Weekly Capital Market Comments

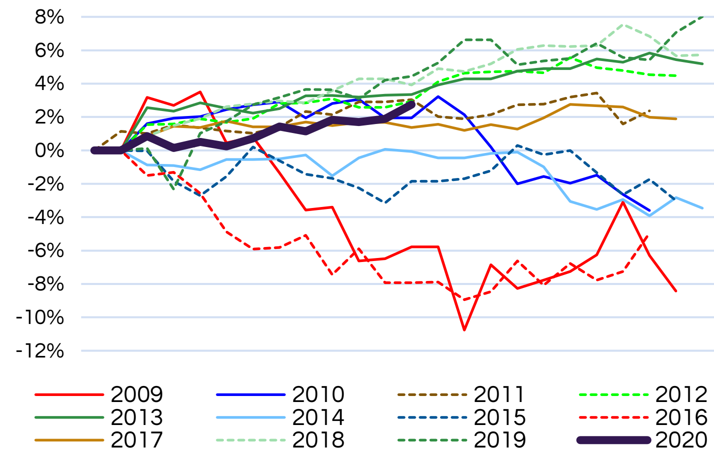
January 17, 2020

NORTHEAST SEQUOIA
PRIVATE CLIENT GROUP

Fundamentally Flawed

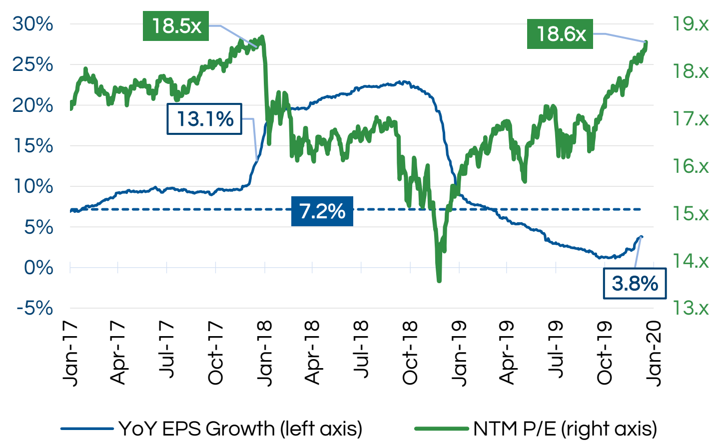
Thursday marked yet another all-time high for the S&P 500 at 3,317. Thus far through January 2020, the S&P is higher by roughly 2.7%. Still, this last 2-week period is only the sixth-best, in performance terms, going back ten years. What we find interesting is that the average monthly gain throughout the first two weeks of January dating back to 2009 is only 0.7%. The reasoning behind this mismatch are two outlying down-years. As we illustrate in the first chart herein, while trends in 2018 and 2019 helped support January returns, trading patterns in 2009 and 2016 (red) have significantly dampened the January average. If we remove 2009 and 2016 from the mix, however, January 2020 is shaping up to be a ***typical*** January. But as we pointed out last week, what we find ***a-typical*** is the fact that the S&P is rallying despite only modest earnings prospects in 2020. In the second exhibit herein, we illustrate that the S&P is currently trading at 18.6x forward 12-month S&P earnings, yet the forward earnings growth expectation for the S&P is only 3.8%, or about 1/2 less than the long-term average (7.2%). **Two years ago this week, the S&P was trading at similar multiples, roughly 18.5x. However, at that time, the projected forward earnings growth for the S&P 500 was over 13%, almost 2x the long-term average of 7.2%.** So as we have pointed out countless times from atop our soapbox, the current capital market and economic cycle seem extended from a historical perspective, driven by extraordinary monetary stimulus, deregulation, and contrarian fiscal stimulus (The Tax Cuts and Jobs Act of 2017) enacted during the declining phase of the business cycle. Yet sentiment is moving in only one direction, and our "over-valuation" call is getting run over. Even the latest political hot-potato admission from Lev Parnas seems to be falling on deaf ears as partisan politics has moved from the House to the Senate. So all we can do now is revert to one of our all-time favorite quotes from John Maynard Keynes, "*markets can remain irrational for longer than you can remain solvent,*" and wait for the pull-backs. And the only comfort we have at this point is the notion that nobody has ever lost money booking profits. We continue to advocate for a more conservative bias (stock/bond allocation) in portfolios, a value-tilt in equity portfolios, an increased focus outside the US and a reduction in duration focus (interest rate risk) for fixed-income portfolios. We'd love to hear your thoughts.

January S&P Return Trends



Source: FactSet and NEPCG

Multiples ≠ Earnings



Source: FactSet and NEPCG