Investor Outlook: Trends are Looking Neutral
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There’s no question about it: The market is a daunting place for investors seeking solid returns without taking on increased risk, especially right now. Equities are expensive, and fixed income is not terribly enticing, especially with the potential for long-term interest rates to rise if the U.S. Federal Reserve finally raises rates in September.

Shifting to “neutral” on U.S. equities

Our models have caused us to shift our position on U.S. equities to “neutral,” after having been moderately positive on them to this point in 2015. We just don’t see an advantage to holding a larger equity position relative to fixed income for the rest of this year. Moreover, in recent weeks the momentum signals for both equities and fixed income have slowed, and the business cycle outlook has softened.

Looking at the numbers

Drilling down into the numbers, the U.S. equities market is the most expensive among major markets globally, with a price to book value of 2.9, compared with 2.7 a year ago.¹ Moreover the Shiller price-to-earnings ratio is 26.7 as of June 2015—which keeps it higher year-to-date in 2015 than at any point since 2007.² Japanese and European equities are also moderately expensive at this time. But there’s still upside—particularly in Europe, assuming the continent gets past its Greek problems and the European Central Bank’s continued quantitative easing takes hold. This contrasts with emerging markets, where the strong dollar, falling commodities prices and China’s slowing growth are all creating headwinds.

Moving with momentum

With all of that, we’re still seeing momentum playing a role in our 2015 outlook for the third quarter. Plus, the stability we’re seeing in most markets means that our overbought contrarian
quarter. Plus, the stability we're seeing in most markets means that our overbought contrarian signals now are more neutral. In Japan, however, a strong run has recently moved that market into overbought territory.

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In our view, with that global mix of high prices, neutral-to-slightly positive sentiment, and a generally positive business cycle, it isn't difficult to land where we have: Largely neutral across the board, with no single market showing either great risk or great upside. European equities are probably our favorite play. Everywhere else, no favorites.

For more detail, be sure to read our 2015 Global Market Outlook- 3Q update. It’s a snapshot of what we think investors and fund managers need to be thinking about before they head to the beach this summer. You can also see a highlight of the forecast at our 2015 Global Market Outlook – Infographic.

1 Russell 1000® Index as of May 2014 and May 2015.

2 Definition: The cyclically adjusted price-to-earnings ratio, commonly known as CAPE, Shiller P/E, or P/E 10 ratio is a valuation measure usually applied to the US S&P 500 equity market. It is defined as price divided by the average of 10 years of earnings (moving average), adjusted for inflation.

3 Definition: In assessing the attractiveness of asset classes relative to one another, Russell’s modeling capability uses a pair-wise construct with asset classes shared across multiple pairs, each with independent valuations. At present, the capability includes over 120 pairs leveraging signals from greater than 400 models. The signals used are based on proprietary models developed by Russell.

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