Rochester Financial Services

Fee-Only® Financial Management Services

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Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Gold	Crude Oil
21,206	2,439	6,306	1,405	2.16%	5.44%	$1,282	$47.74

Investment Strategy Report

This Market Just Wants To Go Higher

Stocks scored a trifecta yesterday (Friday) as all three major indexes, the Dow, S&P 500, and Nasdaq, finished at all time highs. And this occurred following a weaker than expected May jobs report released yesterday morning that showed that only 138,000 jobs were created last month vs. the expected 185,000. No matter what gets thrown at this market, it seems to shrug it off and move higher. The S&P 500 broke out to a new high on May 24th and has continued to power higher ever since.

What makes this achievement that much more impressive is that just a week before this breakout, on May 17th, stocks got slammed, with the Dow dropping 373 points, its biggest drop in 8 months. This drop was the result of word that President Trump had asked FBI Director Comey to stop the investigation of former national security adviser Michael Flynn. Talk of obstruction of justice and impeachment began to be heard and a headline in CNN Money read "Is Wall Street Finally Getting Ready to Throw in the Towel on President Trump?". Nervous investors who didn't understand why stocks kept on rising took this as an opportunity to sell, to lock in profits before the sell-off could get any worse. However, those investors have lost out, as the S&P now sits 3.5% higher. The Nasdaq has been on fire as tech stocks, exhibiting outsized growth prospects, have outperformed. This index has recovered 4.9% since the May 17th sell-off.

Puzzled investors are at a loss to explain how stocks can continue to move forward despite all the turmoil in Washington and the unpredictability of our new president. The answer is that the US economy is doing quite well, and good earnings and the prospects for stronger earnings in the future are what drive stock prices higher.

Steve Sjuggerud (StansberryResearch.com, 5/26) points out that the Index of Leading Economic Indicators is in a significant uptrend and just hit an all-time high. "Historically", he says, "recessions tend to happen after these leading indicators start a downtrend. This index began to fall before every major recession since 1970". The strong uptrend gives the economy the "all clear" sign.

I have written before about how we have seen a surge in optimism since the election, both among consumers and businesses. For the first time in years, companies are beginning to invest more of their cash in their businesses (capital expenditures), setting them on course for increased earnings. In the past, companies were discouraged about the economy and used their excess cash to buy back their stock instead of in capital expenditures. This has now begun to change.

The rise in consumer sentiment also points to a continuation of this bull market. The Stansberry Digest (6/1) reports that a recent Morgan Stanley study states that "the US is currently in a bullish period of "elevated and stable" consumer sentiment, and this level of optimism is very bullish for stocks".

Other potential tailwinds for the economy would be a reduction in taxes as proposed in the President's tax plan, possible new infrastructure spending, a still strong housing market, a weaker dollar that will benefit multinationals, and coordinated global growth for the first time in many years. And for those who think that the market valuation is reaching lofty levels, keep in mind that 1) rising earnings will keep the P/E levels reasonable and 2) low to stable interest rates will justify higher P/E multiples. Once again this year, investors began the year fearing the prospect of rising interest rates. 2017 began with the 10 year Treasury yielding 2.45%. Since peaking in March at 2.61%, the 10 year yield has since fallen, closing yesterday at 2.16%. With interest rates continuing to hold to historically low levels, bonds alter no real competition for stocks, as investors continue to seek the higher returns of equities. *Jeff Feldman*

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