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V-bottom January Barometer

Yes, we're forecasting a 32% rally from Christmas Eve 2018 to New Year's Eve 2019.

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BOTTOM LINE

After a 20% waterfall decline in last year's fourth quarter (including the worst December since 1931), during which investors were pricing in the imminent prospect of a recession, the S&P 500 rebounded with a vengeance to start 2019, surging 8% to post the strongest January in 32 years. Stocks have continued their good run and have now rallied 17% over the past six weeks since Christmas, nearly erasing last year's late collapse. But the technicians remind us that stocks have currently run smack into overhead resistance at the 200-day moving average of 2,750, suggesting that we may experience some consolidation of these outsized gains through the balance of the first quarter.

What might cause this temporary indigestion? Let's return to our three much-anticipated March signposts. Will China and the U.S. complete their trade deal by the March 1 deadline? Will the Federal Reserve successfully adjust their dot plots at their March 20 policy-setting meeting? And will the U.K. and the European Union find some common ground ahead of the March 29 hard Brexit deadline? Uncertainty surrounding some or all of these developments could very easily spark a near-term correction.

In our view, however, any weakness represents an attractive longer-term buying opportunity. We're sticking to our guns, as we continue to forecast an out-of-consensus rally to our 3,100 price target for the S&P this year. As investors eventually realize the U.S. is not sliding in recession this year, we expect P/E multiples to take a roundtrip: moving from an appropriate 18 times earnings last September to an oversold 14 times at Christmas back up to 18 times our $170 estimate in S&P earnings by year-end 2019. Yes, we're forecasting an aggressive 32% rally from Christmas Eve 2018 to New Year's Eve 2019, but we've already successfully banked half that gain in the past six weeks. The January Barometer suggests that we'll achieve the balance over the course of 2019 as stocks grind higher.

Strong positive "January Barometer" signal for 2019 The S&P enjoyed a positive January, rising 7.87% for the full month on a price-only basis. The "January Barometer" remains one of the stock market's most popular and widely followed rules of thumb. Historically, as the month of January goes, so goes the full year. Since 1950, Jeffrey and Yale Hirsch at the Stock Trader's Almanac report that when the S&P started the New Year with a positive month of January, as it has done 42 times since 1950, it finished the year higher in 37 of those instances, for a strong success rate of 88%.

In our view, this is not a random statistical coincidence. Investors begin each New Year by actively demonstrating their investment outlook, making their annual retirement and college-savings contributions and adjusting their asset allocations, thus reflecting either their bullish or bearish sentiment.

Very strong performance in January 2019 For the full month of January 2019, the S&P enjoyed a nominal price increase of 7.87%, starting from 2,507 on Dec. 31, 2018 and ending at the closing price of 2,704 on Jan. 31. The total return (which includes dividends) over this period was a gain of 8.01%. This represents the fourth-best January for the stock market since 1950 and the strongest first month for the S&P since the market's 13.2% gain in 1987. If we look at the other 17 years in which the S&P started January with at least a 4.2% gain (the top quartile of all observations), every full year but one was positive (a 94% success rate). That results in a total return averaging 22.8%, within a wide range of -6.4% last year to 45% in 1954.

Stock-market trifecta The Santa Claus rally period is defined as the last post-Christmas week in December and the first two trading days in January, during which the S&P rallied 4.1% this past cycle. The early January Barometer, defined as the first five trading days of the New Year, posted its tenth-best start in 2019, up 2.7%. And the full January Barometer rose a powerful 7.9% this year, its fourth-best start in history. Historically, going three-for-three with these overlapping indicators collectively suggests that the full year will be strong.

What are the best sectors to own in 2019? The January Barometer Portfolio indicator also holds that the best- and worst-performing S&P sectors in January tend to follow that performance trend the rest of the year.

Here are the S&P's 11 sectors, sorted by their total-return performance in January 2019. The overriding theme is clearly "risk-on," with a more cyclical and growth-oriented bias at the top of the list and a more defensive, dividend-oriented bias toward the bottom:

- Industrials, 11.42%
- Energy, 11.11%
- REITs, 10.79%
- Communication Services, 10.37%
- Consumer Discretionary, 10.30%
- Financials, 8.84%
- **S&P 500, 8.01%**
- Information Technology, 6.96%
- Materials, 5.49%
- Consumer Staples, 5.19%
- Health Care, 4.84%
- Utilities, 3.43%

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DISCLOSURES

Views are as of the date above and are subject to change based on market conditions and other factors. These views should not be construed as a recommendation for any specific security or sector.

Past performance is no guarantee of future results.

S&P 500 Index: An unmanaged capitalization-weighted index of 500 stocks designated to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. Indexes are unmanaged and investments cannot be made in an index.

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