What Happened to the Santa Claus Rally?

The so-termed “Santa Claus Rally” says that stocks have a high likelihood of rallying in the final trading days of the year (after Christmas), often extending into the first couple of days of the new year. The statistics on this seasonal pattern vary depending on who you ask and what timeframe is being used. Generally speaking, though, the consensus is that stocks have a greater than 60% chance of going up during this period, based on history.¹

But Santa never arrived in 2022.

Instead, U.S. stocks gave up some of the strong gains posted from mid-October through the end of November, ending the year with a whimper.

The Santa Claus Rally Didn’t Happen in 2022

The lack of a late December rally has some arguing that it could be a sign of things to come in 2023. Part of the Santa Claus market lore is that a rallying market at year-end, and early in the new year, has been a good predictor of the gains to come. But an investor needs only a look back to 2021 to see the fallacy in this argument. During the 7-day Santa Claus rally period of 2021, the S&P 500 notched a solid +1.4% gain. 2022’s bear market started the next day.

Now that we’re in a new year, some investors are looking for signs that the “January Effect” is taking hold. This seasonal quirk says that stocks – and in particular smaller, value stocks that experienced selling pressure in the previous year – tend to rally in the early days of January. The causes for this supposed rally range from hopefulness in a new year to investors repurchasing stocks following year-end tax loss harvesting.

Next up on the investment calendar is the ‘Sell in May’ adage, which says that investors should ditch stocks at the end of April, wait on the sidelines until Halloween or some arbitrary date.

¹ Source: Federal Reserve Bank of St. Louis
² Source: Federal Reserve Bank of St. Louis
in the fall, and then reinvest in time for the aforementioned Santa Claus late-year rally.

Investors shouldn’t buy into any of this.

In my view, the Santa Claus rally, January Effect, and Sell in May are all just market-timing strategies dressed up as seasonal, statistics-driven investment approaches. But any adage or rule that suggests investors should be getting in and out of stocks over weekly or monthly time frames is not only wrong, in my view, but also harmful to an investor’s long-term return potential.

Stocks have delivered annualized returns of over +10% since 1926, which includes the Great Depression, high inflation during the 1970s, the 2008 Global Financial Crisis, and every other bear market and correction over that time. Trying to dance around seasonal quirks likely means missing significant amounts of the upside needed to capture that total return.

In my book, The Little Book of Stock Market Profits, I wrote: “Over the years I have yet to find a successful investor who obtained his or her returns through market timing…Active investment strategies can be developed that outperform the market over time – but engaging in behavior that borders on day-trading, because of what day is on the calendar, is ill-advised.”

In the years since I wrote that book, my opinion hasn’t shifted one bit.

**Bottom Line for Investors**

In the financial media, I have seen reputable pundits and even financial institutions still leaning into seasonal adages like the Santa Claus rally and the January Effect. But prudent investors should not try to time the market by season or any arbitrary date on the calendar. That’s because stocks don’t follow calendars, which means fundamentals-focused investors shouldn’t follow them, either.
The U.S. Labor Market is an Ongoing Headache for the Fed

Headline inflation in the U.S. is heading in the right direction, with goods inflation falling significantly in the second half of 2022 as supply chain pressures eased and commodity prices fell from peaks. Falling goods inflation is good news, but the services side of the equation continues to cause problems for the Fed’s view on overall inflation. Fed Chairman Powell’s biggest concern is the effect the tight labor market has on wages, which in many cases influences companies to raise prices to make up for higher costs. Powell specifically remarked that “the labor market continues to be out of balance, with demand substantially exceeding the supply of available workers.” Data released this week didn’t help. The Labor Department reported that job openings in the U.S. remain above 10 million (as of the end of November), which far exceeds the roughly 6 million Americans out of work. Initial jobless claims in the final week of December – which gives a read on layoffs –fell by 19,000, which signals that employers continue to cling to workers. What’s more, according to a recently issued report by the Atlanta Fed, workers who stayed at their jobs experienced an average wage bump of 5.5% in November 2022 compared to the year prior, which is higher than the 3.7% wage growth reported in January 2022 and also marks the largest increase in 25 years. A persistently tight labor market is a problem for the Fed and also for the market’s hope for a “Fed pivot” in 2023. Ongoing tightness in the labor market could cause inflation to become entrenched, which also implies the need for higher rates.¹

