Morgan Stanley

INVESTMENT MANAGEMENT

Equity Market Commentary

SLIMMON'S TAKE | APPLIED EQUITY ADVISORS TEAM | November 2024

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The following views and perspectives are formed by the work of the Applied Equity Advisors team in managing assets for investors.

1 *The outcome of the Presidential election* ***rarely*** *reverses the existing S&P 500 trend.*

a) When the S&P 500 has been in an **uptrend** going into the election, the S&P 500 has been **higher** 3 and 6 months later **85%** of the time, <u>regardless of the election outcome</u>.[1,2]

b) When the S&P 500 has been in a **downtrend** going into the election, the market has been **lower** 3 and 6 months later **60%** of the time, <u>regardless of the election outcome</u>.[3,4]

The bottom line: *Today, the S&P 500 is in an uptrend*.[5]

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[1] Strategas. October 29th.
[2] Since 1952. Uptrend defined as 50-day moving average above 200-day moving average.
[3] Downtrend defined as 50-day moving average below 200-day moving average.
[4] Strategas. Since 1952, there have been 18 elections:

a. 13 of them were in uptrends:
   - 2 x the S&P 500 was down 3 months later. 1968 -0.6% and 1976 -1.2%.
   - 2 x the S&P 500 was down 6 months later. 1972 -3.9% and 1976 -4.0%.
   - 11 x the market was higher.

b. 5 of them were in downtrends.
   - 2 x the S&P 500 was up 3 months later. 1960 +11.6% and 2004 +6.4%.
   - 2 x the S&P 500 was up 6 months later. 1960 +20.6% and 2004 +2.7%.
   - 3 x the market was lower.

[5] Bloomberg.

The index performance is provided for illustrative purposes only and is not meant to depict the performance of a specific investment. **Past performance is no guarantee of future results.**

2 We regularly counsel investors looking for opportunities to invest to be patient and wait for pullbacks.

Historically on one hand, November and December is seasonally the *strongest* two-month period of the year.[6] This would argue a near-term pullback is less likely.

On the other hand, that seasonal rally follows the *two worst* months of the year, September-October.[7] But that did not occur this year with the S&P 500 returning +3.0% during this period. Could the seasonality this year be different with November-December weaker than normal and thus offering a pullback?

By the way, I can't stand when forecasters give you the "on the one hand, and then the other" forecasts.

What does that do for us?

I believe November-December will repeat its historic strong performance once we get through the noise surrounding the election.

There are multiple reasons for this belief:

a) November is historically the largest execution month for corporate buybacks, the #1 buyer of stocks.[8]

b) November typically experiences sizable retail inflows into equities, especially in strong years, as investors reallocate.[9]

c) After listening to Q3 earnings conference calls, I am struck by the number of companies who have articulated their corporate customers are waiting for the certainty of the election to be behind them before making capital commitments. I think you could see more corporate activity post the election regardless of the outcome.

d) The Fed is likely to further cut rates on Thursday. While the magnitude of the cut could impact the magnitude of the potential rally, reducing rates is good for stocks no matter how much, as long as corporate earnings remain strong. Based on pretty good Q3 2024 earnings reports, I think that could be the case.

3 Getting more granular on point #1, pre-election performance trends tend to persist after the election *at the style and sector levels as well.*[10]

What has worked going into the election?

Style wise: year-to-date winners (*stock price momentum*) with good fundamentals (*earnings revisions*).[11]

Sectors: Some growth sectors (*communication services*), some value sectors (*financials*) and some defensive sectors (*utilities*).[12]

Therefore, what has *not worked* is a binary bet on one style, i.e. growth versus value versus defensive, which would have presumptively eliminated some of the sectoral winners.

Nor has the Magnificent 7 overall worked! Only 4 of the 7 are outperforming the S&P 500 year-to-date.[13]

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[6] Stockanalysis.com. Average return of the S&P 500 since inception in November and December is 3.3%.
[7] Stockanalysis.com. Average return of the S&P 500 since inception in September and October is -.38%.
[8] Goldman Sachs Tactical Flow-of-Fund. November. Since 1979.
[9] Goldman Sachs Tactical Flow-of-Fund. November. Since 1979.
[10] Evercore. November 3, 2024.
[11] Factset, October 31st, 2024.
[12] Bloomberg. I-share sector performance through November 1, 2024.
[13] Bloomberg. Performance of Google, Nvidia, Amazon, Meta, Microsoft, Tesla, Apple through November 1 ,2024.

Applied Equity Advisors has never believed in the segmentation of the market by styles.

Don't clients just want to make money, and do they really care if it comes in the form of growth, value, or defensive stocks?

4 The capitulation of some of the holdout bears is consistent, in my opinion, with the transition from the second to third year off a bear market low.

I like the boat analogy:

a) At the start of a bull market, the optimistic side of the boat is near vacant. The bearish side of the boat is packed, so crowded that the bearish side of the boat tips over (and therefore is wrong.)

   That crowding creates the best investment opportunities.

b) Yet heading into the third year, more and more investors embrace risk, moving from the bearish to the bullish side of the boat. Not crowded enough to tip the bullish outlook over, but the risk increases.

Ultimately that means market returns may regress lower. I doubt this is fatal for 2025, but perhaps the market return will not be as strong as the first two years (2023 and 2024) off the lows.

We'll address that more on our 2025 webcast, scheduled for January 16th, 2025. Please mark your calendars.

Andrew

Risk Considerations

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