"What Causes Moves In The Market?"

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Geopolitical uncertainty didn't dent U.S. stocks last week. Geopolitics is the intersection of geography, economics, and politics. Last week, there were some fine examples of the ways geopolitical events can create uncertainty. *Barron's* reported:

"President Donald Trump began the week suggesting that a trade war with China was on hold, before later ordering his administration to explore penalties on imported automobiles. The president also canceled talks with North Korea. Italy's bond market melted down following the emergence of a Euroskeptic government, while Turkey's lira tumbled over concerns that President Tayyip Erdogan would take control of its central bank, raising concerns about emerging markets."

Uncertainty caused major indices across Europe to finish lower last week. A majority of Asian-Pacific indices moved south, too, as did Canadian and Mexican indices. Despite pessimism elsewhere, investors in the United States remained unfazed and major U.S. stock market indices finished the week higher. The Standard & Poor's (S&P) 500 Index was up 0.3 percent.

The strong performance of U.S. markets last week was remarkable because the S&P 500 moved higher on news that would seem to inspire uncertainty. It was also remarkable because U.S. stocks gained less when S&P 500 companies reported first quarter profits were better than expected.

First quarter's earnings season – when companies report how profitable they were during the first quarter – is almost over. A majority of S&P 500 companies did better than expected, according to *FactSet*. However, companies with stronger than expected earnings saw share prices increase 0.2 percent on average, less than share prices increased last week. During the past five years, companies with higher-than-expected profits have realized share price gains of 1.1 percent.

Although it would seem counterintuitive for a company's stock valuation to decline with good news on the earnings front, there are two key points (among others) investors must consider:

1. *Liquidity*, which *"is measured by the number of buyers and sellers in relation to the stability of an asset's price"* (*NASDAQ*), describes how easily a stock can be purchased or sold without a shift in price. Highly volatile stocks that react

with few trades are “illiquid”.

2. *High expectations* of pending earnings can impact stock valuation in unexpected ways. According to *NASDAQ*, “when it comes to earnings, if the expectations are already high, the stock has most likely priced in an earnings beat.”

It’s easy to get wrapped up in trying to predict market reactions, though it’s worthwhile to remember an important point, according to *CBS News*, “Two of the basic tenets of the efficient markets hypothesis are that current market prices reflect the total knowledge and expectations of all investors, and any new information must be disseminated to the public rapidly and completely so that prices instantly adjust to new data. In general, it's been found that while news releases result in a rapid increase in volatility, the majority of the effect is relatively short-lived and subsides within the first minute. For example, a study on how quickly the U.S. fixed income markets incorporate new information found that a considerable portion of the changes in interest rates can be attributed to scheduled macroeconomic announcements such as employment reports and inflation data. The major adjustment to the information released (and the window for trading profits) lasts about 40 seconds.”

Whether you’re an optimist, a pessimist, or have supernatural psychic abilities, rather than spinning your wheels trying to predict market turns, your time is most likely better spent staying informed, and using your good ole’ fashioned gut.

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