FINANCIAL
newsletter

Wealth Architects, LLC

January

The January effect

Ever since economist Sidney Wachtel first coined the term in 1942, analysts and market pundits have been eager to talk about a seasonal market movement known as “the January effect.”

In its simplest form, the January effect is the rise in stock prices over the first two weeks of each year. The rise is said to be more significant in small-cap stocks, which will eventually fall behind the gains of large-cap stocks over the remainder of the year. Additionally, the price growth supposedly sets the tone for the rest of the year — a strong January effect means a positive year is coming, while a loss in early January means a bad year.

Though there are logical explanations and repeated documentation of the effect, many individuals refute its reliability and question whether it exists at all.

Sound superstitious? There are some reasons why the January effect makes sense. The growth is largely a recovery from a supposed market drop in the last weeks of December, when investors (both private and institutional) sell off weak stocks to get them off their books and lock in losses for tax purposes. Investors then repurchase the same shares at the start of the year, causing the January effect.

Some behavioral investors believe that psychology also helps boost the January effect, as people tend to be the most optimistic during the first part of the year. For investors, this may mean putting more money into investments or taking a risk on a cheap stock that will hopefully make huge returns.

Changing tax rates are another reason the January effect is said to occur. When the government announces a raise on the capital gains tax in the upcoming year, investors are encouraged to sell their profitable investments before the end of the year to take advantage of the current tax rate.

This causes December prices to fall across the board and then rise to a normal level in January.

Is the January effect real?

Historically, stocks have often risen during the first two weeks of January, and 25 out of the past 40 years have seen the S&P 500 end the month ahead of where it started on January 1. Over the total year, however, the S&P has increased for 30 of those 40 years. The truth is that the stock market, regardless of its performance on a short timeline, has historically always trended upward on a longer timeline of several years.

One of the reasons many say that the January effect cannot be real is that the market would be aware of it. The “effect” is over 70 years old, so investors have had more than enough time to learn how to compensate and, therefore, negate its influence.

Even if stock rebounds were consistent, selling assets for just a week and then repurchasing them is a foolish practice for any long-term investor. Not only could share prices increase in that time but the investor is also guaranteed to spend some money on the sale and repurchase transactions.

It is possible that the January effect provided observant investors a chance to game the market in the years before 1942; however, now that the market is more efficient and much more analyzed, seasonal “sure bets” simply do not exist. Even in the case of raising taxes, eager investors are as likely to cause the January effect in October as they are to cause it in December and January.

The best thing investors can do with the January effect is ignore it. Markets are volatile and short-term fluctuations should not affect an investor’s decision to buy or sell. An investment strategy relies on the appreciation of a successful company’s assets, not on the speculation of market moods from one month to the next.

