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Transitions

WHAT HAS CHANGED?

Only several weeks ago, the stock markets were careening lower. Even as an upward movement began, most saw this “V” as a short-term bounce. The technical thinking was that the market needed more time trading in the lower end of this trading range. The strength of the recent decline, combined with weakening breadth, had market sentiment feeling bearish. Most investment professionals were surprised by the market recovery.

An old Wall Street proverb was: *“As January goes, so goes the rest of the year.”* The reasons this saying remains a proverb is it doesn’t work reliably. In January 2018, the S&P 500 Index was up 5.6% in one month, while the market actually declined -6.2% for all of 2018. Even after the excitement of a January recovery, the market indices are now up slightly from where they were at the end of 2017.

What has really changed? The U.S.–China trade tensions continue; geopolitical standoffs continue; and there is a lack of political leadership from Washington as two large egos dominate decisions. Shutting down the government neither shut the government nor achieved much. If politicians need to shut down the government to achieve a policy, the shutdown pain of no paychecks must be felt by every politician and their entire staff. That is pressure where it counts. Only when decision makers and their advisors feel the pain, is there a need to act. Without this, government shutdowns become theatrical events.

The one noteworthy change is that the Federal Reserve has dialed back its monetary policy of more rate increases. Yet, if inflation picks up, they may resume rate increases to avoid reacting to an overheated economy, causing a future recession. Their needed changes in interest rates are bringing our economy from an artificial zero rate to a more

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normal interest rate environment, where investors are compensated for holding money markets and fixed income bonds.

The real change has been investor confidence. It is hard to imagine that within a few weeks, buyers moved from avoiding the market, to being momentum driven buyers. What if we really are in a trading range, with a minimal number of new 52 week highs or lows? Then the momentum investors are buying high, likely with cash received when they sold low. Investing is supposed to be the other way around, where one buys low, holds a position, and sells at higher prices at a much later date.

If this rally is only momentum driven, then waiting on the sidelines for lower prices makes sense. Yet it is also important to remember that investing in U.S. companies is not only about the future earnings of these companies, but the stability of the U.S. economy. Our strategy is to stay invested during a market correction and not sell out of good companies at a point in time when others are. As nobody can predict the future, also having cash on the sidelines continues to make sense as we navigate a maturing, decade old bull market.

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