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TIME FOR A PAUSE?

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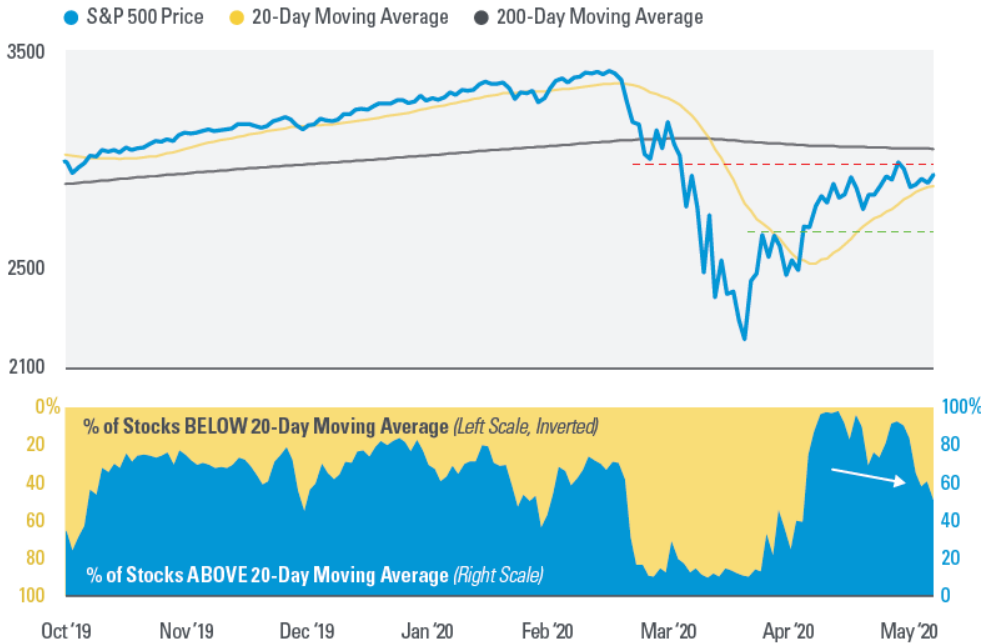
Stocks have had a historic run amid increasingly negative headlines. Historically, stocks have tended to lead the economy, and while a second-half rebound may be likely, some equity weakness over the coming months is also possible. The historically worst six months of the year have officially started, and combined with technical warnings, that suggests stocks may take a well-deserved break soon.

TECHNICAL WARNING SIGNS GROW

In April, the S&P 500 Index had a historic rally off the March 23 lows, gaining more than 31% through April 29. The strength of the move, as well as internal data, suggests that a full retest of the March 23 lows may not be in the cards. While this is encouraging long term, recent price action combined with seasonal headwinds may point to a possible pullback.

The S&P 500's 20-day moving average has been closely watched by investors in recent months, as the index has traded off the average, first as resistance in late March and more recently as support [Figure 1].

1 FEWER STOCKS HOLDING THEIR 20-DAY MOVING AVERAGES



Source: LPL Research, Bloomberg 05/07/20

All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

This metric can also be applied to individual stocks. On April 14, a record 99% of the components in the S&P 500 traded above their respective 20-day moving averages, a bullish long-term signal showing the strength of buying in equities. As the S&P 500 went on to make a new high in late April, however, fewer stocks remained above that moving average. In recent days that number has fallen to 47%, the lowest since April 3, which tells us that recent gains are being led by fewer stocks. In fact, the top five stocks in the index now have a positive year-to-date return, while the overall index is still down nearly 10%.

Finally, last week's reversal near 2940 occurred almost exactly at a closely watched retracement level of the bear market decline and represents a place where short-term traders may want to consider taking profits. The 200-day moving average can be found just above that level, at 3001, representing a high bar for the next leg up in equity prices.

We believe the S&P 500 can make it through these levels in 2020, but we wouldn't be surprised to see a consolidation of recent gains in the meantime. To the downside, we see technical support at 2650, which sits about 10% below the April 29 highs. A correction of this magnitude would be consistent with previous pullbacks following initial spikes off bear market lows.

SELL IN MAY

One of the best known investment axioms is to "sell in May and go away." That's largely because these next six months—May through October—historically have been some of the worst six months of the year for S&P 500 returns. While the next six months have tended to be on the weak side, we just left the historically strongest six months for the S&P 500 [\[Figure 2\]](#).

2 SELL IN MAY?

Various S&P 500 Index 6-Month Returns (1950-Current)

6-Month Period	Average % Change	% Higher
Nov–Apr	7.0%	78.3%
Oct–Mar	6.2%	68.6%
Dec–May	5.5%	72.5%
Sep–Feb	4.7%	68.6%
Aug–Jan	4.5%	70.0%
July–Dec	4.5%	70.0%
Jan–Jun	4.3%	69.6%
Feb–July	4.1%	71.4%
Mar–Aug	4.0%	71.4%
Jun–Nov	3.1%	67.1%
Apr–Sep	2.5%	64.3%
May–Oct	1.5%	64.3%

Source: LPL Research, FactSet 04/30/20

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The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

Given that stocks recently experienced a rally of more than 30% off the March 23 lows, and we're entering a potentially inconsistent part of the calendar year, we believe some weakness in stocks may be likely over the coming months. A few other points regarding the historical May–October S&P 500:

- The S&P 500 actually has gained during these “worst” six months seven of the past eight years.
- When S&P 500 returns in the best six months of the year were lower (like they were this year), the next six months were down 3.8% on average and higher only 7 of 15 times, with an average pullback of 16.4%.
- When stocks have been down year to date heading into May (like 2020), stocks in the next six months have been down 2.7% on average, with an average pullback of 14.8%.
- Last, when the S&P 500 began the worst six months beneath its long-term 200-day moving average (like 2020), then the next six months have been down 2% on average and have had an average pullback of 15.4%.

CAUTION IS WARRANTED

Given the current technical warnings and seasonal headwinds, equity weakness may make sense now, but the possibility of a full retest of the March 23 lows may be quite low.

Based on our analysis of valuation, technical, and sentiment factors, we anticipate that a potential pullback in stocks, possibly around 10%, may create a more attractive entry point for more tactical investors. Historical patterns after bear market lows support this view, and we continue to recommend patience.

For long-term investors, we continue to believe stocks may be more attractive than bonds at current valuations, and we recommend overweight allocations to stocks, and a corresponding underweight to fixed income for suitable investors.

Our year-end 2020 fair value target range for the S&P 500 remains 3,150–3,200, less than 8% from the May 8 close at the low end of the range.

IMPORTANT DISCLOSURES

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The Standard & Poor's 500 Index (S&P500) 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.

All index data from FactSet.

Please read the full [Outlook 2020: Bringing Markets Into Focus](#) publication for additional description and disclosure.

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