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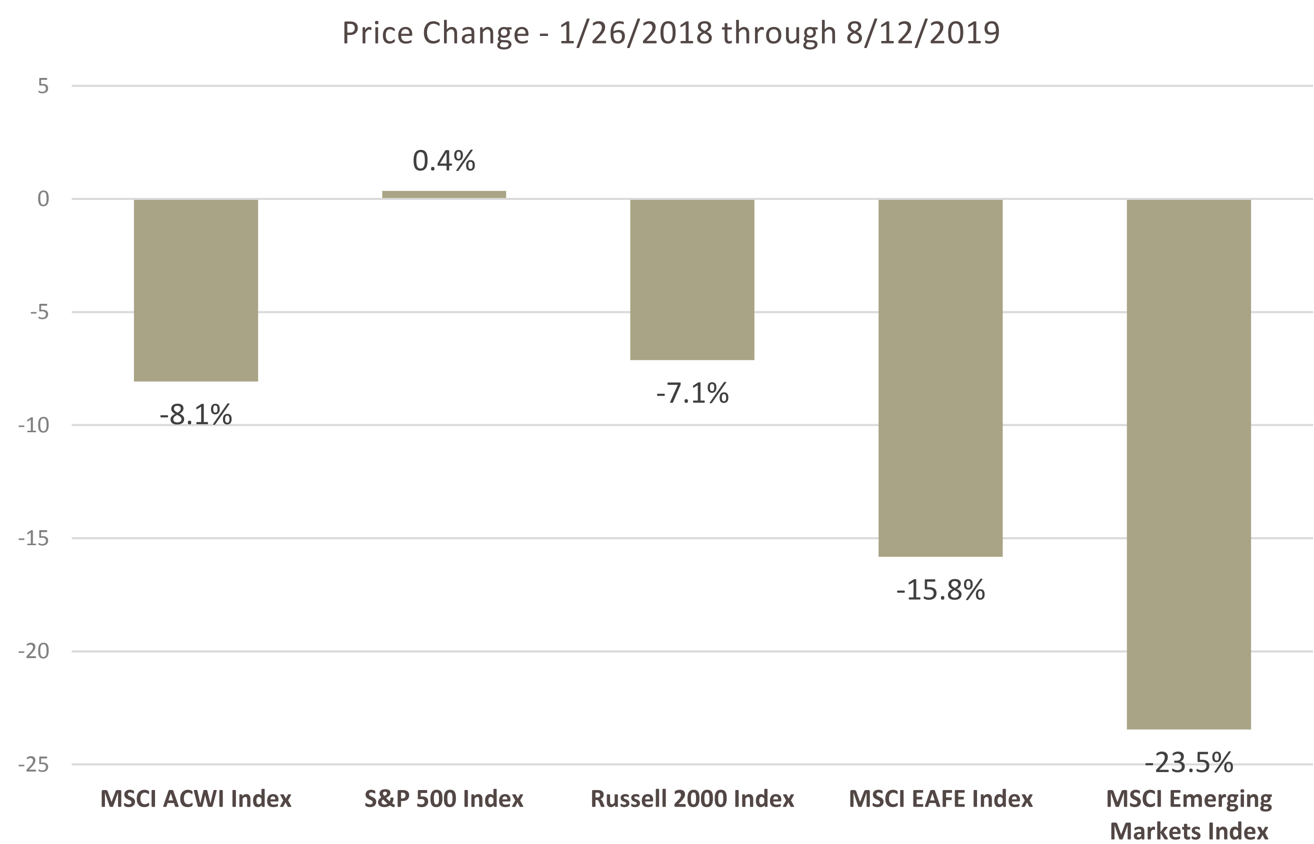
Investment Perspectives – August 2019

In late January 2018, we hosted a client webinar discussing the markets and the economy. The S&P 500 had just risen for an unprecedented 15 consecutive months, taking prices up 37%. One notable quote from that call was, "the S&P 500 is up nearly 7.5% for the month. Things are good. They are probably getting better and everybody knows it." This was meant to convey our belief that the market's advance had already incorporated a significant amount of good news and we were concerned with its ability to move much higher absent new positive news. As it turns out, our call was one day after global stock prices peaked. 18 months later the S&P 500 is basically exactly where it was when we did that webinar and global equity prices are 8% lower.



Considering US stocks are at the same level they were 18 months ago, plenty has changed. Earnings for the S&P 500 grew by 25%, but the majority of that gain came early in 2018 – from the one-time bump up due to the lower corporate tax rate. For comparison, revenue for the S&P 500 has only grown by 12% since last January. Meanwhile the price/earnings multiple shrank from from 18.5 in January 2018 to 14.0 in December before rebounding to 17.0 now.

Expectations for growth going forward have also come down. Estimates for S&P 500 earnings growth over the next 4 quarters are 12%, compared with the 26% projected in January 2018. At that point investors justified high valuations with predictions of synchronized global growth and an extra kick to be provided by tax reform. Now the narrative focuses on low bond yields and easing from the Fed to head off recession. A continually escalating trade war between the US and China, and at times other countries, has weighed on earnings and dampened investment. Geopolitical concerns abound from Britain to Argentina.

If we define a bear market as a 20% decline from previous highs, most markets entered one at some point in 2018. Outside of US large caps, most markets have still not recovered to previous highs. The question going forward is whether this downtrend will continue, or whether this has just been a reset in expectations that will give way to continued growth.

Data Source: Bloomberg, Bloomberg Estimates; Analysis by 6 Meridian; Data as of 08/12/2019

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