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
20,042	2,291	5,659	1,367	2.41%	5.67%	$1,237	$53.03

Investment Strategy Report

The Dow Breaks Through 20,000. Will Gains Spread Globally?

Stocks got off to a great start this year, as they shrugged off the January blues of the previous 2 years and began moving higher from the start, continuing the post-election surge. On Jan. 6th, the Dow hit a high of 19,999.63 but couldn't close the deal, finishing the day at 19,964. For a while it seemed that 20,000 would be a ceiling and possibly a signal to take profits, as the markets struggled for the next 3 weeks. However, on Jan. 25th, the Dow shot up 155 points to a record close of 20,069, proving that it still had some firepower left.

When the average investor sees the stock market averages hitting all-time highs, the natural reaction is to take profits. After all, how high can the markets go? "I'd rather sell now and lock in my recent profits than to see my gains evaporate". However, the analysts at Stansberry Research say that the opposite strategy produces better returns. On Nov. 25th, Steve Sjuggerud wrote "You REALLY want to own stocks after a new 12-month high ... And you really DON'T want to buy stocks after a new 12-month low". The data shows that since 1928, stocks returns on average 7.3% in the year following hitting a 12 month high but only 2.8% after hitting a 12-month low. Over all periods, the 12 month return was 5.1%. Since Steve wrote that, the Dow is up another 900 points.

Well, what about the argument that stocks are expensive, that their P/E ratios are higher than historical norms? Here too Sjuggerud does not see valuations as a reason to sell stocks. With the S&P 500 approaching 2,300 and a current earnings estimate of about 130, that puts the P/E ratio at about 17.5, slightly above average. However, he notes that P/E ratios need to be assessed in connection with interest rates. With our current abnormally low interest rate environment, P/E ratios would have to rise well above 20 before he would consider the market overvalued. Add to this the fact that economists are busy revising earnings estimates higher in light of the new economic optimism that has taken hold. If the S&P 500 achieves earnings closer to 140, that would make stocks that much more reasonably priced.

In this weekend's Barron's (2/6/17), another top analyst, Ed Yardeni of Yardeni Research is interviewed and was asked about the surge in stocks since the election and whether this was a blowoff top. His response: "It would be a mistake to bet against what President Trump might accomplish. We could get substantial tax cuts. You could get $1 to $2 trillion coming back from overseas ... that would be very powerful in terms of keeping the market up". "Nov. 8th (Election Day) was an extraordinarily important day, a major inflection point. It was a radical regime change. We concluded that earnings growth could be closer to 20% than 10%". His analysis indicates that S&P 500 earnings this year could be at $142, up from $128 last year. He then added that with a P/E ratio of 17.6, we could get to S&P 2,500 by year end.

With all this optimism about the US, what does this mean for investing abroad? Without question, the US has been the place to be for the last 5 years as the US stock market has substantially outperformed both developed and emerging markets overseas. As this outperformance has continued, this has made foreign markets that much cheaper in comparison to ours, tempting many investors to take advantage of this disparity. Up until now, investors have only been disappointed. Last year seemed to be a good one for foreign stocks at first. Then came Brexit which torpedoed European stocks. And emerging markets, which had been leading for much of the year, got crushed the last 2 months of the year as a resurgent US market led to a stronger dollar, a death knell for emerging market countries.

However, things seem to be changing. The rise of the dollar has stopped and emerging markets are getting off to a good 2017. Steve Sjuggerud has just declared that now is an ideal time to begin investing there. During the next few weeks, I will be reviewing our portfolios and may begin adding these funds to your accounts. Adding European funds might be next on my list. *Jeff Feldman*

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