-6% zone; it was 5.9% in September, according to the Bureau of Labor Statistics. A smaller percentage than in the spring survey look for the housing recovery to continue—68% to 81%—and a greater percentage are concerned about the threat of inflation: 56% now, versus 51% in the spring.

The dollar has been the world's go-to currency in times of turmoil, and the managers, by a wide margin, expect the buck to continue to strengthen against both the euro and the yen.

WHILE THE BIG MONEY managers are glued to the markets, they're also keeping a close watch on Washington, where next month's elections could alter the composition and priorities of Congress. Our seers, by a 91% margin, expect the Republicans to retain control of the House of Representatives. Sixty-three percent also predict the GOP will gain control of the Senate.

Yet, only 57% think Republican control of both houses will be positive for the stock market. Harlan Cadinha, chairman of Cadinha & Co. in Honolulu, which manages $1 billion, worries that the GOP's aversion to spending might slow the economy's gains.

This has been an active year for financial journalists, but hardly a winner for investment professionals. Just 49% of managers say they are beating the market professionally, while 54% confess that they're doing so personally. If last week's pullback is as healthy—and temporary—as the Big Money folks say, both the stock market and the pros could have a better 2015.

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