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
24,103	2,641	7,063	1,529	2.74%	5.87%	$1,331	$65.12

Investment Strategy Report

Has Market Correction Played Itself Out?

The stock market's rough ride continued into March, as the no-longer tranquil market continued its nauseating gyrations. The fireworks first began on February 2nd when we witnessed a market collapse that lasted until the morning of Friday Feb. 9th. That 10% drop was then followed by an equally dramatic market recovery, which saw a 10% rebound that topped out on March 9th. The rally then stalled for a few days before resuming the next leg down, which took the S&P 500 down another 7%, to 2,588 on March 23rd.

As market technicians watched this play out, it all seemed to be following a standard script of typical market action. When the S&P 500 bottomed the morning of Feb. 9th, it found support at its 200 day moving average. It then rallied – as many technicians "expected". However, a common technical occurrence is the "retest", i.e., a situation in which the stock market needs to retest the lows of the previous down leg before it can resume its march higher. That level of 2,588 that the S&P closed at on Friday, March 23rd, was exactly at its 200 day moving average. This setup made the market action last week (the week of 3/26) critical for the status of the market uptrend. If stocks could move higher from this critical level, then the retest could be called successful. However, if stocks continued their decline last week, then the retest would have failed and the decline was set to worsen.

On Monday March 26th, the Dow rose 670 points, the third highest point total ever. True, it dropped 345 points the next day but it did manage to finish the week with a 250 point advance on Thursday. The S&P 500 is now 53 points, or 2% higher than its 200 day moving average. It is, of course, too early to sound the all clear signal for this bull market, but we have definitely cleared some hurdles during the past few trading days.

Meanwhile, the fundamentals of the market seem to give us more reasons to be optimistic. Steve Sjuggerud points out in his 3/29 column (StansberryResearch.com) that even after 9 years of this bull market, stocks are still not expensive. This is due to 1) the recent correction, which caused prices to drop about 8% from their highs, and 2) corporate earnings growth, whereby the earnings of companies in the S&P 500 are projected to grow by 27% over the next 12 months (due largely to the tax cuts). This combination of lower prices and higher earnings has caused the market's Price to Earnings ratio (P/E), a standard measure of market valuation, to fall to a very reasonable level, basically to its historical average. This gives the market room to move higher, as it is now sitting at the P/E level that it was at in March 2016.

There is also a general consensus among market analysts that a harbinger of bear markets, an economic recession, appears to be nowhere in sight. Last month's employment report showed that a very substantial 313,000 new jobs were created in February. A strong employment picture is an indication of a very healthy economy. In addition, other economic indicators are also pointing to economic strength. The Index of Leading Economic Indicators continues to move higher and consumer confidence and business sentiment indicators are still very strong. These indexes are leading indicators and tend to decline in advance of recessions. Their strength points to a low probability of a recession during the next 6 to 12 months.

One market development that I will be watching carefully is the performance of technology stocks in the days ahead. Shares of Facebook got walloped the past few days as news broke about user information being compromised. Shares of Amazon have also suffered, this time as President Trump targeted the company for not paying their fair share of taxes. Growth companies in general and technology companies in particular have been the market leaders during the past year. While these companies are experiencing excellent growth rates, we always need to be on the lookout for a change in market leadership. It may be time for value stocks to take charge for a while. *Jeff Feldman*

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