LPL FINANCIAL RESEARCH

Weekly Market Commentary

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January May Seem "Super," but Don't Be Bowled Over

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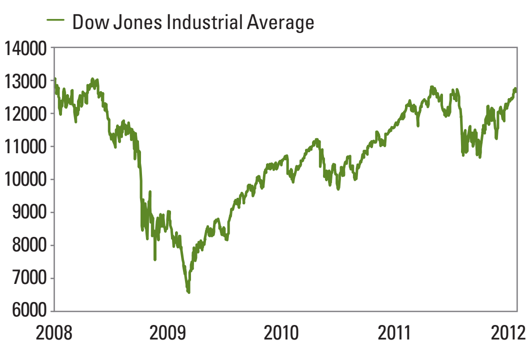
Highlights

- The upcoming Super Bowl will test the stock market's historical correlations with the calendar and events that proved rewarding to investors in 2011.
- Investors' New Year's resolution may have been to buy stocks after five years of selling nearly every month. However, we are afraid this may turn out to be like most resolutions and fade come February.
- We expect volatility to return and the stock market to shed some recent gains. But we adhere to our outlook for 8–12%* gains for the year for stocks.

*LPL Financial Research provided this range based on our earnings per share growth estimate for 2012, and a modest expansion in the price-to-earnings ratio.

1 Dow Jones Industrial Average Near Three-and-a-Half-Year Highs



Source: LPL Financial, Bloomberg Data 01/30/12

Last week, the Dow Jones Industrial Average (DJIA) hit a new three-and-a-half-year intraday high [Chart 1]. Earnings, gross domestic product (GDP), and consumer spending are already back to new highs, so seeing the stock market return to pre-financial crisis levels seems reasonable.

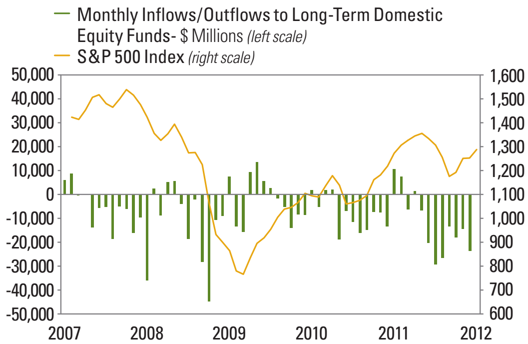
January's gain sets a positive tone for the year. When January was positive for the S&P 500, the year as a whole ended with a gain 90% of the time since WWII. This historical relationship is called the "January effect." Last year, each of these time-worn axioms based on the calendar actually worked for investors. For example:

- "Sell in May and go away," which suggests investors sell and avoid the summer months, worked with stocks peaking for the year on April 29.
- October, the "bear killer" month when stock market downturns famously end and reverse in the month of October, ended the 19% peak-to-trough stock market decline with stocks bottoming for the year on October 3.
- A "Santa Claus rally" in December produced gains in the week between Christmas and New Year's.

Although not based on the calendar, and more than a little bit tongue-in-cheek, another classic stock market indicator worth mentioning this week is the "Super Bowl indicator." Last year, both teams were original NFL teams and the DJIA posted a modest gain for the year. The Super Bowl indicator shows that the DJIA goes up for the year as a whole when the winner comes from the original NFL (NFC team or an AFC team from the pre-1970-merger NFL—like the Steelers or Colts). But when an original AFL or expansion team wins, the DJIA falls. Going into the 1998 Super Bowl when the underdog Denver Broncos defeated the Green Bay Packers, the Super Bowl indicator had been correct in 28 of 31 years.

However, since 1998, the Super Bowl indicator has had a poor record; it has only been correct about 50% of the time over the past 13 years. The most notable failure was the New York Giants' upset win in 2008 over the New England Patriots, which was supposed to bring about a bull run for stocks—instead the Dow plunged that year as the financial crisis took hold. This year's rematch of the 2008 contest will be on Sunday, February 5. While a win for the Giants would suggest gains for stocks in 2012, using longer-term history as a guide, it is unlikely that this event holds any significance for the stock market. In fact, make that highly unlikely.

2 January Brings a Break in the Selling



Source: LPL Financial, Investment Company Institute, Bloomberg Data 01/30/12

Past performance is no guarantee of future results.

Individual investor buying is more likely to empower a rally than historical correlations with the calendar or a sporting event. Investors' New Year's resolution may have been to buy stocks. Individual investors appear to be beginning to "put a toe back in" to the stock market after five years of selling stocks nearly every month. Data on mutual fund cash flows for the month of January suggests that investors are finally once again buying U.S. stock mutual funds—or have at least temporarily stopped selling them [Chart 2]. However, we are afraid this may turn out to be like most resolutions and fade come February.

We expect volatility to return and the stock market to shed some recent gains. But we adhere to our outlook for 8–12% gains for the year for stocks driven by 7% earnings growth and a slight improvement in valuations. In the near term, the recent four weeks of back-to-back gains may give way to a modest pullback, but we expect several factors to mitigate the extent of the slide including upcoming rate cuts in China, solid manufacturing and employment data in the United States, and further steps toward stability in Europe. ■

The Standard & Poor's 500 Index is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

Correlation is a statistical measure of how two securities move in relation to each other. Correlations are used in advanced portfolio management.

Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory.