

Should investors be scared of a Halloween sell-off?

Weekly Market Compass: There are five main issues that could be causing concern for investors, but I believe an October sell-off looks unlikely

Oct 21, 2019 | Kristina Hooper, Chief Global Market Strategist

Many people around the world observe Halloween in the month of October, celebrating all that is spooky and macabre. My kids have all been enthralled with Halloween, choosing their costumes several months in advance (one year, my older son insisted on wearing his costume every single day of the month of October). And plenty of adults who have outgrown trick-or-treat still believe that October would not be complete without horror movies running non-stop throughout the month. But no matter if you celebrate with cute kids' costumes or elaborate haunted houses - what makes Halloween fun is the knowledge that the scares aren't real.

October is viewed as a scary month for the stock market as well. After all, some of the biggest stock market crashes have occurred in October, such as the Panic of 1907, the 1929 crash, and the 1987 crash. We even witnessed a significant stock market sell-off last October. However, if we were to look at the overall statistics, we would see that October has not historically been the worst month for stock market performance. In fact, there is even a name for this behavioral finance phenomenon - "the October effect."

Investopedia describes it as "a perceived market anomaly that stocks tend to decline during the month of October." However, it is perception - not reality. As the definition goes on to explain, "The October effect is considered mainly to be a psychological expectation rather than an actual phenomenon as most statistics go against the theory."

And yet, in my recent interactions with clients, I have sensed a high level of trepidation about this particular October, given the uncertainty we see around many issues. While stocks have eked out gains thus far in the month (with the MSCI World Index up 0.7% and the S&P 500 Index returning 0.32% from Oct. 1 through Oct. 18),¹ clients still seem to be waiting for the proverbial shoe to drop.

So this week, I want to face these fears more closely. What issues are frightening investors today, and what are the chances that these issues could lead to a sell-off by Halloween?

Five issues that might be scaring investors in October

Weak China data

Third-quarter gross domestic product (GDP) growth clocked in at 6.0% annualized (versus 6.2% in the second quarter).² This is the weakest pace in more than two decades. This could be very worrying to markets. That's particularly so since a slowdown in China has usually resulted in a slowdown in Europe and potentially has global implications.

However, even if this data causes jitters among investors, I believe the fear will be very short-lived. After all, 6% GDP growth is still nothing to sneeze at - and it meets the low end of the target range set by China for 2019. It is worth noting that some GDP growth forecasts have been downwardly revised to 5.9% annualized in the fourth quarter. But I believe China will work hard to hit the 6% target. Chinese Premier Li Keqiang, who is technically responsible for the economy, has been encouraging local government officials to provide stimulus for their respective economies. Li told local governments they must "enhance the sense of urgency and responsibility" to ensure stable economic growth and "must put growth in a more prominent position" on their work agenda, according to an Oct. 14 statement on the government's website.³

The US-China trade situation

We are already seeing a chasm in what the US believes and what China believes about phase one of the trade negotiations. To me, this suggests a greater likelihood of a breakdown in negotiations. We also know the power that news flow around US-China trade talks has had on stock market performance. However, I am hopeful that investors will not have outsized reactions to any news on US-China trade talks, as I believe that there will likely be ups and downs, but no resolution in the near term.

Weak US economic data

Last week, we received some disappointing US economic data. September retail sales fell 0.3% from the previous month when they were expected to actually rise 0.3%.⁴ In addition, September industrial production was also weak, down 0.4%.⁵

While a few data points are not conclusive, we will want to follow upcoming US data releases closely. While employment has been strong, many consumers are vulnerable to an economic downturn because they lack adequate savings. For example, a recent survey showed that 60% of Americans would be unable to cover an unexpected \$1,000 expense, such as an emergency room visit or car repair, with their savings.⁶

However, I believe economic data will remain relatively strong in the short term, and I believe any negative economic data might be treated positively, given that it increases the likelihood that the Fed becomes more accommodative.

The Federal Reserve (Fed) meeting Oct. 29-30

Last October, Fed Chair Jay Powell's hawkish comments helped cause a sell-off. And so it stands to reason that an unpopular rate decision - or simply hawkish words from the Fed chair - could be enough to cause another sell-off this month. However, I believe that is unlikely because I expect the Fed to be extremely careful in its wording at the press conference in order to avoid such a fate.

Geopolitical disruption.

Political turmoil in various areas around the world, such as Brexit and the Hong Kong protests, might cause investors to worry as well. However, I believe that markets have become desensitized to most geopolitical turmoil and so, barring some highly unusual development, I expect such events to have little to no impact on stocks.

In summary, it's understandable for investors to be wary this October, but at this point, I believe it's unlikely that this trepidation will turn into a full-blown sell-off. This Halloween, I expect the biggest scares to come from haunted houses and horror movies - not from the stock market.

Source

¹Source: Bloomberg, L.P.

²Source: National Bureau of Statistics of China

³Source: South China Morning Post, "China's economy cause of growing concern in Beijing as US-China trade war takes toll on growth," Oct. 15, 2019

⁴Source: US Commerce Department

⁵Source: US Federal Reserve

⁶Source: Bankrate, January 2019

Important information

The MSCI World Index is an unmanaged index considered representative of stocks of developed countries.

The S&P 500® Index is an unmanaged index considered representative of the US stock market.

Gross domestic product is a broad indicator of a region's economic activity, measuring the monetary value of all the finished goods and services produced in that region over a specified period of time.

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