



THE DANA VIEWPOINT

October 29, 2018

Dow: 24,443

Trick

Or treat? This October, like some past Octobers, has offered up a market correction. The major indexes are down about 10%, with small caps and some of the large tech leaders down more than 10%. Recent darlings, such as Amazon and Netflix, are down about 20% and 30%, respectively. We really shouldn't be surprised when stocks with P/E's of 50 to 100 and year-to-date returns of 50% to 100% undergo a correction. These stocks should be expected to exhibit downside volatility that is similar to their upside volatility when their future growth rates are questioned. High P/E stocks are most sensitive to changes in their expected growth rates in the future. Also, all market trends typically both overshoot and undershoot their natural equilibrium points.

It is impossible to time market corrections, even in hindsight. There are any number of factors that are being held responsible for the current correction. Certainly earnings growth will slow from the 20% rate we have seen the last few quarters, but it isn't showing any signs of slowing this quarter. The Fed and higher rates could be held responsible in the future, but certainly not now. The 10-year Treasury is still in the low 3's, and has only crept up at about the rate of recent short-term rate increases. No serious signs of inflation have reared their heads yet. A China slowdown has been pointed to as a possible factor, and its currency and stock markets are certainly struggling this year against the almighty dollar. Not only is earnings growth strong this quarter, but the advance estimate for Q3 GDP is at 3.5% following a second quarter that was revised up to 4.2%. These are the strongest two quarters of GDP growth that the U.S. has experienced in four years.

So will earnings growth 'peak' at some point in the future? Of course, and it most certainly will start slowing from its current 20% growth rate soon. There is no recession on the horizon, and the correction we are having does not seem to be anything more than that. Corporate bond spreads have behaved, there has been no huge rally in Treasuries, and

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inflation still seems to be well behaved with commodities prices near their average level for the year. Even Yeti, the premium cooler maker and ‘lifestyle’ brand, was able to get their IPO done last week at 2X last year’s sales. As for the correction, the current health of the economy indicates this too shall pass.

Random Thought for October 2018: Uncertainty breeds opportunity.

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