After The Close

U.S. markets continue their tumble lower; The S&P 500 wipes out gains for the year

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October 24, 2018

Stocks can't seem to find their footing

Today, U.S. stocks were again overcome by selling pressure. The S&P 500 Index is now down 8.8% in October. Information Technology, Communication Services, and Consumer Discretionary are all underperforming the S&P 500 Index this month. Large tech stocks hold a significant weighting in these sector indexes, thus their underperformance has contributed to anchoring overall market performance. For markets to stabilize, we believe large tech stocks will need to find their footing.

On the day, semiconductors, banks, telecom, biotech, and metals all experienced outsized selling pressure. Defensive sectors, however, bucked the trend and finished in positive territory. On the fixed income side, U.S. Treasury yields moved lower for the third straight day, as bond prices moved higher. The solid year-to-date gains U.S. stocks brought into October have now evaporated, prompting investors to turn to U.S. Treasuries and gold for safety.

Major Domestic Equity Indices - Today

Benchmark	Index Level	Net Change	% Change
S&P 500 Index	2,656	-84.6	-3.1%
Dow Jones Industrial Average	24,583	-608.0	-2.4%
Russell 2000 Index	1,469	-57.9	-3.8%
NASDAQ Composite	7,108	-329.1	-4.4%

All data via FactSet as of approximately 4 PM ET

On Tuesday, stock prices moved sharply lower after two key Industrial companies disappointed on the earnings front. The weaker-than-expected news out of 3M and Caterpillar sent the Dow Jones Industrial Average down more than 500 points early in yesterday's session, though the 30-stock Index was able to recover much of that loss by the close. In our view, this type of quick change in market direction is often technical, and a reflection that the environment may remain volatile over the near-term.

The S&P 500 and Russell 2000 have both been down in six consecutive trading days. Concerns about peak earnings growth across U.S. companies, slowing economic growth and tightening financial conditions appear to have caught U.S. markets off-guard. We believe international equities already reflect some of this anxiety and U.S. markets may still have room to adjust. Italian budget concerns also remain a risk, as do weak housing data and a near-term hold on corporate share buyback activity. Corporate buybacks should resume over the coming weeks as earnings season ends. Today, President Trump also ratcheted up his criticism of Fed Chair Jerome Powell, saying he is having second thoughts about placing Powell in the Chair role. White House pressure may be a bit unnerving, but it should have no impact on Fed independence, in our view.

Earnings season is not providing the boost it usually does

Although third quarter corporate earnings are coming in mostly as expected, the results are clearly not offering stock prices much support. Companies that have beat expectations are not seeing the corresponding stock price boost that was the norm over the first half of the year. Revenue growth has also slowed amid slower international growth and a stronger U.S. dollar. What is most telling, however, is companies that miss EPS and revenue expectations are being punished more severely compared to previous quarters. There has also been a material uptick in the number of companies offering lower earnings guidance.

Yet, for the smaller number of companies that have beat EPS and revenue expectations and offered higher earnings guidance, stock prices have reacted quite well. The point: 'really good corporate news' is still rewarded and recognized in an otherwise downbeat market environment.

In our view, that is a positive factor for investors to build-on over the coming weeks. Unlike the experience of the year's first-half, earnings season has become a 'case-by-case' story for companies – with serious consequences for those that can't keep up.

Committee View

Although we do not believe a bear market is forming, underlying market and economic fundamentals are indeed evolving. This could make for a more turbulent investment environment over the intermediate-term. During such times, we believe that the time-tested value of diversification can shine.

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