The Fed vs. The Stock Market

A closer look at the minutes from the December 2022 Fed meeting show a central bank increasingly concerned about stock market rallies. Part of the issue is that investors are anticipating a sharp decline in inflation in 2023, which in turn has driven hope that the Fed would stop raising rates and perhaps even lower them in 2023. The gap between where the market thinks inflation will land in 2023 and where the Fed sees inflation is meaningful – according to Barclays, the bond markets are projecting the consumer price index will fall to 2.6% by the end of 2023, which would arguably put the Fed’s preferred PCE price index very close to the 2% target. Meanwhile, the Fed raised its 2023 core PCE inflation forecast from 3.1% to 3.5% at its most recent December meeting. The Fed is increasingly concerned that the market’s optimism over lower inflation will also drive hope over a “Fed pivot” in the new year, which in turn will lead to market rallies. The problem with market rallies, according to the Fed, is that easing financial conditions could hurt their efforts to cool hiring and wage growth, which as mentioned above is a top concern.²

China’s Economy Suffers, for Now

China’s economy continues to reel from the hangover of “zero Covid” policies followed by the rapid spread of the virus as restrictions were lifted. Activity in China’s manufacturing and services sectors has plummeted to levels last seen during global economic lockdowns. China’s purchasing managers index (PMI)
dropped to 47.0 in December, and anything below 50 signals a contraction. But that wasn’t even the worst data point – in the key services sector, PMI fell from 46.7 in November to 41.6 in December. The transition to an open economy is likely to be messy in the first quarter, particularly as winter months combined with low levels of natural immunity make handling Covid outbreaks much more challenging. But at the same time, a trough in economic activity argues for a strong rebound once the transition to reopening has taken place, much like the rest of the developed world experienced in 2021. The Chinese government has also signaled a willingness to inject fiscal stimulus into the economy, which could boost growth in the second half of the year and contribute to a rebound in the broader global economy.³


DISCLOSURE

Past performance is no guarantee of future results. Inherent in any investment is the potential for loss.

Zacks Investment Management, Inc. is a wholly-owned subsidiary of Zacks Investment Research. Zacks Investment Management is an independent Registered Investment Advisory firm and acts as an investment manager for individuals and institutions. Zacks Investment Research is a provider of earnings data and other financial data to institutions and to individuals.

This material is being provided for informational purposes only and nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. Do not act or rely upon the information and advice given in this publication without seeking the services of competent and professional legal, tax, or accounting counsel. Publication and distribution of this article is not intended to create, and the information contained herein does not constitute, an attorney-client relationship. No recommendation or advice is being given as to whether any investment or strategy is suitable for a particular investor. It should not be assumed that any investments in securities, companies, sectors or markets identified and described were or will be profitable. All information is current as of the date of herein and is subject to change without notice. Any views or opinions expressed may not reflect those of the firm as a whole.

Any projections, targets, or estimates in this report are forward looking statements and are based on the firm’s research, analysis, and assumptions. Due to rapidly changing market conditions and the complexity of investment decisions, supplemental information and other sources may be required to make informed investment decisions based on your individual investment objectives and suitability specifications. All expressions of opinions are subject to change without notice. Clients should seek financial advice regarding the appropriateness of investing in any security or investment strategy discussed in this presentation.

Certain economic and market information contained herein has been obtained from published sources prepared by other parties. Zacks Investment Management does not assume any responsibility for the accuracy or completeness of such information. Further, no third party has assumed responsibility for independently verifying the information contained herein and accordingly no such persons make any representations with respect to the accuracy, completeness or reasonableness of the information provided herein. Unless otherwise indicated, market analysis and conclusions are based upon opinions or assumptions that Zacks Investment Management considers to be reasonable.

Any investment inherently involves a high degree of risk, beyond any specific risks discussed herein.

