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Dear Valued Investor:

The late baseball legend Yogi Berra was known for many memorable quotes, including one that is relevant for investors today, "it's like déjà vu all over again." The renewed downturn in stock prices feels like déjà vu all over again. Just when it appeared the August lows were the bottom and a rebound had begun, stocks retested the recent low on Monday, September 28. The ongoing correction rekindled the painful memories of 2008 and a difficult summer of 2011.

Corrections can be especially nerve-racking for investors when the reasons for the sell-off keep shifting. Fears over China's slowdown shifted to oil prices and then to the possible implications — negative of course — of a possible Federal Reserve interest rate hike.

And speaking of déjà vu, the latest threat to the stock market appears to be another potential stand-off in Washington, similar to what we experienced most recently in 2013. But, as is often the case in Washington, lawmakers appear to be coming together in the final hours on an extension that would avoid a government shutdown. The specter of another possible furlough of workers and spending halts will likely be avoided.

Difficult memories stay with us, which helps explain why investors are lacking the confidence needed to move higher. Stocks were higher just a few months ago and on pace for a good year. But the challenges that emerged over the summer, coupled with above-average valuations for the U.S. stock market, eroded confidence. Concerns over the energy sector and the headwind of a strong dollar on U.S. multinational companies have overshadowed the strong profit growth produced by the remainder of corporate America. Excluding the impacts of energy and a strong dollar, corporate earnings are still likely to rise by 6% for 2015.* Over the long term, earnings growth drives stock prices, not concerns we believe to be short term, such as a deceleration in China or potential gridlock in Washington — both of which we've seen before.

We remain vigilant for signs of a recession; but so far, the data we closely follow that have historically provided early warning signs are not indicating the near-term possibility of a recession. Improvement in consumer spending reported this week was dismissed by investors even though it bolstered expectations for another consecutive quarter of 2–3% economic growth, far from recession. We continue to look for signs of overborrowing, overspending, and overconfidence to determine whether complacency has settled in more broadly.

*According to Thomson Reuters estimates.

The lack of top-tier economic data in the past few weeks may have undermined confidence. With no new data to effect a positive change, negative sentiment has reappeared. The absence of consistent signposts during periods when investor sentiment is weak can often lead to a “sell first” mentality.

Healing may begin soon, however, as another batch of top-tier economic reports will be released in the second half of this week, including the Institute for Supply Management (ISM) and the monthly employment report. The ISM is a measure of manufacturing activity, and therefore, is likely to be impacted by both energy and a strong dollar; but this broad measure may help to confirm or deny the extent of a slowdown indicated by regional surveys, which may help restore confidence. And the jobs report, scheduled for Friday, October 2, is one of the truest measures of the economy’s strength.

During these situations it is always helpful to take a longer-term view. After noteworthy market declines, questions arise if it is the time to sell or an opportunity to add. In recent years, opportunities to step in and buy have been few and far between due to the consistent strength of the market. We believe an opportunity might be here now. Stock gains may not match the extraordinary gains of prior years, but as long as the earnings trajectory remains positive for the year, we expect current weakness to remain a correction and not something more severe, and the market may begin to move higher.

As always, if you have questions, I encourage you to contact your financial advisor.

Sincerely,

Anthony Valeri, CFA
SVP, Thought Leadership & Investment Strategist
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