The market at a glance

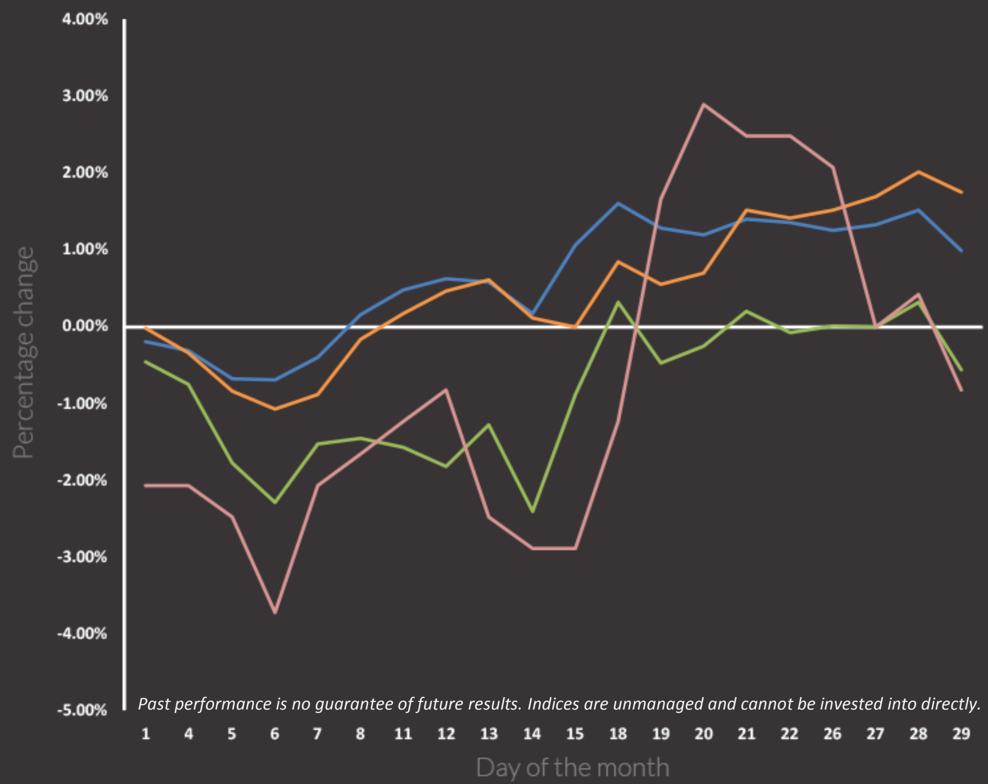
December

U.S. Large Cap
(S&P 500)
2,673.61 (0.98%) ▲

U.S. Mid/Small
(Russell 2000)
1,535.51 (-0.56%) ▼

International Large
(NYSE International 100)
5,792.03 (1.74%) ▲

U.S. Treasuries
(U.S. 10-year Treasury yield rate)
2.40 (-0.83%) ▼



The market in action

- The government passed legislation that represented the most significant overhaul to the tax system in decades. The “Tax Cuts and Jobs Act” will alter main tenets of the tax code, including: lowering the corporate tax rate, raising the standard deduction, adjusting individual tax brackets, and more.
- In the final months of 2017, bitcoin became one of the most frequently discussed topics in the world of finance and economics. At its peak, bitcoin increased in value by over 1,900 percent since the start of the year. Ultimately, bitcoin ended the year valued at about $13,860, roughly 1,261 percent higher than its value at the beginning of 2017.
- The Walt Disney Co. bought the majority of 21st Century Fox. The deal, which was announced in mid-December, is reportedly worth over $52 billion.
- According to a recent study by NerdWallet, the average household in the US owes nearly $16,000 in credit card debt.
- In a recent report by the Wall Street Journal, about 5 million Americans are currently in default on student loans — roughly double the amount from four years prior. This represents nearly 13 percent of all outstanding student loans.
- Existing home sales in November hit an 11-year high. Sales increased by about 5.6 percent from the previous month. Some analysists believe that this information points to a recovering housing market that has been slow to regain its value following the Great Recession.

New Year's financial resolutions

For many of us, a New Year's resolution is a great way to simplify what we want out of the coming year. Each year, many people set financial goals like "save more income."

However, making the resolution to save money is easy; the difficulty comes from deciding how to save that money. Fortunately, improving your financial situation can be a side effect of making other positive changes in your life.

Learn how some popular New Year's resolutions, as well as financial goals, can save you money.

Lose weight

Losing weight and increasing overall health very frequently tops the list of most common resolutions, but a healthier lifestyle means more than just the physical and mental benefits. On average, obese adults spend 42 percent more on health care costs than adults with a healthy weight. Good health can provide you with more than just a higher quality of life, including a sizeable financial benefit over the course of your life. Additionally, health-focused commuting options (like walking or biking) can provide additional savings.

Prepare food at home

According to the Bureau of Labor Statistics, the average household spent $7,203 on food in 2016. From this, money spent dining out accounted for over $3,150. Aside from the financial impact, a 2014 study from Public Health Nutrition indicates that those who ate out consumed about 200 more calories per day than those who ate at home. Though dining out is a fun, relaxing, and communal experience, it can be incredibly expensive.

Quit that smoking habit

Smoking, in addition to the well-known physical effects, is a financial lose-lose. It is an expensive habit upfront and can lead to myriad health problems later on in life. Buying a pack per day at the national average of $6.16 will cost you about $2,250 over the course of a year—over $80,000 in 20 years with inflation—and can generate thousands of additional dollars in medical costs. That money could be in a bank account instead of vanishing in a puff of smoke. The good news: When a person quits smoking, the physical and financial benefits start to become noticeable within less than a month.

Read more

Many people make a resolution to read more in the coming year but some may worry about the cost of the exercise. Fortunately, if you go about it carefully, reading can actually be used to lower your monthly expenses. Libraries and thrift stores can make access to reading materials cheap or free. By turning these books into a primary source of entertainment, you can cut back or eliminate the media that costs the most, like movies or cable subscriptions.

Pay off major loans

Aside from health-related resolutions, a new year is an opportunity to implement new financial habits. Learning to live with extra loan payments may be a difficult adjustment at first, but you will ultimately be saving money that would have otherwise been lost to accumulating interest. When the loan is completed, you will have funds available that you have already learned to live without, providing you with a great opportunity to save more for your next goal.

Adjust savings percentage

A new year may also come with a bonus or a raise. If your salary increases, consider putting some of that new money towards your savings. Increasing contributions to a company-sponsored retirement plan — no matter how small — can aid your retirement plan without compromising your current standard of living.

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