1400 Dow Points Just Ain't What They Used to Be—I Don't Care What the Media Says

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I know the financial media likes to use words like "massive sell-off", "crushed", "tumble", "correction" and "free-fall", and print headlines asking if we are at long last about to see stocks fall off a cliff into a dreaded bear market. The thing is this: Don't mistake normal volatility with a bear market. A 1400-point decline in the Dow is merely a 5.2% decline—broadly not yet a correction (normally 10%) and hardly a bear market (a 20% decline).

And, even more interestingly than the headlines of the last two days is the stealth bear market that has been taking place under the radar in the S&P 500 for the year-to-date prior to the last few days. Twenty-five percent of the stocks comprising the S&P 500 are in bear market territory this year. That is good news as we prepare for the Q3 earnings season, which kicks off in earnest with J. P. Morgan reporting. Much better for stocks to enter earnings on the heels of a sell-off rather than a significant rise as we did in January/February of this year. Let's remember the indices are still in the black for the year: DJIA +1.4%; S&P 500 +2.1% and the NASDAQ +6.2%.

As someone who appears in the financial media, I don't want to discount the service these journalists provide to investors. I appeared on CNBC and NBR and will appear on CNBC's Closing Bell again today. These savvy journalists comb the market and the experts for insight, and explanations. But in the very short-term it is impossible to know exactly what triggers the selling unless you believe, as I do, that the algorithms utilized by floor traders read the headlines and react without context or experience. Just words in a headline: The Fed… Inflation… Trade War… and then massive selling programs. However, most of the experts the journalists interview feel the need to offer a reason, a special insight. Wednesday, I heard from many of my peers that the blame belonged to Fed Chairman Powell's comment that we are a "long way from neutral" causing investors to worry that rate hikes will march along into infinity, surging inflation, worries about third quarter earnings disappointing and the trade tariffs eating into profits (this after a single warning from PPG about tariffs causing rising raw material costs). All of the above may prove out to be true eventually—but it is impossible to ascertain in the near term.

Let's consider what is going right:

- 77% of the tax cuts went to individuals. Consumer spending is up 3.5% this year and the consumer is healthy—with modest debt in comparison to 2008. We think that the benefits of the tax cut will carry into Q2 2019 with increased tax refunds for individuals thanks to the improvement in the Alternative Minimum Tax (largely underestimated).

- Lowest unemployment rate since 1969 at 3.68%

- Wage pressure is modest at 2.8% versus inflation at 2.3%

- Inflation is under control and has not spiked above 3% for 20+ years. The CPI is hovering just above 2%. If anything, the trend is toward deflation.

- The Fed is hitting all their targets—which is why they are raising rates. They are not being aggressive, they are being prudent. If the economy is as strong as it appears, monetary policy must be normalized. The real Fed Funds rate just crossed over into positive territory—we have room for rates to rise before having a negative impact on stocks.

Of course, there is always plenty to worry about. The trade war, if protracted, will eventually slow earnings growth and put upward pressure on inflation. If the Fed increases too much, too fast the economy will roll over. Earnings growth is slowing—that is expected, but margins are at historical highs of 11.5% and we will be watching. Same with top line growth. The upcoming earnings season will provide clarity and stocks are cheaper than they were two weeks ago. That is good news for investors.

We are not perma-bulls, we just don't believe that this is the cliff many claim it is. As I write, the futures are up over 150 points on the Dow. We will see. But markets are not made in days, rather over weeks and months and years. The economic expansion is the second longest in history since The Civil War. A great deal is going right. Eventually the party will end and we will be contemplating and anticipating the signs, and acting on your behalf to protect your wealth and your legacy.

Call your wealth advisor if you would like to participate in a call with Paul Dickson, our Director of Fixed Income, and me in the coming weeks. We welcome the opportunity to speak with you and share our thoughts and ideas.