Market Bulletin

Issue No. 239
February 3, 2014

Commentary – January Barometer has very limited predictive power

Over past 25 years, has only worked for S&P 500 when January change is more than 4%

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January 2014 has not been a good month for equities, with most global equity indexes registering declines in this period (Canadian indexes have been notable exceptions). Here's how major North American indices performed last month: S&P 500 -3.56%, DJIA -5.30%, Nasdaq Composite -1.74%, TSX Composite +0.54%, TSX-Venture +2.08%.

The first month of the year is closely watched by investors because of the widespread notion that "as goes January, so goes the year." To check out the validity of the January Barometer, as this phenomenon is known, we analyzed S&P 500 and TSX Composite results for January and the full year for the 25 years from 1989 to 2013 (Table 1). Our research suggests that while there's some truth to this belief, but only in those years when the S&P 500 has a big change in January (more than +4%/-4%). The results are discussed below.

- Over this 25-year period, the January Barometer worked on 17 occasions for the S&P 500. **That is, the January Barometer confirmed the trend 68% of the time for the S&P 500 from 1989 to 2013**, with a gain in January followed by a gain for the year and a decline in January followed by a decline for the year. **This has zero predictive power, since the index has a 67% chance of appreciating in any given year**. **For the TSX Composite, the barometer only worked in 14 years, for a success rate of 56%**.

- **The January Barometer had better predictive power for the S&P 500 in the first half of this 25-year period**. While the barometer worked in 10 of the 12 years from 1989 to 2000, for a success rate of 83%, it only worked in 7 out of 13 years from 2001 to 2013 for a success rate of 54%. Corresponding figures for the TSX Composite are 58% (1989-2000: 7 out of 12) and 54% (2001-2013: 7 out of 13).

- Of the 17 years when the barometer worked for the S&P 500, 13 were positive years and four were negative years. The index had an average gain of +20.1% in those 13 positive years, and an average decline of -18.4% in the four negative years. For the TSX Composite, of the 14 years when the barometer worked, there were 10 positive years (average gain +13.4%) and four negative years (average decline -22.3%).

- **We also looked at index performance when there were big swings in January, specifically a gain or decline of more than 4%. The S&P 500 had 10 of these big swings in January, and the barometer worked in nine of those years (six up years, three down years) for a 90% success rate**. The average gain in the six up years was 24.5% and the average decline in the three down years was -18.4%. The **TSX Composite also had January swings of more than +4%/-4% in 10 years, but the barometer worked in only six years (four up, two down), for a 60% success rate**. The average gain in the four up years was 15.3%; the average decline in the two down years was -26.5%.

Bottom-Line: The January Barometer has very limited predictive power, and only works for the S&P 500 in those years when it has a big January change (> +4%/-4%). It has no predictive power in other years. It also has no predictive power for the TSX; you might as well flip a coin to figure out how the index is going to do in a given year, based on its performance in January.

Table 1: S&P 500 and TSX January and yearly performance – 1989 to 2013

Year	S&P 500		Jan. Baro-	TSX Comp.		Jan. Baro-
	Jan.chg.	Year chg.	meter conf.?	Jan.chg.	Year chg.	meter conf.?
1989	7.11%	27.25%	Yes	6.69%	17.10%	Yes
1990	-6.88%	-6.56%	Yes	-6.68%	-17.96%	Yes
1991	4.15%	26.31%	Yes	0.50%	7.85%	Yes
1992	-1.99%	4.46%	No	2.38%	-4.61%	No
1993	0.70%	7.06%	Yes	-1.34%	28.98%	No
1994	3.25%	-1.54%	No	5.40%	-2.50%	No
1995	2.43%	34.11%	Yes	-4.65%	11.86%	No
1996	3.26%	20.26%	Yes	5.41%	25.74%	Yes
1997	6.13%	31.01%	Yes	3.08%	13.03%	Yes
1998	1.02%	26.67%	Yes	0.01%	-3.19%	No
1999	4.10%	19.53%	Yes	3.76%	29.72%	Yes
2000	-5.09%	-10.14%	Yes	0.80%	6.18%	Yes
2001	3.46%	-13.04%	No	4.35%	-13.94%	No
2002	-1.56%	-23.37%	Yes	-0.52%	-13.97%	Yes
2003	-2.74%	26.38%	No	-0.68%	24.29%	No
2004	1.73%	8.99%	Yes	3.66%	12.48%	Yes
2005	-2.53%	3.00%	No	-0.46%	21.91%	No
2006	2.55%	13.62%	Yes	5.97%	14.51%	Yes
2007	1.41%	3.53%	Yes	0.97%	7.16%	Yes
2008	-6.12%	-38.49%	Yes	-4.90%	-35.03%	Yes
2009	-8.57%	23.45%	No	-3.26%	30.69%	No
2010	-3.70%	12.78%	No	-5.55%	14.45%	No
2011	2.26%	0.00%	N/A	0.81%	-11.07%	No
2012	4.36%	13.41%	Yes	4.16%	4.00%	Yes
2013	5.04%	29.60%	Yes	2.02%	9.55%	Yes
Average	**0.55%**	**9.53%**		**0.88%**	**7.09%**	
Jan. Barometer confirmed			**17**			**14**
Jan. Barometer not confirmed			**7**			**11**
Inconclusive			**1**			**0**

Economic Analysis

Friday's jobs numbers may set loonie direction after worst January since 1972

The Canadian dollar tumbled 4.5% against the greenback in January, its worst start to a year since at least 1972, according to Bloomberg. The currency's near-term direction may be set by January's payroll numbers for Canada and the U.S., scheduled for release on Friday.

Economists' average forecasts are for the Canadian economy to have added 20,000 jobs in January, rebounding from an unexpected loss of 45,900 jobs in December. The unemployment rate is forecast to improve marginally to 7.1%, from 7.2% in December. In the U.S., economists' average forecasts are for a January increase of 180,000 – led wholly by private-sector payrolls – after a gain of only 74,000 in December, which was the lowest in three years due to inclement weather.

The Canadian dollar traded past 1.12 to the US dollar (i.e. C$1 = 89.30 US cents) on Friday for the first time since July 2009. The currency fell to a low of 89.10 before rebounding by ¾th of a cent to close at 89.86 US cents, down 0.4% for the week.

The Canadian dollar is being forced lower by speculation that the Bank of Canada may lower interest rates later this year if the economy continues to struggle, even as recent data highlight the strength of the U.S. economic rebound. Friday's jobs number may go some way towards confirming these viewpoints. A marked divergence in the jobs numbers between Canada and the U.S. could lead to more pressure on the loonie, while an upside surprise in the Canadian numbers could trigger a rally as speculators unwind short positions.

Market Snapshot

At close on Friday, January 31, 2014

S&P TSX	13694.94	-40.34	**Commodities**			**Yields (%)**	**Can.**	**US**
TSX Venture	951.32	-1.56	Canadian $ (US cents)	89.86	+0.26	90 Day T-Bill	0.88	0.02
DJIA	15698.85	-149.76	Gold (Spot)-US$	1244.55	+0.63	2-Year Bond	0.94	0.33
S&P 500	1782.59	-11.60	Oil (WTI-March)	97.49	-0.74	10-Yr.Bond	2.33	2.64
NASDAQ	4103.88	-19.25	CRB Index	283.31	-0.25	30-Yr. Bond	2.92	3.60

Thought for the Day

"I don't believe in taking foolish chances, but nothing can be accomplished without taking any chance at all." – Charles Lindbergh

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