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SEASONAL ROTATIONS

Like whitewater rafting, let the market take you where it wants to go

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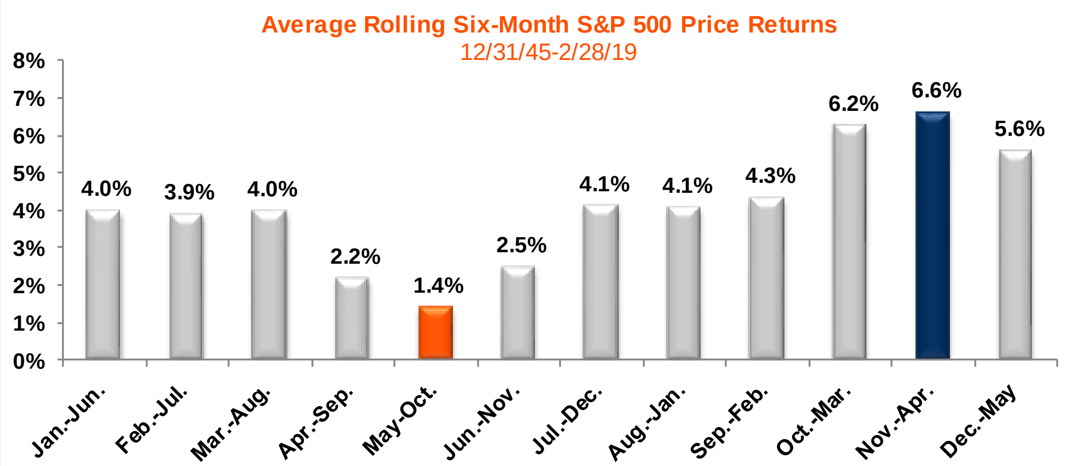
To everything there is a season, and the same goes for the stock market. Most investors are familiar with the old Wall Street axiom "Sell in May and go away." This adage has been around for decades and maybe even centuries. Search the web and you may find reference to an Old English saying "Sell in May and go away. Do not return until St. Leger's Day." From the perspective of a U.S. investor, however, tradition holds that the stock market registered the weakest six-month return from May through October (M-O) and the strongest from November through April (N-A). As seen in the chart below, showing 12 rolling average six-month price returns, the S&P 500 posted an average gain of 6.6% during N-A since 1946, but only 1.4% from M-O. Taking this analysis one step further, the S&P 500 posted a positive six-month return 76% of the time N-A, but only 64% of the time M-O. Finally, the market's return in N-A outpaced the return in the subsequent M-O period in seven out of every 10 years.

As seen in the chart on the following page, this pattern of seasonal strength and weakness is not just a U.S. large-cap phenomenon. The S&P Equal Weight 500, S&P SmallCap 600 and S&P Global 1200 also recorded their weakest six-month returns in the M-O periods and the highest average six-month gains N-A. Specifically,

- The S&P Equal Weight 500 posted an average 9.5% return N-A, and an 89% frequency of a positive return since 1990, while eking out a 0.9% average increase in M-O, though rising 69% of the time. In addition, the N-A return beat the M-O results 71% of the time.
- The S&P SmallCap 600 also saw its best rolling six-month return in N-A, averaging 9.0% since April 30, 1995, while rising 91% of the time. Yet in M-O, its weakest six-month period, the average gain was 2.5% and the index rose in price 67% of the time. And like its two domestic siblings, the N-A return was higher than the following M-O result 70% of the time.



Source: CFRA, S&P DJ Indices. Past performance is no guarantee of future results.

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- Finally, this rotation of strength and weakness held true overseas as well. In particular, the S&P Global 1200, of which 80% of the holdings come from outside the U.S., recorded its highest average six-month return in the N-A period, with a 6.3% gain and an 83% frequency of advance, but posted its weakest six-month return in M-O, gaining only 0.6% and rising in price 67% of the time. Once again we see that the S&P Global 1200's N-A return beat the next M-O results 77% of the time.

Semi-Annual Price Returns Based on Size and Region

	Nov.-April (N-A)		May-Oct. (M-O)		N-A Beat
Index	Avg. %	Up?	Avg. %	Up?	M-O?
S&P 500 (Since 1946)	6.7	77%	1.4	64%	70%
S&P Equal Weight 500 (1990)	9.5	89%	0.9	69%	71%
S&P SmallCap 600 (1995)	9.0	91%	2.5	67%	70%
S&P Global 1200 (1995)	6.3	83%	0.6	67%	77%

Source: CFRA, S&P DJ Indices. Past performance is no guarantee of future results.

