Churchill Management Group

Monthly Market Update

May 12, 2020

TACTICAL STRATEGIES

PREMIER WEALTH TACTICAL & PREMIER WEALTH TACTICAL CORE

Sudden market drops often invite sudden snap backs, and both have now been experienced by the market over the past three months. Thanks to $8 trillion plus in stimulus from the Federal Reserve and the Treasury, optimism on multiple fronts resulted in the best monthly gain on the major indices since 1987. It was also the best April since 1938, with the Nasdaq, S&P 500 and the Dow all posting double-digit gains. It should be noted that throughout history, the best trading days, weeks, months, almost always follow the worst. It is likely to take a while before we know for sure that the coast is clear, despite how markets have reacted over the last few weeks.

Since bottoming out in March, the retracements for the Dow Jones Industrial Average, S&P 500, and Nasdaq have been 57%, 63%, and 77%, respectively. While the oversold bounce for the DJIA and the S&P 500 are still within the normal range, the Nasdaq has shown some exceptional strength.

The Nasdaq has been buoyed by the mega cap technology companies that have been little affected by the quarantine. Many tech firms have even seen growth as their products help enable people and organizations to work remotely. The tech-heavy index also has a large share of the biotech and healthcare industries that are benefitting from the pandemic.

Earnings season is in full swing and it is apparent that Wall Street has already looked beyond what might be bad numbers for Q1 and the next couple of quarters. Stocks seemed to be rewarded with gains regardless of whether they met or missed their targets.

Fundamentally, earnings visibility remains very poor going forward, with many companies withdrawing any guidance for the rest of the year. On the plus side, the monetary and fiscal stimulus has had its intended effect, at least buying the economy some time. Despite a bleak economic outlook, the markets have looked past the near-term issues and appear firmly focused on the

recovery. Analysts have latched on to the idea of a rebound and are quite bullish, baking in a recovery and record earnings by 2021. That would be a challenging achievement.

In terms of valuations, the sharp rally has put the markets in rarified territory, with the forward P/E Ratio at its highest level in 18 years. The forward P/E passed 20 last week, the first time it has hit that height since April of 2002.

Sentiment has been strangely resilient, with the Advisory Sentiment (professional) and AAII surveys (retail) showing moderate readings despite what appears to be the biggest economic disruption since the 1930s. Advisory Sentiment is still more positive on a weekly level than the reading in January of 2019. Meanwhile, the AAII outlook has barely budged, with most investors more bullish than even levels seen in October of 2019. Capitulation in the form of extremely bearish readings would qualify as an indicator of a bottom, but we are clearly not there yet.

Technically, the markets have rallied straight off the lows in a V formation without the normal bottoming process seen historically. Can markets recover and make new highs? While possible, we believe the odds of that are low that this could happen without some type of consolidation phase at the least.

One exogenous event with which to draw a parallel may be 9/11. Like Covid-19, the events of 9/11 created a sharp sell-off, followed by a very sharp recovery. The market bounced from the end of September 2001 into the first week of January 2002, but then ultimately failed. The difference was that 9/11 occurred in the middle of a Bear Market, although we can agree that these exogenous events likely do not care about where in the market cycle they happen to occur. The government bailed out the airline industry then, but today they are trying to do the same for a whole slew of industries including travel, hospitality, retail, restaurants, and more.

Only time will tell what the ultimate consequences will be for shutting down an economy for this long a period. What percentage of businesses will close permanently? How many of the job losses will never come back? How long before consumer activity returns to pre-pandemic levels? With so many unknown variables, there is no shortage of questions. Visibility is the worst since the financial crisis, and we expect the shadow cast by the coronavirus will be a long one.

Markets do not go straight down nor straight up. The indices have shifted from extremely oversold to now being extremely overbought, which often calls for a period of consolidation. The action during a consolidation should yield some more insight into the sustainability of the current rally or if we will experience a test of previous lows. We will keep a close eye.

TACTICAL OPPORTUNITY

After seeing the sharp selling in March, the portfolio has now formed a nice looking group of core stocks. Holdings include Microsoft, Walmart, Alphabet, Amazon, Home Depot, and Apple. The

snapback rally in April did allow for some increased exposure with the addition of four holdings, including two from the healthcare sector. Cash levels remain decently high.

FULLY INVESTED

ETF SECTOR ROTATION

The Energy sector put up the best numbers among the sectors in April. After monthly declines of 11%, 15%, and then 36% in January, February, and March, respectively, Energy led for the group, with more than a 20% return since April 1. Unfortunately, that still adds up to a compounded decline of over 35% for the first four months of the year for the sector.

The Consumer Discretionary sector also rallied nicely – some 20% – in April despite awful retail numbers for most. That is because Amazon, which accounts for a fifth of the sector, saw a surge in business due to Covid-19. Technology also remains a strong performer. Not surprisingly, the defensive Consumer Staples lagged in the bounce back, although the group was still up for the month.

We remain overweight Tech and Healthcare, and less significantly so in Consumer Discretionary, Consumer Staples, and Communications. In the broad markets, Growth outpaced Value, despite it being an opposite type of snapback month. Small Caps performed better than the general market, as they had been the hardest hit in the coronavirus crash. Therefore, the rebound in this group was likely a retracement after being oversold. Globally, we continue to prefer the U.S. over holdings in both Europe and Emerging Markets.

EQUITY GROWTH AND VALUE

Familiar names such as Apple, Facebook, Amazon, and Home Depot all posted nice months in April. Welcome pops also came from some recent purchases, including Zebra Technologies, Chipotle Mexican Grill, and Thermo Fisher Scientific. Our focus has remained on the growth side of the ledger.

EQUITY DIVIDEND INCOME

After seeing tremendous activity in March for tax-harvesting and rotational adjustments, April stayed fairly quiet as we rode the bounce. Our mix has largely excluded Financials and, until recently, Energy, which has given our dividend portfolios more stability when compared to most dividend indices during the recent choppiness. It would not be surprising to see a pickup in activity given the market's behavior.

For a full description of each strategy, please click here.

Best regards,

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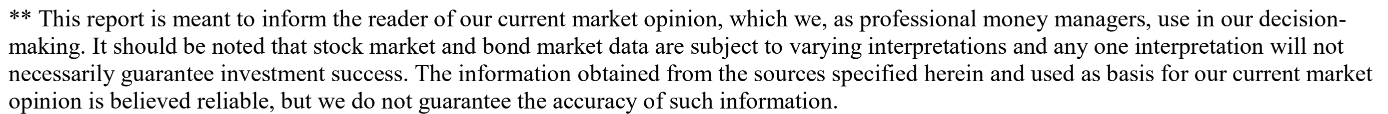

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