



Weekly Market Commentary

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Highlights

Investors are not currently displaying signs of optimism that have historically marked a peak for stocks.

Bubble Check

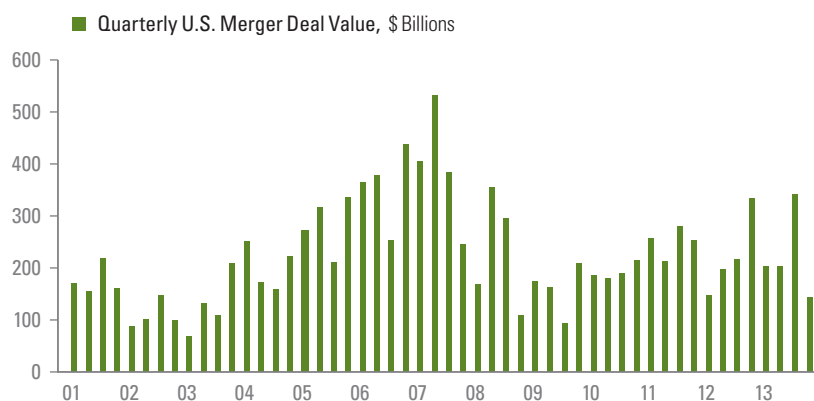
Sentiment can be an important tool in measuring risk in the stock market. When investors get too bullish, it can be seen as a cautionary flag that the market may be due for a fall or a bubble is nearing its peak.

Fortunately, investors are not currently displaying signs of optimism that have historically marked a peak for stocks. When we look at sentiment, we focus most of our attention on the actions taken by market participants, rather than how they respond to surveys. A few key measures include: quiet mergers & acquisitions (M&A) activity, the lack of a surge in initial public offerings (IPOs), and only a very recent uptick in inflows into funds that invest in U.S. stocks.

M&A Activity Remains Quiet

A hot market for mergers and acquisitions has often been a sign of an overheated stock market as confident corporate executives seek to aggressively expand their businesses. The most recent example can be seen in the run-up in deals that took place in the mid-2000s that foreshadowed the 2007 peak in the stock market [Figure 1]. In addition, M&A deal premiums—the amount offered above the pre-deal price—remain around 25%, in line with the 10-year average.

1 M&A Activity Remains Subdued



Source: LPL Financial Research, Bloomberg data 12/09/13

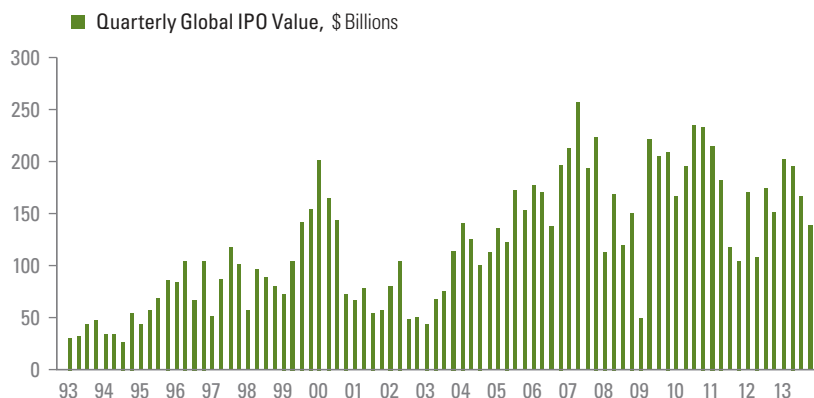
Past performance is no guarantee of future results.



IPO Activity Is Not Surging

IPOs tend to soar leading up to market peaks when confident investors are eager to snatch up the shares in the newly public companies, as we saw in 1999 and the mid-2000s [Figure 2]. Currently, global IPO activity is not showing signs of heating up.

2 IPO Activity Not Heating Up



Source: LPL Financial Research, Bloomberg data 12/09/13

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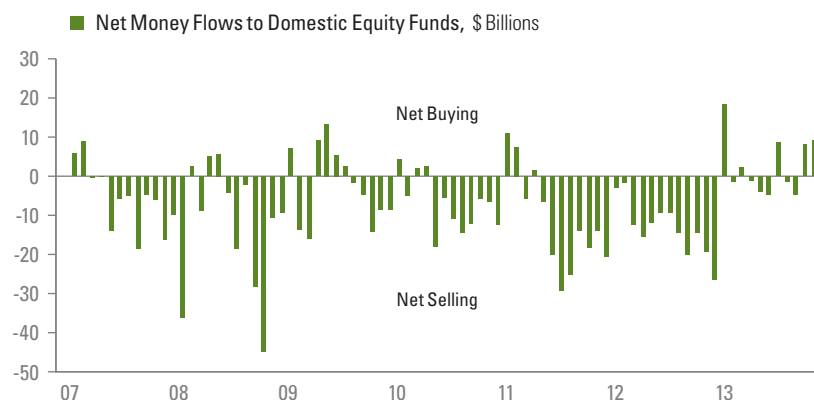
Individual Investors Have Not Been Aggressive Buyers

While not always a sign of a market peak until it reaches extremes, a pickup in money coming into the stock market from individual investors is a sign of improving confidence.

We may be quite some time away from an extreme in the appetite of the individual investor for stocks.

Net inflows to funds that invest in U.S. stocks have been weak and only recently posted two months of back-to-back inflows—an occurrence not seen since early 2011. As presented in the *Weekly Market Commentary* from November 13, 2013 entitled *Chasing Returns*, investors tend to follow moves in the five-year rolling return for the stock market, which turned

3 Money Flows to Funds That Invest in U.S. Stocks Have Been Weak



Source: LPL Financial Research, Investment Company Institute 12/09/13

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sharply positive with a double-digit margin over bonds about a month ago, helping to sustain the recent trend of inflows. We may be quite some time away from an extreme in the appetite of the individual investor for stocks.

Currently these sentiment indicators, among others, are not waving any cautionary flags for investors despite the strong stock market performance in 2013 and since the low of nearly five years ago. However, we will continue to watch these indicators as a sign of rising risk in the market. ■

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INDEX DESCRIPTIONS

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

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