Should You Really Go Away?

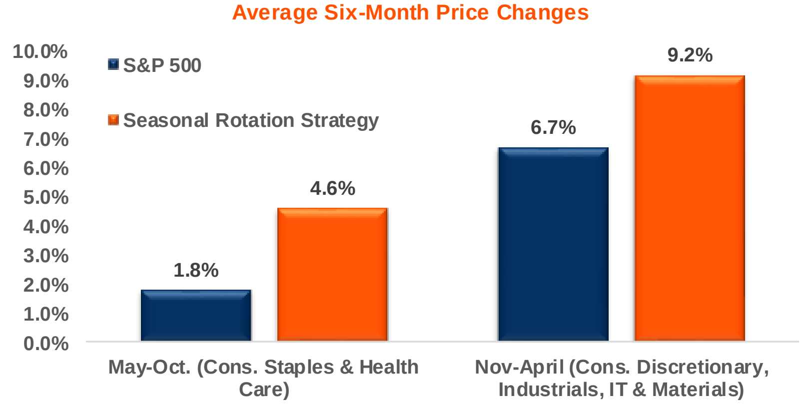
Even though the average advance of 1.4% for the S&P 500 from M-O is the weakest of all 12 rolling six-month periods, it delivered an annualized return of nearly 3%. This is still better than what an investor would have received from a money market fund. Also, the market has risen in more than two out of every three years. Retreating from the "500" in that six-month period would have caused investors to miss out on unexpected summertime surges of 14.1% in 1997, 14.6% in 2003 and 18.7% in 2009, just to name a few. Besides, investors need to consider transaction costs and the tax consequences of selling out. Therefore, wouldn't it be better to identify a more attractive alternative approach to retreating from stocks altogether during this seasonally slow period?

Rotate, Don't Retreat!

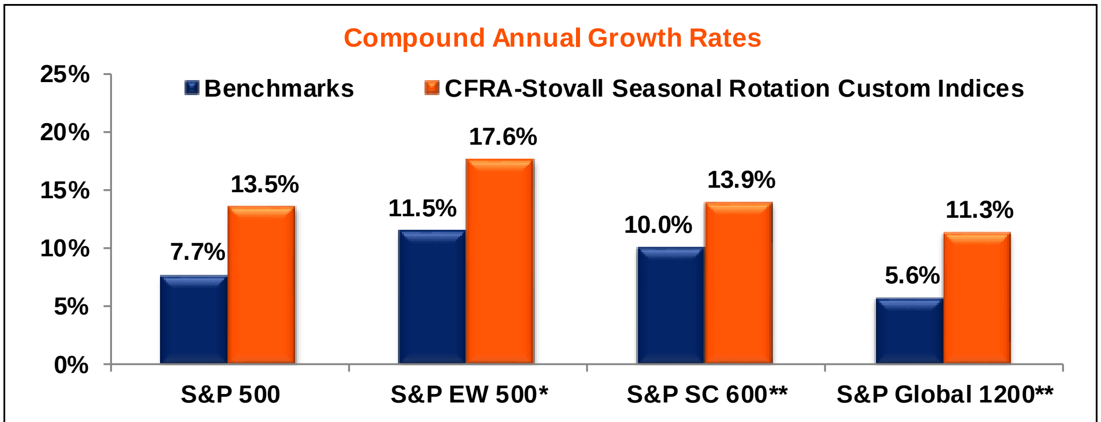
Some sectors have their day in the summertime sun, while others skate along smoothly in winter. Since 1990, which is as far back as S&P DJ Indices has sector-level data, while the overall market was eking out an anemic advance of only 1.8% from M-O, the S&P 500 consumer staples and health care sectors recorded price gains of 4.4% and 4.9%, respectively. In addition, these two sectors posted 62% frequencies of beating the S&P 500 during this traditionally low-rising period for the overall market. It's not that people prefer to get hip replacements in the summer, but health care and consumer staples likely do better during challenging times for the overall market, since investors prefer to rotate into more defensive sectors than bail out of stocks altogether.

