Financial Services Advisory
GROW WISER®

# Party Like it's 1999—Again?

**May Market Review—June 9, 2017**

Stocks have posted pretty solid returns since the surprise election of Donald Trump, with most indices rising in the double digits. The returns have been strong across most equity assets, including large-cap stocks, small-cap stocks, and even foreign stocks. Not all assets participated in this broad stock market rally, as high quality bonds and gold returns have been essentially flat. Nevertheless, for those willing to take the volatility of investing in stocks, it's been party time.

So why the reference to 1999? If you remember, it was a time of bubbles growing, then popping, followed by the ensuing pain of a bear market. Lately, we've noticed the recurrence of a phenomenon that was apparent in the late nineties: stock returns are being generated by fewer and fewer names. Back then, stock returns were dominated by a handful of technology stocks, such as Cisco, JDS Uniphase, Oracle, and Yahoo. This year we are seeing returns dominated by such names as Amazon, Apple, Facebook, and Netflix. According to research from Bespoke Investment Group, the returns from five technology companies were responsible for nearly 60% of the gain of the entire S&P 500 index for 2017 as of the end of May.

Money chasing after fewer and fewer stocks is often a sign of an unhealthy stock market. In the late nineties, this narrowness ultimately presaged a three-year bear market. We saw this anomaly also occur in 2014/2015, leading to sharp corrections in late 2015 and again in early 2016.

Take a look at the table below. It shows a number of stock index returns for 2017 (through May). The Value Line index is a good barometer of how the typical or average stock is performing, which is why it is included in this table.

| **Index** | **1/1-5/31** |
|---|---|
| S&P 500 Index | 7% |
| Dow Jones Industrial Average | 9% |
| Value Line Index (average stock) | 4% |
| Russell 2000 Index (small-cap) | 1% |
| MSCI EAFE Index (foreign stocks) | 14% |

Notice how the broader indices (Value Line and Russell 2000) are falling behind and the stronger returns are concentrated in the more narrow ones (Dow Jones and S&P 500). The exception for this year comes from the strong performance of the foreign markets. They have lagged U.S markets considerably over the past several years, so it will be interesting to see if foreign markets can maintain their performance advantage for the rest of the year.

Positive returns generated by a wide range of stocks within an index is usually a sign of a healthy stock market. Narrow participation does not always suggest a down market, but it raises a yellow flag for us to be sensitive to signs that overall price trends could be reversing. For now, with most areas of the equity market on an upward trend, we are content to have very low money market allocations in all the investment strategies. Nevertheless, we are watching diligently for evidence that this positive trend could stall out or begin to turn down. Parties are fun, but we don’t want to be too far from the exits when the band stops playing.

Ronald Rough, CFA
Director of Portfolio Management