It is not possible to invest directly in an index. Investors pursuing a strategy similar to an index may experience higher or lower returns, which will be reduced by fees and expenses.

The ICE U.S. Dollar Index measures the value of the U.S. Dollar against a basket of currencies of the top six trading partners of the United States, as measured in 1973: the Euro zone, Japan, the United Kingdom, Canada,
Sweden, and Switzerland. An investor cannot directly invest in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

Zacks Investment Management, Inc. is a wholly-owned subsidiary of Zacks Investment Research. Zacks Investment Management is an independent Registered Investment Advisory firm that acts as an investment manager for individuals and institutions. Zacks Investment Research is a provider of earnings data and other financial data to institutions and to individuals.

This material is being provided for informational purposes only and nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. Do not act or rely upon the information and advice given in this publication without seeking the services of competent and professional legal, tax, or accounting counsel. Publication and distribution of this article is not intended to create, and the information contained herein does not constitute, an attorney-client relationship. No recommendation or advice is being given as to whether any investment or strategy is suitable for a particular investor. It should not be assumed that any investments in securities, companies, sectors or markets identified and described were or will be profitable. All information is current as of the date of herein and is subject to change without notice. Any views or opinions expressed may not reflect those of the firm as a whole.

Any projections, targets, or estimates in this report are forward looking statements and are based on the firm’s research, analysis, and assumptions. Due to rapidly changing market conditions and the complexity of investment decisions, supplemental information and other sources may be required to make informed investment decisions based on your individual investment objectives and suitability specifications. All expressions of opinions are subject to change without notice. Clients should seek financial advice regarding the appropriateness of investing in any security or investment strategy discussed in this presentation.

Certain economic and market information contained herein has been obtained from published sources prepared by other parties. Zacks Investment Management does not assume any responsibility for the accuracy or completeness of such information. Further, no third party has assumed responsibility for independently verifying the information contained herein and accordingly no such persons make any representations with respect to the accuracy, completeness or reasonableness of the information provided herein. Unless otherwise indicated, market analysis and conclusions are based upon opinions or assumptions that Zacks Investment Management considers to be reasonable. Any investment inherently involves a high degree of risk, beyond any specific risks discussed herein.

The S&P 500 Index is a well-known, unmanaged index of the prices of 500 large-company common stocks, mainly blue-chip stocks, selected by Standard & Poor’s. The S&P 500 Index assumes reinvestment of dividends but does not reflect advisory fees. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor. An investor cannot invest directly in an index.

The Russell 1000 Growth Index is a well-known, unmanaged index of the prices of 1000 large-company growth common stocks selected by Russell. The Russell 1000 Growth Index assumes reinvestment of dividends but does not reflect advisory fees. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

Nasdaq Composite Index is the market capitalization-weighted index of over 3,300 common equities listed on the Nasdaq stock exchange. The types of securities in the index include American depositary receipts, common stocks, real estate investment trusts (REITs) and tracking stocks, as well as limited partnership interests. The index includes all Nasdaq-listed stocks that are not derivatives, preferred shares, funds, exchange-traded funds (ETFs) or debenture securities. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The Dow Jones Industrial Average measures the daily stock market movements of 30 U.S. publicly-traded companies listed on the NASDAQ or the New York Stock Exchange (NYSE). The 30 publicly-owned companies are considered leaders in the United States economy. An investor cannot directly invest in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The Bloomberg Global Aggregate Index is a flagship measure of global investment grade debt from twenty-four local currency markets. This multi-currency benchmark includes treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers. An investor cannot invest
directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.

The ICE Exchange-Listed Fixed & Adjustable Rate Preferred Securities Index is a modified market capitalization weighted index composed of preferred stock and securities that are functionally equivalent to preferred stock including, but not limited to, depositary preferred securities, perpetual subordinated debt and certain securities issued by banks and other financial institutions that are eligible for capital treatment with respect to such instruments akin to that received for issuance of straight preferred stock. An investor cannot invest directly in an index. The volatility of the benchmark may be materially different from the individual performance obtained by a specific investor.