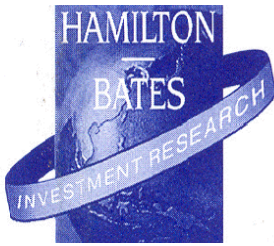

Hamilton-Bates

Market Update

April 8, 2019

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The market maintained its strength through the end of March and into April, with money flowing into stocks during the quarter-end window with a flourish. The U.S. market had its best quarter in over a decade. Of course it comes on the heels of one of the worst quarters in a decade—but we'll take it. The major averages managed to recoup some modest mid-March losses thanks to those aforementioned flows, with the major averages hitting new recovery highs into April. However, the allocation-window that historically occurs around quarter-end should now be largely completed, and once again economic and corporate news-flow should be back in control.

We are also entering into earnings season, although we are still a few days away from the kick-off, but with the market back to within a whisker of its all-time high, the bar has been raised considerably from where we were last quarter. The market's rise is a reasonable indication that expectations are for another solid year for corporate earnings. It seems as though the twin troubles that ailed the market last year—a tightening Fed and a trade war have been removed (although the latter is still open to question). We maintain that there are some concerns that remain, namely the inversion of the yield curve (more on that in the next Update), and the continued weakness in the housing market.

Gains for the market are nearly always 'good', but as far as gains go, it was far from an ideal week. There is a price gap left behind with last Monday's strong open (gaps tend to get filled in), and the buying volume deteriorated during last week's rise. It seems there are fewer and fewer buyers the higher the market goes. If that continues it would become a concern. Even if the market succumbs to a short-term correction, the market structure and Fed flip flop leave the bull back in place.

Economy, Earnings, and Interest Rates

The economy as a whole seems to be recovering from a December stumble, although Retail Sales came in weaker than expected once again. Whether this weakness is the start of a long-term trend or just a retrenchment from record levels will dictate how the economy fares in the latter half of the year. To be clear, the year-over-year figure of retail sales still shows growth - just at a slowing pace. There's also a possibility that, like January's shocking setback, the data read could have been misleading. Even so, the consumer spending data doesn't jibe with the still strong employment and sentiment data.

We also got the ISM data last week. The ISM services index fell from 59.7 to 56.1, while the ISM manufacturing index inched up from 54.2 to 55.3 for March. Both ISM levels are trending slightly lower over the past few months, but remain well above the 50 level which denotes expansion. We also got March's auto sales last week, and they were a welcome sign of strength. Car sales perked up, and truck sales jumped to a record-breaking annual pace of 12.392 million. The combined annualized rate perked back up to 17.45 million. That's back to the stabilized levels seen near the end of last year.

Finally we got the March jobs report on Friday. The knee-jerk reaction to the most watched numbers were well received, and understandably so. But, digging beyond the headlines reveals some concern. The number of employed people fell, and the number of unemployed people grew. The labor force participation rate as well as the proportion of the population actually both fell. Even so, nonfarm payrolls grew by 196,000, reversing February's lull, and the unemployment rate held steady at a multi-year low of 3.8%. With a weak report in for February, and now a so-so one for March, April becomes a swing month to show the economy is still on track.

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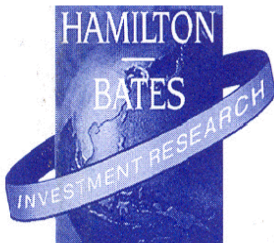

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Market and Investment Outlook

As was noted already, last week's solid gain (about 2.0%) was a nice follow-through on the previous week's rebound effort. But, stocks are now back to an overbought condition, and running into resistance from the highs of 2018 (between 2850-2900 on the S&P 500). The rebound since December has been phenomenal, but the nearly 60 degree upward slope is not likely to be maintained. The S&P 500, for example, is now up more than 23% from its late-December low. It is also 7.4% above its 100-day moving average, which is very extended above trend, and suggests some short-term pullback is likely. But while the trend should flatten out, we still look for higher levels in 2019.

Given the renewed uptrend along with extended short-term conditions the most plausible outcome here, given long-term history, is a modest pullback and the renewal of the bigger-picture uptrend at a more sustainable pace. But we wont' make any assumptions about what any one week holds. The prospect of an end to the tariff war with China could easily fan the flames and drive higher highs. We saw stocks become more overextended than they are now in late 2017 and early 2018, and that could continue.

Either way, September's high of 2940 is a key psychological ceiling, and the 200-day line (red line) currently at 2757 is the most important floor right now. We look for some flattening of the 'V-shaped' move off of the December lows, and look for some consolidation which is very possible in Q2. Our longer-term outlook suggests the DJIA and S&P 500 will clear 30,000 and 3000 respectively (and by a good margin) before the rally runs its course.

S&P 500 Long-Term Chart

The S&P 500 decisively cleared first resistance around 2800 in late March, and although its not shown, the 50-day moving average has closed back above the 200-day average—triggering the so-called 'golden cross'. This bullish configuration has lead to further gains six months later 7 of 8 most recent cases. The intermediate-term market trend has been reversed back to 'up'. We look for further gains in the back half of 2019.

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