Hamilton-Bates
Market Update

May 22, 2019

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Sell in May and Go Away?
A hitch in the trade talks with China finally triggered the pullback that had been overdue. The market had virtually priced in that a trade deal was all but done, but when China changed some terms on the final draft, the US balked.

After a blistering rally from the December low some sort of pullback was clearly due. Whether it was the trade-deal or something else, there would have been a trigger. The market had been up nearly 25% from the 2018 lows heading into May, so a 5-7% pullback really should not be a shock to investors.

Sell in May is an ‘old stock market saw’ that suggests the summer months are likely to see weaker than usual markets, or a low volume market, so its better to sell and go away to enjoy the weather. We are not sure the entire summer will be weak, or even low volume, but a May-June pullback that reloads the market for the second half of the year seems the most likely case right now.

Economy, Earnings, and Interest Rates
GDP growth for Q1 came in over 3%; Q2 is expected to slow to the 2% level, but there are some concerns that the economy could weaken rapidly if the trade deal and relief packages for key industries (farming, housing, autos) weaken further from current levels. Since we really don’t export much to China other than food, its our beleaguered farmers that are already struggling with flood conditions in the Midwest that will suffer the most. Failed farms could lead to food inflation/stagnation down the line.

Housing is another sector we have concerns about, as even with lower rates since December activity and pricing in this key area have been weaker. If housing continues to remain weak it would be a major red-flag. The auto sector is also and area we are watching, but its not SALES so much as the auto loans themselves. What we are seeing is a jump in defaults on used car loans to levels not seen sine 2009. People need their cars more than their house, since its usually their means of transport to a job. The softness in the housing and auto areas tell us the economy is more **fragile** than the current growth rates suggest, and that if things turn really ugly with China, a deeper than expected slowdown could happen fairly quickly.

Market and Investment Outlook
As of yet the stock market is undergoing a normal correction, but given our concerns over the key sectors mentioned above, and the fact that the trade deal has seemingly been put on hold for some time–we’ll be watching to see how resilient the market is to this weakness. Big sell-offs like last Fall start out like any other ‘normal pullback’, but seem to snowball. We are watching key levels for signs the selling could indeed snowball.

Some accounts already had increased cash levels from Tactical sells in early May, and with recent weakness in Small-Caps and International Markets, additional cash has been raised from sales and repositioning. We also added to corporate bonds, which are benefitting from the fact that a rate hike in 2019 is looking highly unlikely. In fact the next move is likely a cut.

So far the market is suffering through a normal pullback. Could it develop into something more—certainly. But we’ll et the market provide the answer to that question, an answer that depends on how the market reacts and how investors respond. Weakness below 2800 on the S&P would suggest a defensive posture on stocks is warranted for now. We still believe however that the bull market is not over—and we expect to see the DJIA above 30,000 and the S&P 500 well above 3000 before its all said and done.

The market is closed for the Holiday on Monday, and volume is likely to slow as the week moves along. Be safe and enjoy the Memorial Day weekend.

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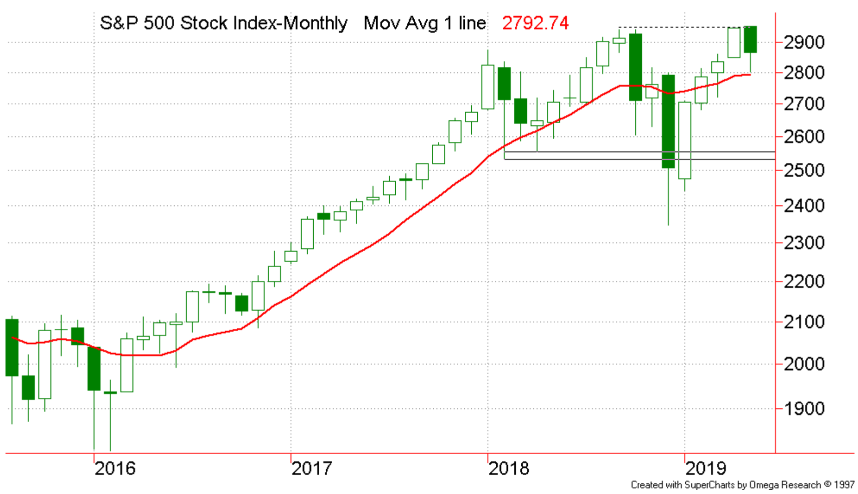
Key Market Charts

S&P 500 Near-Term: The S&P 500 stalled in the area of the 2018 peak, and has broken below its 50-day average (red line**).** The recent rebound was not able to move above this level, and further corrective activity may be needed to recharge the bulls batteries**. As long as key support in the 2750-2775 area (the 200-day average in yellow) is not broken, we see the pullback as constructive.**



S&P 500 Long-Term: Looking at a longer-term chart of the S&P 500 gives us some perspective. You can see clearly the pause at the 2018 high, with the MONTHLY bar now showing a potential reversal pattern. The market needs to hold above 2750-2800 on the S&P to maintain near-term upside momentum. A drop and close below the 10-month average (red line) would be a strong negative sign.