Rochester Financial Services

Fee-Only® Financial Management Services

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October 3, 2019

Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Gold	Crude Oil
26,201	2,911	7,872	1,486	1.54%	5.79%	$1,511	$52.31

Investment Strategy Report

Will Weak Economic Data Sink Stocks?

After a weak month of August, investors were fearful that September, seasonally the worst month of the year for stocks, could only lead to more trouble. However, stocks managed modest gains in September, with the S&P 500 gaining 1.6%. Good economic data was enough to bounce stocks higher, although not good enough to send prices to record levels. After large gains for the first part of the year, stocks were treading water.

However, while stocks made it through September unscathed, the first 2 trading days of October were another matter. The Dow dropped 343 points on Tuesday (10/1) and another 494 points on Wed. These drops came as a reaction to the release of weak manufacturing data, which pointed to the steepest contraction in the manufacturing sector since June 2009. Then earlier today, the release of the service sector data was also much weaker than expected. This sent the Dow down another 340 points by 10:10 am, 10 minutes after the release of the data.

However, the selling didn't last. Stocks reversed course and ended the day substantially higher, with the Dow, S&P 500, and Nasdaq higher by 0.5%, 0.8%, and 1.1%. It appears that the market had gotten oversold and sentiment had become overly negative. The stock market was due for a bounce. But will the bounce last or will weak economic data continue to drive stocks lower.

Part of the answer will come tomorrow morning (10/4) at 8:30 am when the September Jobs report will be released. Investors are hoping that a strong report will allay fears of a slowing economy. However, a weak report might not spell doom for stocks since a low jobs number would encourage the Federal Reserve to be more accommodative, a plus for the stock market.

The bigger question, though, is not what stocks will do in the next few weeks, but whether a recession looms for 2020. That would be a big negative for the stock market. In Bob Brinker's October newsletter, he reviewed his 5 recession indicators in order to evaluate the risk of a recession. Of the 5 indicators, only the inverted yield curve is a cause for concern. He is still projecting GDP growth of approximately 2% for 2020, not negative growth which is the definition of a recession. He is also projecting S&P 500 earnings of $175 per share for next year, which together with a P/E ratio of 18 would result in an S&P price "into the mid-to-upper 3100s range". That would be an 8-9% increase from today's price.

Jim Cramer argues that part of the reason for the weak manufacturing data is because of a) the trade war with China, 2) the GM strike, and 3) the problems with Boeing's 737. Any resolution to these issues could result in a rebound in the manufacturing sector.

Fritz Meyer (9/10) argues that manufacturing is only 10% of the economy. Consumer spending, which comprises 70% of the economy is still strong. He continues that with companies such as Target, Walmart, and Home Depot all recently at record highs, the chances of a recession are low.

It appears that while the economy is slowing, we will not sink into a recession any time soon. Interest rates at such historically low levels will act to stimulate the economy. Money flows will be directed towards stocks, with their high dividend yields vs. low yielding bonds. I would surmise that a combination of trade wars and political drama are acting as a drag on rising stock prices. Any resolution in these areas should help to get the bull market back on track.

Required Minimum Distributions (RMDs) – For those of you over 70½ or who have inherited IRAs, it's time to take your required IRA distributions. I will be contacting you shortly if you haven't yet taken care of this. *Jeff Feldman*

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