ClarkCapital MANAGEMENT GROUP

Navigator® Market Update
K. Sean Clark, CFA, Chief Investment Officer

May 12, 2014 - Market Commentary

K. Sean Clark, CFA
Chief Investment Officer

As Clark Capital's Chief Investment Officer, Sean oversees all of the Firm's investment activities and heads the Firm's portfolio team. Sean joined the Firm in 1993 and is responsible for asset allocation and investment selection for Navigator Investment Solutions as well as directing ongoing market research and contributing to the development of proprietary products. Sean is a member of the Clark Capital Board of Directors, the Investment Committee and the Management Committee. He graduated from the University of Delaware, earning a B.S. and an M.A. in Economics. Sean is a Chartered Financial Analyst and a member of the CFA Institute (formerly AIMR) and the Financial Analysts of Philadelphia, Inc. Sean is considered an industry expert and is often asked to appear on CNBC and Bloomberg television to share his views on the market. In addition, Sean has been featured in a number of articles in nationally distributed business journals and newspapers.

SELL IN MAY AND GO AWAY?

The U.S. markets have gone through a sharp rotational correction over the past two months. Growth, small cap, and high beta stocks have all collapsed relative to defensive investments. The rotation raises the question: have we have seen the best the market has to offer this year or will the rotation to defensive utilities, staples, and late cycle basic material and energy names provide new leadership for another charge higher? We made the case in our ETF.com column in January 2014 that the middle of this year would be wrought with challenges given the mid-term election year trends and the new chairperson at the helm of the Federal Reserve. Are we at the point now?

We have all heard the saying: "Sell in May and go away." That suggests investors would do well to be out of the market from May 1 through October 31. Is that just stock market lore or is there really something to it that investors need to pay attention to?

According to Ned Davis Research, since 1950 all of the market's gains have come from October 31 through April 30. Let's break out the two six-month seasonal time periods since 1950, November 1 – April 30 and May 1 – October 31, and look at the growth of $10,000 in each period. For example, $10,000 invested in the S&P 500 in 1950 has grown to $606,167 during the strongest six-month seasonal period while $10,000 invested in the weak six-month seasonal period has declined to $6,920.

Now, I actually think it is quite silly to base one's investment decisions purely on what month we are in, but it is hard to argue the statistics. There is also the problem that once an accepted Wall Street adage such as "Sell in May and go away" becomes widely publicized in the press, it often does not prove true. Last year was a prime example, with many analysts proclaiming a need to get defensive because of the calendar. However, instead of declining during the "normal" seasonally weak period, the S&P 500 Index rose 11.1% from April through October.

If we break out the study a little further, it is revealed that all of the weakness experienced with this stock market lore has occurred in the mid-term election years. Since 1950, the mid-term election year is the only year to have had an average decline in the May 1 – October 31 period, with an average decline of 0.37%. The other three years in the cycle averaged gains of 1.82% during the May 1 – October 31 period. The chart below illustrates that the pattern of returns in the mid-term election years (blue) is dramatically different from other years (black). Which raises the question, should investors heed the warning about potential risks as we tread further in the second quarter? History suggests yes. In addition, the rotational correction that we have witnessed also hints at a market that is getting more defensive. For those investors who want to stay invested, despite the potential risks, we would heed the market's recent shift to defensive allocations and look toward higher dividend plays.

Even in a declining market, there are opportunities somewhere — or at least areas that can offset losses occurring in the broader market. "Sell in May and go away" might have some truth in it; however, by digging a little deeper into market and economic history we can uncover more specific triggers for market declines over the summer months and make more educated investment decisions.

The S&P 500 measures the performance of the 500 leading companies in leading industries of the U.S. economy, capturing 75% of U.S. equities.

The Dow Jones Industrial Average is a stock market index that shows how 30 large publicly owned companies based in the U.S. have traded during a standard trading session in the stock market.

The NASDAQ Index is a market-weighted index of all common stocks listed on the NASDAQ exchange.

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performers of developed markets outside the U.S. and Canada.

The MSCI World Index is a free float-adjusted market capitalization index that is designed to measure global developed market equity performance.

The MSCI World Index ex. U.S. is a free float-adjusted market capitalization index that is designed to measure global developed market equity performance excluding the U.S.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

The MSCI All Country Europe is a free float-adjusted market capitalization index that is designed to measure the performance of European equity markets.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000 Index.

The Russell 3000® Index measures the performance of the 3,000 largest U.S. companies based on total market capitalization, which represents approximately 98% of the investable U.S. equity market.

The VIX Index is a forward looking index of market risk which shows expectation of volatility over the coming 30 days.

Barclays U.S. Government/Credit Bond Index measures the performance of U.S. dollar denominated U.S. Treasuries and government-related and investment grade U.S. corporate securities that have a remaining maturity of greater than one year.

The Barclays U.S. Aggregate Bond Index covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities. To qualify for inclusion, a bond or security must have at least one year to final maturity, and be rated investment grade Baa3 or better, dollar denominated, non-convertible, fixed rate and publicly issued.

The Barclays U.S. Corporate High-Yield Index covers the dollar-denominated, non-investment grade, fixed-rate, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's, Fitch, and S&P is Ba1/BB+/BB+ or below.

Index returns include the reinvestment of income and dividends. The returns for these unmanaged indexes do not include any transaction costs, management fees or other costs. It is not possible to make an investment directly in any index.

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