Weekly Market Review

***e*Research Corporation** is pleased to provide a review of the markets by Eddy Elfenbein of **Crossing Wall Street**.

Mr. Elfenbein introduces his commentary with the following quote from Charlie Munger (Berkshire Hathway):

"People calculate too much and think too little."

Read Mr. Elfenbein's analysis and market comments on the following pages.

Information about **Eddy Elfenbein** and **Crossing Wall Street** is provided at the end of this article. You can also learn about **Crossing Wall Street** by going to its blog website at: http://www.crossingwallstreet.com/.

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Bob Weir, CFA
Director of Research

December 8, 2017

Crossing Wall Street: Weekly Market Review

by Eddy Elfenbein

BW: We have taken only an extract of Mr. Elfenbein's latest weekly article. If you wish to read the entire article, which includes stocks in his recommended portfolio, there is a link provided below.

On Thursday, the S&P 500 finally halted its four-day losing streak. The damage was very minor, and the major indexes are still very close to all-time highs.

I have to say that the recent market environment has been nearly picture-perfect; interest rates and inflation are low, corporate profits are growing, and consumer confidence is soaring. The S&P 500 has traded above its 200-DMA continuously for 18 months. I will warn you—this won't last!

Lately, some big-name tech stocks have been getting knocked about. At the same time, Wall Street has been favoring cyclical stocks. The Dow Transports, for example, recently broke 10,000 for the first time ever. This could be the start of a major rotation.

We also have a big Fed meeting coming our way next week. Expect another rate hike. I think it is a mistake but, alas, they didn't ask me.

Wall Street Turns from Tech to Cyclicals

While the stock market has remained strong, quietly there has been a changing of the guard. Recently, big tech stocks have been lagging the market. Bear in mind what a good year it has been for them. The tech sector has made up nearly half the S&P 500's gains this year. If you lump Amazon in with the techs, then it is more than half.

Tech first started to lag the market last Tuesday, November 28. It then got much worse for tech on Wednesday, November 29. After that, tech stocks appeared to stabilize, but lagged again this past Monday.

Overall, the impact has not been earth-shaking, but it is interesting because it has been so new. For so long, large-cap tech was such an easy trade. (There was a brief hiccup in June, but that didn't last long.)

Here is what is important: The flip side of lagging tech is a buoyant environment for cyclical stocks. By cyclicals, I mean stocks whose businesses are heavily tied to the economic cycle. You may own a wonderfully run homebuilder or chemical maker, but their prospects are always at the mercy of where we are in the cycle. Investors need to understand that.

We can see a good example of this by looking at the **Consumer Discretionaries ETF** (XLY). This sector was a giant winner at the start of this bull market. Their out-performance lasted for years, but starting about two years ago, the Consumer Discretionaries started to lag. Not badly, but they did fall behind. Lately, however, they have been rock stars.

Similarly, the **Dow Transports** (^DJT) have been popping. This is an old-time index of 20 stocks involved in the business of moving people and things about. For the first time ever, the Transports broke 10,000. I wonder how many investors are aware that **CSX Corporation** (CSX), a boring old railroad, is up 56% this year. That is more than all the FAANG stocks.

If we drill down a little, one of the best-performing sectors of the cyclicals has been the home-builders. **NVR** (NVR), for example, is a $3,400 stock that has more than doubled this year. After a long brutal stretch, things are finally looking up for the housing market. Home prices are rising at their fastest pace in three years. Last week, we learned that new-home sales jumped to a 10-year high. It is all about the cycle.

We are also seeing new-found strength in financial stocks. The theme seems to be stocks that do the financing, and stuff that is bought via financing.

What Does This Rotation Mean for Us?

What does this shift to cyclicals mean? I suspect that this is the market's confirmation of some recent good news for the economy. As we have noted before, consumer confidence is at a 17-year high. Inflation is still low. Housing is coming back. GDP growth for Q2 and Q3 were pretty good, and it looks like Q4 may even top those two. Simply put, the economy is doing well, and the market's rotation is reflecting that.

Another reflection of the improving economy is the flattening of the yield curve. The spread between the 2- and 10-year Treasury yields recently fell to just 53 basis points. That is down from 130 basis points less than a year ago, and 260 basis points four years ago.

