SYNOPSIS

- The Dow Jones Industrial Average index broke through the 23,000 level this week.
- Investors want to know the implications surrounding this milestone.
- Both the bulls and bears make a compelling case for the near-term future for the stock market, so investors understandably feel torn on the issue.

ANOTHER MILESTONE

The Dow Jones Industrial Average is a stock market index that tracks 30 large publicly traded stocks. The “Dow” was first calculated in 1896, and it remains one of the most popular stock indices in the world. In fact, the index is so widely followed that it is often regarded as a proxy for the entire U.S stock market.

The current bull market pushed the Dow to yet another all-time this week, breaking through the 23,000 level and representing a year-to-date gain of 16.5%, excluding dividends.

These milestones are covered so intensely by the media that many investors feel like they need to understand the implications of the Dow sitting at an all-time high, but market pundits cannot seem to agree on what to do next.

The bears want to sell stocks and lock in profits before the market takes a breather. They believe that the stock market is no different than a professional athlete, in the sense that even those in the best of shape still need their rest. Since the Dow has almost tripled from the depths of the financial crisis, a market correction is not only imminent but “healthy.”

Evidence is aplenty for the bears, but no greater tale of caution can be cited than what happened just a few months after the Dow broke 2,000. Back in 1987, the Dow started at 1,896 and then staged one of the most impressive runs in history, surging nearly 44% to 2,722 in late August.

Days later, it reversed and dropped nearly 1,000 points in two months. The selling fury plateaued with a 23% crash on October 19, which lives in infamy as “Black Monday.” The fact that this new all-time high occurred two days before the 30th anniversary of Black Monday is too much of a coincidence for the bears to ignore.

The bulls see things differently. They claim that hitting an all-time high only adds fuel to the engine of growth. It’s a psychological level that will ignite even more confidence in a market that wants to go higher. Momentum will rule the day, so enjoy this blissful period of rising equity prices with historically low volatility.

Once again, investors feel that this situation is forcing them to pick a side. Since both make an equally convincing case, it’s hard to know who will prevail.

WHAT’S IN A NUMBER?

I turned 40 years old right before the New Year, and my wife was kind enough to throw a surprise birthday party with close friends and family who flew in from all over the country to celebrate. The night was incredible and will always be a cherished memory.

The reason we celebrate big birthdays is that they represent milestones in life that society has designated to be important. The same applies to the Dow, and investors should most certainly recognize major milestones because it signifies that the world’s greatest economy has thrived over the past century in ways that few civilizations have ever experienced.

However, both my age and the current level of the Dow are just numbers. I did not wake up on my 40th any smarter, more confident, or wealthier. Aside from my amazing party, it was not much different than any other day that week.

The same goes for the Dow because it’s doubtful that hitting 23K will further accelerate the entrepreneurship coming out of Silicon Valley or the innovation in biotech around Boston. Nor will it cause unemployment to improve further or increase the profit margins of companies in the index.

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Now let’s look at the data to see just how rare it is to close at an all-time high. Since July 1, 1986, there have been a total of 7,892 days where the New York Stock Exchange was open for trading. The Dow closed at an all-time high on 613 of these days, which represents almost 8% of the time.

This year alone, there has been 51 closing all-time highs and 200 trading days, which comes out to just over 25% of the time. Said another way, the Dow has averaged more than one closing all-time high a week in 2017.

Simply put, all-time highs are neither rare nor do they do much to support a bull or bear case for owning stocks. Again, it’s just a number.

**IMPLICATIONS FOR INVESTORS**

For those readers experiencing a little déjà vu right now, there is a good reason. Much of the commentary above is verbatim to my Thought for the Week published back on January 13, 2017, right before the Dow hit 20K. I just copied and pasted, update the math to reflect 23K from 20K, and then modified the grammar in a few places. That’s it.

While this move may appear to flirt with a contemptible level of laziness, the intent was to highlight two critical observations. The first is how quickly people forgot about the Dow breaking 20K. Leading up to this milestone, the story was page one material. Days after, it fell off a cliff never to be discussed again.

The second is how eerily similar the Dow 23K story is mirroring the Dow 20K one. To me, it is a carbon copy. The same bull and bear arguments, similar attention from the media, and investors once again feel compelled to make a call one way or the other.

This is not to say that investors should run with the bulls on the expectation that history will repeat itself (the Dow is up over 15% just 10 months after it broke 20K). Nor should investors assume that this will be a catalyst for a market selloff.

Markets can be moved by emotions in the short-term, so there very well may be some impact over the coming weeks/months. But since emotions cannot drive $19 trillion economies, any influence good or bad will be as temporary as it is unpredictable.

Instead, it is meant to show that Dow 23K will soon be as much of a distant memory as the Dow 20K, Dow 15K, and the Dow 5K have become. Ironically, the media will be the first to have moved on because the story will become stale fast. They will put it away for a while until the day when the Dow begins to see 30K on the horizon. Then, take a wild guess what they will do.

**THE BOTTOM LINE** is that index milestones cannot impact the fundamentals of the economy or the companies that operate within, so they are irrelevant to the long-term direction of stock prices.

SINCERELY,

Mike Sorrentino | CFA
Chief Investment Officer
Global Financial Private Capital

Source: Bloomberg, as of 10/18/2017

Index Definitions:

All indexes are unmanaged and an individual cannot invest directly in an index. Index returns do not include fees or expenses. Past performance does not guarantee of results. Index returns do not reflect fees or expenses and it is not possible to invest directly in an index.

The Dow Jones Industrial Average is a U.S. stock market index that tracks 30 large publicly traded stocks.