Commentary January 1st, 2019

On December 18th, in the midst of the worst December for the stock market since 1931, (Financial Times December 22nd 2018) Chairman Jerome Powell announced that the Federal Reserve Bank would be raising its benchmark interest rate while signaling he expected additional raises in 2019, stating “this move is appropriate for what is a very healthy economy”. In response, the Dow Jones Industrial Average fell 800 points, demonstrating the dissociation between stock prices and the economy. (NY Times December 19th 2018) A market strategist asserted the stock market does not care if the economy is good or bad, but rather if it is improving or deteriorating. Market sentiment was very negative towards year-end 2018, and Chairman’s Powell comments, while sounding constructive, effectively amplified the doom and gloom forecast by analysts throughout the investment community.

Wall St. started 2018 strong, buoyed by a growing economy and robust corporate profits. Stocks climbed to new highs early, shook off a sudden steep drop by spring and rode a wave of positive feelings to another all-time high in September before jitters set in. Investors grew worried that the trade dispute between the U.S. and China and higher interest rates would impede the economy. A slower American housing market, lower sales of Apple IPhones worldwide and forecasts of weaker global growth in 2019 stoked anxiety. Bearish market analysts once again predicted the end of the bull market, contributing to the pessimism. What followed was an example of a self-fulfilling prophecy: a prediction of a falling market evoked behavior which in fact caused the market to fall. The S&P 500 Index, the market’s main benchmark, finished the year with a loss of 6.2%, the first time it fell for the year since 2008. The Dow Jones Industrial Average declined 5.6%, with the NASDAQ retreating 12.2%. (Wall St. Journal January 2nd 2019)

It was natural that all prognosticators of bad tidings would come out of the woodwork to project an impending recession once stock prices began their descent. Doom and gloom forecasts garner headlines and visibility, the primary motive behind a prediction in the first place. Forecasts are a form of marketing, and if the forecaster is correct, he will have made a name for himself. James Stack, a market strategist, was featured in a front page story of the NY Times for his prediction of a market in decline during 2018. (NY Times December 27th 2018) Most of us, however, are terrible forecasters, especially about the stock market. In a world constantly evolving, with new information and innovations changing the narrative on a daily basis, forecasting stock market performance is a frivolous endeavor. Investing with an eye towards forecasts typically generates awful results.

The data is, in fact, not so terrible. Due to the recent setback, the S&P 500 is trading below 15 times 2019 earnings projections, inexpensive on a historical basis. (Wall St. Journal January 2nd 2019) A drop in global growth from 3% to 2% should not be a reason for distress, as stocks have done well with an economy expanding at a 2% rate, and a weakening economy will discourage the Fed from further rate increases. Chinese officials appear set to offer a mix of concessions, including reducing tariffs on American goods, as they try to defuse trade tensions. Continuous expansion of the middle class in emerging markets provide consumer buying thrust for earnings growth worldwide. From a strictly technical perspective, stocks have declined for 2 consecutive years only twice since 1928, so another down year when most indicators are positive seems highly unlikely. (Barron's January 6th, 2019)

It is quite possible that your intended mix of stocks and bonds has drifted from its target allocation, and now would be a propitious time to rebalance. Investors make money buying into bear markets, not selling, although they need to be prepared to first lose money along the way.

We invite and encourage clients to contact us with questions and concerns and are available to meet at your convenience.