

Sell in May and Go Away Revisited

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2011 Outlook

GDP GROWTH:
3.0%

UNEMPLOYMENT:
9.0%

INFLATION:
1.75%

FED FUNDS RATE:
0.35%

The world is full of generalizations. And because they are generalizations, they are not truisms. One generalization which originates from Wall Street is “Sell in May and Go Away.” Historically, there is some truth to this generalization. Will it be the same this year?

The old Wall Street saw of “Sell in May and Go Away” means an investor (speculator) should sell stock holdings at the beginning of May, take the summer off and repurchase stock positions at the end of October. How has this mechanical trading strategy worked in the past? Like all generalizations, there is some degree of truth to the concept, but there are also significant holes.

Track Record

The following data shown is historical price return data for the S&P 500 Index from 1950-to-2010.

	<u>May 1-to-Oct. 31</u>	<u>Nov. 1-to-April 30</u>
Average Price Return	+1.30%	+6.83%
“Batting” Average	0.622	0.780
Positive Return	+6.90%	+11.07%

The data above shows that indeed, returns on average have been lackluster from May-to-October. This is particularly true when compared to the average returns from November-to-April. As a matter of fact, if an investor was hapless enough to consistently invest \$10,000 in stocks only during May-to-October from 1950-to-2010, the total gain made during that 61-year period would have been \$6,575. If a more fortunate investor simply invested \$10,000 in the index from November-to-April during those same years, the gain would have been \$385,073!

All of this being said, it is important to understand that the “batting average” (or percent of the time the market has generated positive results during both periods) is not all that dissimilar. So what is different? It is the degree of changes within the respective time periods. On average, when the market is generating positive returns, those returns from May-to-October tend to be much smaller (+6.90 percent) than the returns the market generates during the November-to-April period (+11.07 percent).

Very Long Term - Globally

This phenomenon holds not only in the U.S., but also globally. During the last 26-year period, the MSCI World stock index has outperformed the Citigroup World Bond Index 55.9 percent of the time. During the summer months of June-to-September, the worldwide stock index has outperformed the bond market 43.0 percent of the time – with the bond market obviously outperforming the stock market 57.0 percent of the time.

Why does this abnormality exist? There are many theories. Some believe stock analysts are more bullish on earnings estimates earlier in the year. And as time unfolds, downward estimate revisions start to take place following the first quarter earnings season. Others believe investors simply go on “holiday” during the summer months and do not pay significant attention to stock values and the market in general during this mid-year time period. Some investors believe flows into the market tend to be strong at the beginning of the year (bonus periods and 401k/IRA funding season) as compared to the rest of the year, which helps drive stock prices to the upside during the first portion of the year.

Final Word

Are we expecting the market to swoon this summer? We would not be surprised. If the market does correct, we do not believe the move will be the start of a new serious bear market, but rather a “correction” in the current bull run.



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