StraightTalk

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The Summer Doldrums? Only if You Read the Headlines!

The old adage, "sell in May and go away" gets trotted out every year as we enter the summer season. Given that this is a time of year when investors, advisors, traders, and even fund managers often plan and take their vacations – there is definitely some truth to the idea of the summer slowdown. In fact, statistically, three of the next four months rank as the bottom three performers for the stock market over the last 25 years. A BTN Research report on monthly returns shows that June is ranked 10th of all of the calendar months, September is ranked 11th, and August is dead last. It is worth pointing out that the average monthly return for those three months over two and a half decades is not so scary, an average loss of just 0.28%, according to that same report. While there have certainly been summer months with declines greater than that, if the potential for less than a half percent loss makes you alter your long term plan, then see me after class...

The question, of course, is will this year follow the trend of a quiet summer, or follow the trend of last year, when the S&P 500 gained 4.3% from June through September? Actually, as generational holders of the great companies of America and the world, this is not really the question at all. The real question is will we allow the relentless acid rain of the mainstream news media to shake us from our well defined plan and the diversified portfolio that matches our plan?

In the summer, when trading volume slows down, share prices can move more sharply on news items in the short run, which often only adds to the news narrative the following day. And although you each may be well versed in (maybe even tired of) the unwavering long-term focus of our conversations and review meetings – clearly the majority of the investors in this country are not, based on the evidence from the first quarter.

The first quarter – in case you have already forgotten it – contained the 10% correction we had all been waiting for, with the S&P 500 down a sharp 10.2% during February. A few of you called just to check in, and my advice was that our economy was just starting to pick up steam, and this downward price move would be short lived.

However, Credit Suiss reports that first quarter withdrawals of money from stock funds and ETFs was greater than $53 billion, with $48 billion of that occurring in February alone. Almost all of that money went into bond funds and ETFs, roughly $47 billion, according to the same research report. In other words, in the middle of one of the strongest bull markets in the last half a century – after a routine, normal, and slightly smaller than historic pullback – investors pulled more money from stocks in any month since 2008! And where did they put those dollars, you ask? Why, into bonds, which have gone exactly nowhere since that pullback, while the stock market…you guessed it, has recovered the dip and is flirting with all-time highs once again.

The message here is that, as Hugh Grant said to Julia Roberts about unfavorable news coverage in the classic movie, *Notting Hill*, "Can't we just forget about all this? Today's newspapers will be lining tomorrow's waste paper bin." This pithy line is true, but as we all know, tomorrow there will be another scary headline. In fact, the toxic levels of negative news washing upon our shores each day seems to be increasing, rather than reporting the strong economic realities we are enjoying today.

Frankly, it is hard to concoct a better scenario for portfolios with meaningful exposure to

stock markets than what we have presently. At every turn, the economic news is good and getting better. Unemployment hit 3.8% in the month of May. Would anyone like to guess the last time that our economy saw that number? It was back when Neil Armstrong was walking on the moon. But, rather than celebrate this excellent economic news, the headlines are ablaze with stories either about how this will lead to inflation, or that the number is not actually the number.

Regarding the latter, the naysayers will point out that the unemployment number does not capture those who have dropped out of the labor force and are no longer looking for work. This is true, although the group that has given up is much smaller than it was five years ago. The other side of this data point is that the unemployment number also does not catch those who have left the labor force and have become self-employed. The number of part-time, work from home, gig economy jobs has exploded from just five years ago with opportunities like Uber, Lyft, Airbnb, Taskrabbit, and hundreds of others offering a way to earn income that is not captured in the employment data. If you have ever had a child babysit, or sell lemonade from a stand, or seen a neighbor's kid mowing lawns for money – none of these jobs are in the employment numbers, and there are hundreds of thousands of them for adults in our economy today. So, one could actually make the argument that our real unemployment is even better than the 3.8% headline number.

Another news item that you should see everywhere but aren't, is that the Atlanta Fed now predicts the economy will grow above a 4% rate in the second quarter. There were many news outlets that mocked the idea of 4% growth during the last election cycle….I wonder how many of them will admit they were wrong? This economic growth is happening not just in one or two sectors like technology or energy, but across the entire economy. Speaking of which, our economy is now poised to pass the $19 trillion dollar mark shortly, and the companies that make up our economy are in great shape, as measured by sales, book value, cash on the balance sheet, or earnings.

And speaking of earnings, according to Federated Investors, during that same quarter that the rest of America was panicking out of stocks in favor of bonds, the earnings of the biggest 500 companies in the country rose by 25% compared to the prior year. The first three months of this year was the fourth consecutive calendar quarter with double digit growth in corporate earnings, and the second quarter should extend that streak further. So, three quarters of all public companies beat the increased earnings expectations by more than 7% in the first quarter, but all of the headlines were about a 10% price drop that has already come and gone! Those higher earnings? They're still here…

In late April, the Commerce Department released an economic report that showed business investment was up 6.1% in the first quarter, and has now averaged a staggering 6.3% for the last five quarters. That number for all of 2015 and 2016 was 90% lower, averaging just 0.6%. Business investment is a forward looking indicator of future growth in productivity and wages, and it has clearly exploded since the election. If you missed this critically important data point in the daily tsunami of negative news coverage – don't worry, you are not alone – good news like this tends to get pushed far down below the salacious headline of the day.

Luckily, the optimism for corporate America has not gone unnoticed by those in it. Becky Quick, who is a morning anchor on CNBC, recently pointed this out on Twitter. She tweeted something from J.P. Morgan's CEO, Jamie Dimon, widely regarded as the smartest banker on all of Wall Street. She tweeted "Jamie Dimon says the U.S. economy is in the 6th inning." Immediately afterwards, Warren Buffet added "We have our sluggers coming up to bat right now, numbers 3, 4 and 5 in the line-up." Even if we do have some summer doldrums – if those two guys think we're in a great place in this bull market cycle, who am I to argue?

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