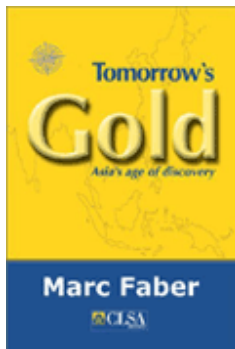


UAE stocks: a bear market rally or a new bull run?

When AME Info columnist Dr. Marc Faber appeared on stage in Dubai a couple of weeks ago he forecast a sharp rally in UAE stocks, and the market has duly obliged our guru from the Far East with a rally of more than five per cent last week alone. But can this upturn be sustained? Is it more than a bear market rally?



The classic investment book by Dr. Marc Faber

Perhaps it is appropriate to return to the learned text of Dr. Marc Faber's 2000 classic investment book 'Tomorrow's Gold'. Here he sets out the six phases of an emerging market business cycle in some considerable detail.

If you interpret the UAE in the 2000s in the context of this analysis then you can see where the future is most likely heading. Phase three of this cycle was clearly identifiable in 2005 with the UAE stock market bubble which peaked in November that year.

In phase four, Dr. Faber writes: 'After an initial sharp fall, stocks recover as foreign investors who missed the stock market's rise in phase one and two pour money into the market'. And he adds: 'It is not uncommon that foreigners increase their buying of stocks in phase four since they tend to be latecomers to the market'.

Foreign support

What supports this optimism? Again Dr. Faber has a list to hand: an economy that continues to grow, sharply declining interest rates, rising corporate profits or 'simply optimistic statements by business leaders and government officials'.

However, the cycle of investment expansion and contraction of emerging business cycles is well established. The UAE stock market correction has led to a displacement of local investment funds into real estate which now also has to undergo a cyclical correction.

A whole host of local analysts now see a real estate correction as imminent, from EFG Hermes to Standard Chartered Bank. And any correction in this sector will impact on the profitability of the quoted real estate companies which comprise a large component of the local stock markets.

Real estate correction

In these circumstances it is hard to see how the UAE stock market's current rally can be sustained for very long, and the knock on effect from a real estate correction will surely be to take the stock market down further. There could also be concern about the health of some financial institutions in such circumstances.

For the final signal that a stock market has bottomed out is usually that investors give up entirely on stocks, and this has just not yet happened, hence the current summer rally. Ironically, when investors do give up on stocks, like previously from 2000 to 2002 in the UAE that will actually be the best time to buy!

In the meantime, we have some summer madness and a chance for a few fleet-of-foot traders to make a quick turn. But just as Dr. Faber predicted the UAE stock market rally this summer his complete analysis puts it into a longer cyclical context which suggests that the market is not quite at the bottom yet.