Conversely, as the S&P 500 recorded its strongest six-month return in the N-A period, it should come as no surprise that the cyclical sectors also outperformed the defensive ones during these months. Indeed, since 1990, above-average price gains came from the consumer discretionary, industrials, materials and technology sectors. What's more, these sectors consistently racked up benchmark-beating returns across the large-cap, equal weight, small-cap and global index spectrum. Knowing this, wouldn't it be more advantageous to rotate among defensive sectors during the "Sell in May" months, and then into the cyclical sectors during the remainder of the year?

Average Six-Month Price Changes



Source: CFRA, S&P Global. Past performance is no guarantee of future results. Data: 4/30/1990-2/28/2019.



Source: CFRA, S&P Global. Past performance is no guarantee of future results. Data: 4/30/90-2/28/19. * Total Return. **Since 4/30/95.

Hypothetical Portfolios

From 1990 through February 2019, a hypothetical portfolio that owned an equal weighting of consumer staples and health care sectors from M-O, but then rotated into an equal exposure to the consumer discretionary, industrials, materials and tech sectors from N-A would have seen an increase in compound annual growth rates (CAGRs), as well as a reduction in annual volatility, vs. its benchmark, all while beating its bogey from 67% to 76% of the time.

- The S&P 500 posted a CAGR of 7.7%, while the semi-annual seasonal rotation strategy returned 13.5%, In addition, this strategy experienced lower annual volatility as the standard deviation of annual returns was 15.6% vs. 16.5% for the S&P 500 Index itself.
- This seasonal rotation strategy delivered 600 basis points of outperformance using the S&P Equal Weight 500 sectors since 1990 and beat its benchmark in 76% of all calendar years since 1990, while posting a lower standard deviation of annual results.
- The outperformance by the S&P SmallCap 600 and Global 1200 Seasonal Rotation Strategies since 1995 ranged from 390 basis points per year for small-caps and a doubling for global stocks, while beating their benchmarks in two out of every three years. Again, both the small-cap and global strategies experienced a reduction of annual volatility relative to its benchmark. Of course, past performance is no guarantee of future results.

S&P Dow Jones Indices is the custom calculation agent for the CFRA-Stovall Seasonal Rotation indices, which embrace this investment strategy by owning cyclical sectors N-A and defensive groups M-O in the S&P 500, Equal Weight 500, SmallCap 600 and Global 1200. For information, please visit:

CFRA-Stovall Seasonal Rotation Custom Indices

	% Returns					
	2019			Since	Beat	Standard
Indices	MTD	YTD	2018	4/1990	Benchmark	Deviation
S&P 500	3.0	11.1	(6.2)	7.7	NA	16.5
Seasonal Rotation Large Cap.	4.0	12.8	0.6	13.5	72%	15.6
S&P Equal Weight 500*	**3.7**	**13.9**	**(7.6)**	**11.5**	**NA**	**17.8**
Seasonal Rotation Equal Weight*	**5.0**	**15.3**	**(2.4)**	**17.6**	**76%**	**16.1**
S&P SmallCap 600**	4.2	15.2	(9.8)	10.0	NA	16.2
Seasonal Rotation SmallCap**	5.7	18.8	(2.9)	13.9	67%	15.6
S&P Global 1200**	2.6	10.3	(10.5)	5.6	NA	14.8
Seasonal Rotation Global**	3.3	11.9	(3.5)	11.3	67%	13.8

Source: S&P DJ Indices. Returns: 4/30/1990-2/28/2019. *Total Return. Others are price changes.
**Since 4/30/1995. Past performance is no guarantee of future results.
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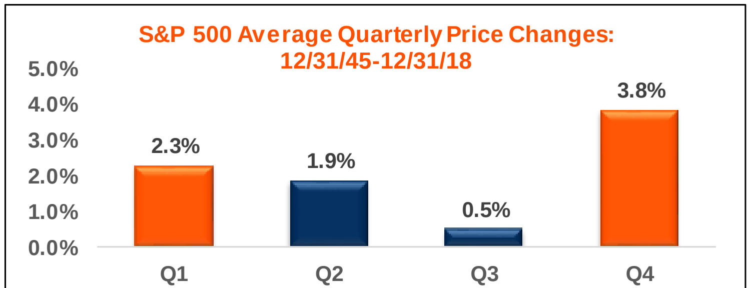
Rotation Rationale

Just because the Seasonal Rotation Strategy has worked in the past, doesn't guarantee that it will continue to do so. Price weakness during the M-O period is likely the result of a combination of reduced capital inflows, investor vacations, Q3 earnings reality, and Mutual Funds' fiscal year-end window dressing. In turn, the above-average strength in the N-A stretch may be aided by an increase in cash infusions, particularly during the beginning of each calendar year from pension fund additions, bonuses, 401K contributions, IRAs, and tax refunds.

