Sell in May? Maybe Not This Year

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By Ellis Mnyandu

NEW YORK (Reuters) - Betting against the latest upsurge in U.S. stocks is likely to be a losing proposition even for the balance of May, a month historically associated with the onset of a volatile period for equities.

Now that the U.S. government's stress tests have been released, relieving the market of some of the uncertainty surrounding the financial sector, the old "Sell in May and go away" adage might need a rethink this year.

A series of stronger-than-expected economic reports and hopes that U.S. banks are healthier than previously thought have fueled a 36 percent jump in the benchmark S&P 500 from a 12-year low on March 9.

After such a heady run in markets many experts anticipate stocks will pull back.

Owen Fitzpatrick, head of Deutsche Bank Private Wealth Management's U.S. equity group, termed the latest upswing -- notwithstanding Thursday's more than 1 percent losses -- a "relief rally" that will require some kind of consolidation.

However, he said, "we're looking to add on any type of pullback," underscoring the ongoing optimism despite the surge.

While a large move lower is inevitable at some point, analysts believe technical indicators, measures of sentiment, cash levels and volatility trends all suggest that the rally could persist, defying the skeptics.

The phrase, "Sell in May and go away," is borne of the fact that since 1950, May traditionally signifies the start of what has tended to be the dreariest six-month period for stocks.

According to the Stock Trader's Almanac, since 1950 the Dow Jones industrial average has eked out a average gain of 0.6 percent in the May-October period, compared with an average gain of 7.6 percent in the November-April period.

As with any other strategy, there have been recent exceptions. Schaeffer's Investment Research showed in a study that May has been the third-best month over the last five and 20 years, with average returns of 1.1 percent and 1.8 percent, respectively.

DEFYING THE NAYSAYERS

In all likelihood there are plenty of investors who initially doubted that the stock market would push this far in its recovery. That alone is seen as enough fuel to sustain the run-up through May, analysts said.

"There's a lot of cash that's been on the sidelines and probably missed a lot of this rally," said John O'Brien, senior vice president at MKM Partners LLC in Cleveland.

"So there's definitely going to be some catching up to do, probably more likely at month's end than in the middle of May. A lot of people this year think maybe you want to stay invested since we are coming off such low levels."

To gauge how much money is currently on the sidelines, PNC Wealth Management uses a proprietary measure of household cash available. That metric shows the current cash pile at nearly $9.2 trillion, compared with an all-time high of more than $9.3 trillion in early March as the stock market hit 12-year lows.

"There remains more than sufficient fuel to propel the market higher if risk aversion continues to fade," William Stone, PNC chief investment strategist, told clients in a note.

Among other measures signaling the broad strength of the latest rally is the S&P 500's 200-day moving average, which shows the benchmark index is less than 50 points away from registering its first daily finish above this closely followed strength metric since December 2007.

The Chicago Board Options Exchange's Volatility index , also known as Wall Street's fear gauge, fell below 32 on Thursday. That has not happened since September of 2008, suggesting market volatility is receding to levels investors were accustomed to prior to the freeze-up of the credit markets in the fall.

Moreover, according to the NYSE's Bullish Percent Index, about 70 percent of stocks listed on the NYSE are currently trading above their 200-day moving averages, compared with a May 2008 peak of just 54 percent.

That is a bullish signal, said Bruce Zaro, chief technical strategist at Delta Global Advisors in Boston. He said that when the indicator reached a similar level back in 2003, the S&P 500 went up another 20 percent from where it was.

"The potential really exists that this year is going to be more like 2003 and less like 2007-08, when you should have sold in May and gone to Italy."