

RBS uber-bear issues fresh alert on global stock markets

Three-month slide could hit record lows, Royal Bank of Scotland chief credit strategist Bob Janjuah predicts.

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A bear market is being forecast for after the summerPhoto: REUTERS

Britain's Uber-bear is growing again. After predicting a torrid "relief rally" over the early summer, Bob Janjuah at Royal Bank of Scotland is advising clients to take profits in global equity and commodity markets and prepare for another storm as winter nears.

"We are now in the middle of a parabolic spike up," he said in his latest confidential note to clients.

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"I expect this risk rally to continue into – and maybe through – a large part of August. What happens after that? The next ugly leg of the bear market begins as we get into the July through September 'tipping zone', driven by the failure of the data to validate the V (shaped recovery) that is now fully priced into markets."

The key indicators to watch are business spending on equipment (Capex), incomes, jobs, and profits. Only a "surge higher" in these gauges can justify current asset prices. Results that are merely "less bad" will not suffice.

He expects global stock markets to test their March lows, and probably worse. The slide could last three months. "A move to new lows is highly likely," he said.

Mr Janjuah, RBS's chief credit strategist, has a loyal following in the City. He was one of the very few analysts to speak out early about the dangerous excesses of the credit bubble. He then made waves in the summer of 2008 by issuing a global crash alert, giving warning that a "very nasty period is soon to be upon us" as – indeed it was. Lehman Brothers and AIG imploded weeks later.

This time he expects the S&P 500 index of US equities to reach the "mid 500s", almost halving from current levels near 1000. Such a fall would take London's FTSE 100 to around 2,500. The iTraxx Crossover index measuring spreads on low-grade European debt will double to 1250.

Mr Janjuah advises investors to seek safety in 10-year German bonds in late August or early September.

While media headlines have played up the short-term bounce of corporate earnings, Mr Janjuah said this is a statistical illusion. Profits were in

reality down 20pc in the second quarter from the year before. They cannot rise much as the West slowly purges debt and adjusts to record over-capacity. "Investors are again being sucked back into the game where 'markets make opinions', where 'excess liquidity' is the driving investment rationale.

"The last two Augusts proved to be pivotal turning points: August 2007 being the proverbial 'head-fake' when everyone wanted to believe that policy-makers had seen off the credit disaster at the pass, and August 2008 being the calm before the utter collapse of Sept/Oct/Nov... 3rd time lucky anyone?"

The elephant in the room is the spiralling public debt as private losses are shifted on to the taxpayer, especially in Britain and America. "Ask yourself this: who bails out Government after they have bailed out everyone?"

Mr Janjua said governments might put off the day of reckoning into the middle of next year if they resort to another shot of stimulus, but that would store yet further problems. "If what I fear plays out then I will have to concede that the lunatics who ran the asylum pretty much into the ground last year are back in control."

Over at Morgan Stanley, equity guru Teun Draaisma thinks we are through the worst. "We were on course for a Great Depression in February, but armageddon was avoided. Governments did not repeat the policy errors of the 1930s."

"We have seen the lows of this crisis. This is a genuine rebound rally, and it has been short by historical standards so far," he said.

Mr Draaisma, who called the top of the bull market almost to the day in mid-2007, has crunched the worldwide data on 19 major stock market crashes over the last century. They show that the typical rebound rally (as opposed to bear trap rallies, when markets later plunge to new lows) lasts 17 months and stocks rise 71pc. The 1993 rally in the US was 170pc over 13 months. Finland's rally in 1994 was 295pc. Hong Kong rallied 159pc in 2000. This rebound is only five months old. The key indexes have risen 49pc in the US and 42pc in Europe. Mr Draaisma advises clients to stay in the stocks for now, but stick to telecom companies, utilities, and oil.

Yet he too expects a nasty correction once this rally falters. The usual trigger at this stage of the cycle is when central bankers start to make hawkish noises, typically a couple of months before the first turn of the screw (normally a rate rise, but in this case an end to "quantitative easing". "As long as policy-makers are talking about how fragile the recovery is, equities are unlikely to go down much."

This moment can be hard to judge. There has already been rumbling from some governors at the US Federal Reserve and from the European Central Bank's Jean-Claude Trichet. Markets are pricing in rates rises by early next year.

The pattern after major financial bust-ups is that the rebound rally gives way to another fall of 25pc or so, lasting a year, followed by five years of hard slog as stocks bounce up and down in a trading range, going nowhere. Mr Draaisma suggests taking a close look at the chart of Japan's Nikkei index from 1991 to 1999. Gains were zero.

We are in uncharted waters, however. Monetary and fiscal stimulus has been unprecedented. Russell Napier at Hong Kong brokers CLSA says a powerful bull market is already taking shape as the American giant reawakens. Perma-bears will be left behind. He said: "It is dangerous to be in cash."

When the finest minds in the business disagree so starkly, the rest of us can only shake our heads in confusion.

<http://www.telegraph.co.uk/finance/markets/6018076/RBS-uber-bear-issues-fresh-alert-on-global-stock-markets.html>