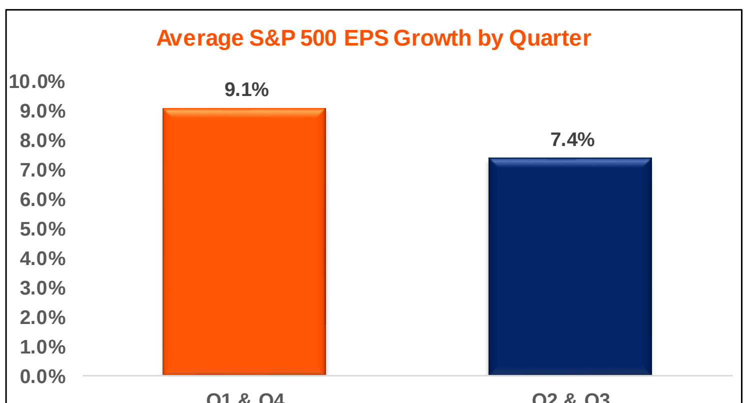
Capital Infusions – The above-average strength in the November-April stretch may be aided by large cash infusions into the market, particularly during the beginning of each calendar year. Bonuses are typically paid by March. After taxes from these bonuses are paid, and 401(k) contributions are withdrawn, some of the residual is likely invested in the market. Next, should someone be due a tax refund, they will likely file their returns early. This will allow them time to invest their proceeds before the end of April. Third, IRAs for the prior tax year need to be funded by April 15th of each year. Finally, full-year 401K contribution limits are typically fulfilled early, aided by bonuses. As a result, it should come as no surprise that there is a first-quarter income bump.

Vacations – From the perspective of seasonal sluggishness, history shows that the S&P 500 posted its weakest three-month average return in the third quarter, as investors may be focusing more on their vacations than their investments. Since 1946, the S&P 500 recorded its strongest quarterly returns in Q4, which jumped 3.8% on average and Q1, which gained 2.3%. However, the S&P 500 climbed only 1.9% on average in Q2 and only 0.5% in Q3.



Source: CFRA, S&P DJ Indices. Past performance is no guarantee of future results.

Earnings – End-of year earnings revisions may also be a reason the market performs poorly in the third quarter. An investor may be forgiving of soft Q1 and Q2 EPS on their way toward solid full-year estimates. Should Q3 look like it's going to miss as well, investors usually don't wait around. Like a veteran retailer, they'll "mark 'em down, and move 'em out." As a result, this could be one reason September has been the worst performing month of the year since 1928, 1945 and 1970, particularly as Mutual Funds engage in some end-of-quarter window dressing ahead of their fiscal year end. What's more, let's not forget that five of the last 10 bear markets ended in October, as did the near-bear of April through October 2011. Therefore, the S&P 500 has traditionally entered November at a fairly low price point when compared with other months. In addition, November is also around the time of year that analysts begin looking toward next year's earnings estimates, or five quarters ahead, rather than just focusing on the final one of the current year.



Source: S&P Global Markets Intelligence. Data: 12/31/1995-12/31/2018

Glossary

★★★★★ 5-STARS (Strong Buy):
Total return is expected to outperform the total return of a relevant benchmark, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

★★★★☆ 4-STARS (Buy):
Total return is expected to outperform the total return of a relevant benchmark over the coming 12 months, with shares rising in price on an absolute basis.

★★★☆☆ 3-STARS (Hold):
Total return is expected to closely approximate the total return of a relevant benchmark over the coming 12 months, with shares generally rising in price on an absolute basis.

★★☆☆☆ 2-STARS (Sell):
Total return is expected to underperform the total return of a relevant benchmark over the coming 12 months, and the share price not anticipated to show a gain.

★☆☆☆☆ 1-STAR (Strong Sell):
Total return is expected to underperform the total return of a relevant benchmark by a wide margin over the coming 12 months, with shares falling in price on an absolute basis.

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