High quality, cheap stocks – ANZ, Ansell

by Roger Montgomery

Is there anything worth buying?

If you like to get comfortable with a warm blanket or a glass of red (or perhaps both) before commencing your reading of the Switzer Super Report, today I am not giving you the chance. Today we ask the question on many investors' minds.

Let's cut straight to the heart of the matter. Experts have been telling us for some time that the market is expensive. The current circumstances however are a little more complex.

According to Ray Dalio, legendary founder of hedge fund giant Bridgewater & Associates, the prices of risky assets (shares) are high and the expected returns are low relative to traditional levels. But he adds, these aren't traditional times. Interest rates are at zero and liquidity is unusually high. Under those conditions, the stock market isn't displaying unusually stretched valuations. Cash returns are terrible and while investors aren't thinking about how much worse the loss of capital could be, there aren't many signs that they should be worried yet.

That said, other experts such as Jim Paulsen at US Manager Wells Capital Management notes that the P/E ratio of the median US stock is actually at a post war record high.

The bigger risk we believe is not an outburst of inflationary growth that causes the US Federal reserve to raise rates. No. The bigger danger lurks in US economic growth entering its seventh year, which as former US Treasury Secretary Larry Summers noted, is the "typical life-expectancy of recoveries."

When recessions have hit in the past, the US Fed has needed to cut rates by 3 or 4%. With rates at near zero, this is not an option.

Ray Dalio concurs "Additionally, in our opinion, inadequate attention is being paid to the risks of a [economic] downturn in which central bankers' abilities to ease are significantly impaired."

When QE was first announced many observers noted that the US was merely 'kicking the can down the road.' What Summers and Dalio are alluding to, is that the 'can' might be losing some of its momentum from that original kick.

The conclusion however might be that rates could stay low for some time and calls for US rates hikes later this year might be premature.

If that is the case then markets may stay supported for a time. One might reasonably expect the support to remain until one of three things happen. Those triggers could be rising interest rates, declining liquidity and/or investors turning their attention to a deteriorating economic environment.

So what are the companies that we reckon are high quality and cheap in the market today? I could of course produce a long hypothetical list but I could also simply go through those that we have backed with real money.

Here's the list in alphabetical order, followed by a quick description of each company. Do keep in mind that Montgomery funds own these shares and may have purchased at current, lower, much lower or higher prices. In short we are incentivized to see them rise, so please seek and take personal professional advice before transacting in any stock listed below.

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