

TOBAM CEO: There is a bubble brewing in US low volatility stocks

US market 'never been as concentrated as it is today'



Tom Eckett 17 NOVEMBER 2016

Yves Choueifaty, CEO of TOBAM, has said low volatility stocks in the US are in bubble territory as a result of strong inflows and the high concentration of the US stockmarket.

Speaking to *Investment Week*, Choueifaty (*pictured*) said: "There are bubbles within the bubble. The areas in which we see the most concentration are financials in Europe, financials and energy in emerging markets and low volatility [stocks] in the US."

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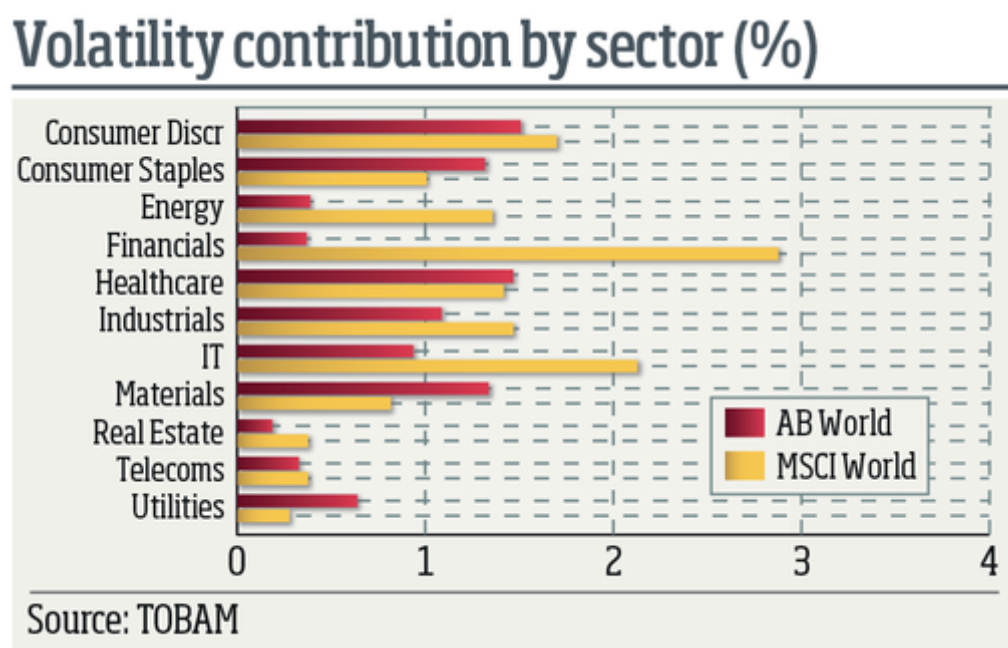
Choueifaty said as these stocks, which include defensive names, become more expensive and the concentration of the market grows, the firm's diversified smart-beta strategies underperform.

TOBAM runs Anti-Benchmark smart-beta strategies, which aim to deliver maximum diversification for investors within equities and fixed income using its proprietary

'diversification ratio', which rebalances the weight of every stock in the tracked index to maximise diversification.

However, Choueifaty said periods of high concentration for stockmarkets, such as the tech bubble in 2001 and financials in 2007, which led to the global financial crisis, threaten the performance of highly diversified funds.

"Plenty of people have been right buying low volatility stocks in the US, they have outperformed a lot, but they became more and more expensive compared to where they were. And the more expensive they become, the more likely it is that this will result in a bubble," he said.



The CEO said the US market "has never been as concentrated as it is today", which is leading to underperformance on TOBAM's portfolios. Over one year to 4 November, the TOBAM Anti Benchmark US Equity fund is down 4.2%, while the S&P 500 is up 1.4%.

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In 2016, Choueifaty sees a bubble brewing in the 'nifty nine' stocks, which comprise Facebook, Amazon, Netflix, Google, Priceline, eBay, Starbucks, Microsoft and Salesforce. These represent a large part of the US stockmarket and contribute to increased concentration.

The allocation of the Anti-Benchmark portfolios to concentrated stocks is lower than the market and its peers, so it is not benefitting from gains on these stocks and therefore underperforms the market.

However, Choueifaty sees high concentration of sectors or stocks as the biggest risk to any portfolio and believes diversification should be the main aim of any manager.

He said: "Indices are naturally biased to what is expensive. They avoid what is cheap and this increases concentration and reduces diversification.

"One can reduce the risk of any portfolio by 20%-35% simply by being diversified. The Anti-Benchmark neutrally allocates risk to the effective independent sources of risk."

Choueifaty also argued against traditional passive investing, since these indices tend to be highly concentrated.

He believes that "if one cannot forecast, you should only diversify", which is the key aim of his Anti-Benchmark strategies.



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