The yield curve is going to get flatter soon. The Federal Reserve is getting together next week, and it seems certain that they will raise interest rates again. The central bank has said it sees three more rate hikes next year, plus another three in 2019. I think the prospect of three hikes in 2018 has a good chance of happening, but I am not so sure about 2019.

At the upcoming Fed meeting, the Fed will update its projections. I will not be surprised if they walk back their 2019 forecast.

The reason is the key part of the flattening yield curve—long-term rates are not moving that much. In fact, long-term yields are lower than where they were at the start of the year. Frankly, I am not sure why that is.

Fortunately, we are not economists, and we do not have to overly concern ourselves with why something is happening. As investors, it is good enough to know that it is happening. Shortly after the election, we saw a similar rotation away from tech and towards cyclicals. However, that move was matched by a sharp drop-off in long-term bonds. We are not seeing that this time.

This means that bonds are still pretty weak competition against stocks. While stock valuations are elevated (but not extreme), you can still find good deals.

The big news next week will be the Federal Reserve meeting. It will be a two-day meeting, on Tuesday and Wednesday. After the meeting, Janet Yellen will be holding a press conference. The Fed will also update its economic projections for the next few years. Then, on Thursday, we will get the retail-sales report and, on Friday, the industrial-production report comes out.

Be sure to keep checking the blog for daily updates, and I will have more market analysis for you in the next issue of *CWS Market Review*!

Here is an interview I did this past week on Bloomberg.

- Eddy

BW: In the rest of the newsletter, Eddy reviews the earnings announcements of the companies on his Buy List. You can read about them and the entire article by clicking on the following link:

http://www.crossingwallstreet.com/archives/2017/12/cws-market-review-december-8-2017.html

Named by CNN/Money as the best buy-and-hold blogger, Eddy Elfenbein is the editor of Crossing Wall Street. His free Buy List has beaten the S&P 500 for the last six years in a row. This email was sent by Eddy Elfenbein through Crossing Wall Street.

BW: Information on Eddy Elfenbein and Crossing Wall Street follows on the next page.

ABOUT THE AUTHOR

Welcome to Crossing Wall Street

I started this Web site to help individual investors. I have to admit that I *love* the stock market. I think I must be an addict. In my opinion, the stock market is one of the greatest inventions in history. The stock market is simply the most consistently successful way to make money over the long term. Even after the financial crisis, stocks have still beaten every asset category over the long haul—bonds, commodities and real estate.

While the stock market may bounce around from day to day, and even month to month, the long-term trend has always been higher. Over the last 35 years, stocks have gone up 35-fold. And since the end of World War II, the stock market is up an amazing 120,000%. I wish I had been around! That was the beginning of an American financial revolution. Today, we’re at the beginning of a *global* financial revolution. That is why I think the next 70 years will be even better.

The key to doing well on Wall Street is actually very simple: Buy and hold shares of outstanding companies. But too many investors never learn this valuable lesson. Or if they do learn it, they learn it the *hard* way. That is where I come in. I want to help investors avoid the mistakes that separate successful investors from those who always find themselves spinning their wheels.

There are lots of pitfalls on Wall Street. From shady companies that are more popular than they are profitable to a mutual fund industry that is more interested in its fees than serving investors. Todayis investors must be careful.

At Crossing Wall Street, I give investors my free and unbiased view of the market. I probably analyze dozens of companies every week. I am always looking over income statements and balance sheets. I’ve spent several years collecting my list of the best companies to own. This is my current Buy List. I’ve included a description of each company and its current share price. These are the ones that I make the most effort to follow on the site, but please feel free to ask me my opinion on any stock. I don’t receive compensation from any of the stocks I recommend. Also, I don’t “short” any of the stocks I criticize. At any time, I may own the companies on my Buy List. All of the information on this site is free and unbiased. I also have a section for Frequently Asked Questions that will help you learn more about Crossing Wall Street.

Please feel free to e-mail me. I enjoy getting feedback from investors. I am happy to give you my opinion on any stock or investing in general. I should warn you that I cannot give out personal portfolio advice, but all other topics are fair game. You can also check out some of my favorite links.

- Eddy Elfenbein

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