

Six Week Market Recap: How Fundamental Data Has Impacted Cabana's Allocation

We hosted our monthly advisor webinar on Friday and touched on a variety of tools and resources we have in the works at Cabana, as well as the markets' performance over the past six weeks. We often receive questions from advisors about how and when we know to reallocate portfolios, and this past week was no different. I'd like to use today's commentary to walk through our process and how you can follow along.

Our rules-based investment process:

First, let me say that we are not psychic, and we do not have all the answers. What I believe we do well is recognize what is important and what is not. We also have a rules-based process that is integrated into our algorithm and reflects a simple but time-tested approach to investing. Our algorithm is monitoring interest rates, earnings and price. These data points form the foundation of our investment process. In other words, these simple pieces of information give us clues as to what assets will be attractive and what assets will not. When combined, they can form a powerful tool for investing. We do not always get it right nor do we expect to. We do however want to put odds of a correct decision in our favor as much as possible.

With that, let's take a look at what we have reported in our commentaries since September. I believe it will give considerable insight into our process of allocating assets.

A look back at the past six weeks:

September 30: We noted continued mixed messages in the market. While markets saw selling and we were in a technical manufacturing recession, jobs numbers were strong, the yield curve was improving, and we were only 2% below all-time highs in the major indexes. We called the glass "half full" and commented that dividend payers, defensive equities and real estate were attractive. Shortly after this commentary our algorithm signaled a reallocation to less risky assets.

October 7: We felt that the jury was still out and explained that the previous six months of rangebound volatility would result in the market giving us a "verdict". We were looking for a breakout above or below the range and provided the levels on the S&P 500 that we were watching (2720 and 3000).

October 14: We suggested that the "news" doesn't matter. What does matter is interest rates, earnings and price. We noted that earnings would ultimately carry the day and were looking forward to the beginning of earnings season the following morning.

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October 18: Our algorithm signaled a reallocation to more bullish conditions. This was primarily due to changes in price of the broad markets, as well as initial earnings reports that had come in over the previous three days. Our algorithm observed that things were “better” and that we should reallocate to assets that outperform in a “better” market environment. We began the process of reallocating our portfolios and notified our advisor partners.

October 21: We noted stellar earnings reports from financial institutions and outperformance in the transportation sector. At that point, the yield curve had maintained a better spread between short- and long-term interest rates. We also pointed out that equity markets were right at all-time highs and we were watching for a breakout and fourth quarter rally.

October 28: The breakout above 3000 on the S&P 500 had occurred. We identified rotation into higher beta assets as further evidence that professional investors were reallocating in response to growth prospects improving. We were watching for buying in energy, commodities and transportation. As soon as we said it, that’s what occurred.

November 4: We pointed out that the fourth quarter rally was officially on us, and were watching for outperformance in risk assets like small caps, emerging markets and industrials in order to continue.

November 6: We provided a chart visually showing positive money rotation into risk assets and out of defensive positions during October and early November.

November 11: We discussed the rally and what to expect going forward. We highlighted improvements in global markets and how that could provide support to our market going forward. Lastly, we talked about how markets are forward looking and how that coincides with the performance we saw in 2018 and this year.

What’s happening now?

As of today, 92% of companies have reported earnings. Of those, 75% have beaten estimates and 60% have reported positive sales surprises. Year-over-year earnings growth is 9%. The 10-year Treasury is at 1.81%, up from 1.55% at the beginning of September. The spread between the 10-year and 2-year Treasury has increased 20 basis points during that time. These fundamental data points are what matters and is what is driving the rally we are currently seeing in equity markets. It is also what dictated our decision to reallocate to more bullish conditions on October 18, when price improved. Since then the market has rallied almost 5%. While price had not officially broken out on October 18, things underneath the hood were getting better. Things that matter like interest rate spread and earnings. Those factors increased the chances that the improvement in price was meaningful and that a reallocation to assets that would benefit from these conditions was appropriate. As an investor, that is all you can do - gather relevant information and make investment decisions accordingly. But what is relevant information? Each of us must make that determination on our own and on our own terms.

I hope this outline, as well as review of our commentaries over the past weeks, will help our partners and clients better understand our process. We are far from perfect, but we try to always be transparent. Allocation history back to 2017 can be found [here](#).



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