CASTLE ROCK
WEALTH MANAGEMENT

Registered Investment Advisor Firm

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Reasons to be Bullish

Hopefully, you have been participating in the current run in the S&P 500. U.S. growth remains sound and sustainable, driven by the strong capital spending, rising productivity, tepid inflation and lower taxes.

Unfortunately, many investors haven't been jumping on the equity bandwagon. According to strategists, investors have pulled $91 billion from equity funds this year and $148 billion near the December 2018 lows. That's nearly a quarter of trillion dollars that missed out.

The question is, should investors take their gains and exit the market or should they stick with the rally and expect more gains?

History suggests the latter – stay bullish. Below are four different rationales supporting further gains in this market.

There is a 46% probability of a 20%-plus gain in 2019. Looking back at the annual S&P 500 returns in secular bull markets (1949-1968, 1982-2000 and 2011–current); a total of 46 years, in 21 of those years (46%) the gains surpassed 20%, with an average gain of 30.1%. That would push the S&P 500 above 3,250 in 2019. A secular market is a market driven by forces that could be in place for many years, causing the price of the particular investment or asset class to rise or fall over a period of time. In a secular bull market, positive conditions such as low interest rates and strong corporate earnings push stock prices higher. The data also shows that secular bull markets have never experienced two consecutive down years. On a historical basis, this makes it unlikely that 2019 will end in the negative column like 2018.

The strongest Q1 in two decades points to a surge higher. Since 1950, there have been only 10 times when the S&P 500 has been able to gain 10% or better in the first quarter. But that wasn't the end of the gains. In nine of the 10 cases, the market continued to gain even more. The median gain for those years was 21.6%, giving the market a goal this year of 3,050 for the S&P 500. The one case when the market closed below the Q1 gain was 1987. That year included the infamous crash and bear market in the fall. We experienced a bear market last year, and it would be unlikely for another bear market to occur so soon.

Historically, the third year of a presidential term is bullish. Going back 70 years and looking at the average gain from the midterm-election-year low to the pre-election-year high in secular bull markets, the average gain has been 48.9%. We hit the midterm-election-year low on December 24, 2018, when the S&P 500 dropped to 2,351. Add on the average gain of 48.9% and the high for pre-election-year becomes 3,500.

Market rallies following bear markets. Can we expect a 40% gain for the S&P 500 off the December 24, 2018 low? Going back 61 years and looking at 13 past bear market declines of over 19% for the S&P 500, the market gained on average 38.7% over the following 12 months. That would put the S&P 500 at 3,470 by year end 2019.

Although the four reasons point to different highs, what is important is that they point to highs above today's prices. History tells us that a market melt-up may be in the cards. "FOMO", fear of missing out, will come into play as overly pessimistic investors who have stayed on the sidelines may ultimately be compelled to put their cash back in the market, lest they be left behind.

A recent Barron's article questioned whether this expansion could last another 10 years. Savings rates are higher and indebtedness is lower than at any point since the mid-1990s. Americans are far less willing to boost their spending in response to rising asset prices than in the past. The job market also has room for improvement, with the employment rate of working-age adults well below its level in the 1990s.

The previous record expansion was from March 1991 to March 2001. The current expansion started in June 2009, another 10 years? I doubt it will happen. In April, 83% of chief financial officers surveyed by Duke University said they believed the U.S. will have entered a recession by the beginning of 2021. This could become self-fulfilling if companies cut their capital spending. Stay tuned.

If you need help with this market analysis or any other financial questions, contact me at (707) 648-2024.

FED Watch

At the April-May FOMC meeting, the FED held rates steady as expected and says inflation is "running below" its target of 2%.

The FED's decision not to change rates affirms the March FOMC meeting that economic projections signal no rate changes for the rest of 2019. In that meeting, the FED said low measures of inflation, concern over global growth and tightening financial conditions warranted pausing on interest rate hikes while policymakers reassess the data.

The central bank's statement reversed its March view that the economy had "slowed" from the end of 2018, noting that recent development showed that economic activity "rose at a solid rate".

The FED will continue the process of reversing the quantitative easing by allowing assets to mature off their balance sheets, rather than re-investing them and plan to taper this process and plan to complete by October of this year

Next meeting:
June 18th and 19th.

Castle Rock Wealth Management

Castle Rock Wealth Management is a Hybrid Advisory firm servicing the needs of clients across the United States.

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If you have questions or would like further information on this month's topics or any other financial or investment related subjects, please contact me by phone or through my email address at:
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