Rochester Financial Services

Fee-Only® Financial Management Services

Jeffrey Feldman Ph.D., CFP
Certified Financial Planner
Principal

July 4, 2017

Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Gold	Crude Oil
21,479	2,429	6,110	1,427	2.35%	5.44%	$1,219	$47.07

Investment Strategy Report

Trying to Read the Market As Stocks Head Into the Second Half

The first half numbers are in the books and investors thus far have nothing to complain about. For the first 6 months of the year, the US stock market, as measured by the S&P 500, was up 8.3%. For those analysts who back in January predicted a typical annual return of 10% for US stocks, they have to be pleased with almost achieving that goal in the first 6 months.

However, the real stars of the first half were technology stocks, as the growth heavy Nasdaq was up 14.1%. Stocks like Apple, Amazon, Netflix, Google, and Facebook put in strong performances as investors looked to companies with strong earnings momentum to lead the way. Healthcare also did well in the first half returning 15.1%, recovering from a weak performance in 2016.

On the flip side, the laggards were led by the S&P energy index which was down 13.8%. With the price of a barrel of oil falling from the mid 50's to the low 40's during the half, energy stocks could not get any traction. Another underperformer were the financials which were up only 6.0%. At the beginning of the year, these companies were hopeful that rising interest rates would help to increase their profit margins and thus boost their stock prices, as they were already selling for very attractive valuations. However, interest rates, as measured by the 10 year Treasury yield, which began the year at 2.45%, fell through the first half, hitting 2.14% last Monday (6/26).

We are now 6 trading days past that low in interest rates and today, the 10 year Treasury yield sits at 2.35%, with a large 20 basis point increase. This rise in rates has been accompanied by a spike of 4.2% in financial shares. Energy shares have also rebounded, moving higher by 3.2% this past week as the price of oil has stabilized and has begun to move higher. In contrast to those sectors that are rebounding, we have seen the fortunes of tech shares reverse course during those 6 days as the Nasdaq has fallen 2.2%.

Whenever we move past a calendar milestone, whether it's a new year or a mid-year mark, it's always a question of whether the trend currently in favor will continue to do well, or whether a changing of the guard will occur. And if a change does occur, the question then always becomes, is it just a temporary move, or a true change in market direction.

That is the question that we are faced with now. Is the strong momentum in growth stocks over and is it time for value (e.g. financials) to take over the leadership role? Or will the strong earnings growth that we've seen with tech stocks be enough to continue pushing those shares higher?

And as is often the case with investing, there may not be a clear cut answer, as either both growth and value could do well, moving all stocks higher, or the sector rotation could be a prelude to a looming general stock market correction. These are the issues that I will be watching in the coming weeks, to see whether I need to make changes to our portfolios. For those of you concerned about the possibility of a large scale correction, my feeling is that that is not in the cards. Corporate earnings reports have been strong and the economy is doing well.

There might be a larger concern about technology companies, with stocks like Tesla, Amazon, and Netflix selling for stratospheric valuations. However, the core tech companies like Apple, Facebook, and Google are all selling for very reasonable valuations given their rapid growth rates. This mini correction that they have been going through should not last very long. And if the rotation into the financials and energy stocks continues, then the market could very well see both growth and value sectors move it higher. *Jeff Feldman*

Tel: 585 / 442-7580
Fax: 585 / 351-2458
Email: jmfeld@aol.com

7 Hastings Circle, Pittsford, NY 14534
http://www.rochesterfinancial.com

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