November 4, 2019

Weekly Viewpoint

Stocks Continue to Climb the Wall of Worry

Performance for Week Ending 11.1.19

The Dow Jones Industrial Average (Dow) added 1.44%, the Wilshire 5000 Total Market Index[SM] (Wilshire 5000[SM]) gained 1.38%, the Standard & Poor's 500 Index (S&P 500) finished up 1.47% and the Nasdaq Composite Index (NASDAQ) tacked on 1.74%. Sector breadth was positive with 8 of the 11 S&P sector groups finishing higher. The Healthcare sector (+3.04%) was the best performer followed by Technology (+2.05%) and Industrials (+2.04%).

Index*	Closing Price 11/1/2019	Percentage Change for Week Ending 11/1/2019	Year-to-Date Percentage Change Through 11/1/2019
Dow	27347.36	+1.44%	+17.23%
Wilshire 5000	31262.57	+1.38%	+21.41%
S&P 500	3066.91	+1.47%	+22.34%
Nasdaq	8386.40	+1.74%	+26.39%

Market Observations: 10/28/19–11/1/19

The S&P 500 finished higher for a fourth consecutive week after the Federal Reserve lowered rates for a third time this year, payroll data came in much stronger than expected, the wobbly manufacturing sector showed signs of stabilizing, and third quarter earnings reports continued to trend at a better than feared pace. The S&P and NASDAQ both finished the week at new all-time highs.

Fed Cuts Rates Again: As was widely expected, the Federal Reserve reduced rates for the third time this year. The central bank lowered its benchmark interest rate by a quarter-point to a range of 1.50%-1.75% and signaled that it would likely refrain from cutting rates further in the near future. The post-meeting policy statement removed a pledge that the Federal Open Market Committee would "act as appropriate" to sustain the expansion, a phrase that had become synonymous with readiness to lower interest rates amid escalating trade wars and a global slowdown.

Instead, the Fed said that it would "continue to monitor the implications of incoming information for the economic outlook as it assesses the appropriate path of the target range for the federal funds rate." During the after-meeting press conference, Fed Chairman Powell emphasized the US economy's longer-term challenges and noted that it would take a lot to push the Fed to consider raising interest rates again. Overall the comments out of the Fed and Powell seemed vague enough to leave the door open to additional cuts, although the bar has certainly been raised.

Economic Round-Up: While there is no arguing that economic growth has cooled, the forward path still looks more like a “muddle through” environment than outright contraction. Last week, the Labor Department reported that nonfarm payrolls expanded by 128K during the month of October, solidly ahead of the 85K forecast by economists. In addition, the September payrolls data was revised upward to 180K from the initial estimate of 136K. The unemployment rate during October ticked up to 3.6% (from 3.5%) while wages grew at a 3.0% year-over-year pace. Meanwhile, the Commerce Department reported that the initial estimate of Q3 GDP showed the economy expanding by 1.9%, ahead of the 1.6% growth forecast by economists but down slightly from the 2.0% pace in Q2. Personal Consumption rose by 2.9%, ahead of the 2.6% estimate. Core PCE—the Fed’s preferred inflation barometer—gained 2.2%, up from 1.9% last quarter.

Q3 Earnings: On the earnings front, third quarter earnings season continues to trend at a “better than feared” pace. Of the 358 S&P 500 companies that have released results (through Friday), nearly 80 percent have met or exceeded expectations. Earnings growth has been on the weaker side (aggregate growth is off 1.3 percent), but still ahead of the 2.7 percent decline currently forecast by FactSet Research.

Market View: We maintain a tactically cautious view on the near-term market outlook reflecting the strong year-to-date gains and worries that the still unresolved trade war with China could continue to weigh on business sentiment. While we are not bearish on the market, we feel the current risk/reward outlook is not particularly attractive. The strong year-to-date performance has been driven almost exclusively by the expansion in the market’s P/E multiple, which in turn, leaves the market vulnerable to negative developments on trade and political risk. Earnings growth will need to be the key driver of forward performance and until revisions begin to move higher, upside from current levels will likely be limited. Better buying opportunities are likely to emerge down the road, but now is not the time to be chasing the market higher.

The Week Ahead: Earnings season will begin to taper off this week with 86 members of the S&P 500 Index scheduled to report results. Highlights of the data calendar include; September factory orders, the October Institute for Supply Management’s (ISM) non-manufacturing index, the September JOLTS report, the preliminary estimate of third-quarter productivity and costs, and the University of Michigan’s November consumer sentiment survey. Fed Heads will be out in full force with eleven presentations scheduled throughout the week.

Definitions

The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally defined as the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Wilshire 5000 Total Market IndexSM represents the broadest index for the U.S. equity market, measuring the performance of all U.S. equity securities with readily available price data. The index is comprised of virtually every stock that: the firm's headquarters are based in the U.S.; the stock is actively traded on a U.S. exchange; the stock has widely available pricing information (this disqualifies bulletin board or over-the-counter stocks). The index is market cap weighted, meaning that the firms with the highest market value account for a larger portion of the index.

Standard and Poor's 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Nasdaq Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.

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