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In 2016, May wasn't the time to sell and go away

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Last month I asked a rhetorical question: Should we sell in May and go away as the old market saw suggests? I pointed out that what was once a predictable market event has shown, in recent years, to be unreliable.

This May turned out to be no exception, as the markets once again confounded the experts. If you sold in May, you left the party too soon. The Standard and Poor's index rolled up a 1.53 percent gain in May – 1.8 percent with dividends reinvested. For the three months ending in May, the blue chip index was up 9.12 percent with dividends. The markets were expected to decline because the Federal Reserve was expected to raise rates in June or July.

Once again the Fed has egg on its face, as the most recent jobs report showed that only 38,000 jobs were created in May. The consensus forecast of economists was 160,000 new jobs. This was the worst job growth number in five years. Jobs growth for previous months was also revised downward.

Even 160,000 new jobs is a paltry number, because the economy needs to create 250,000 jobs each month to absorb the new workers. Furthermore, for the past several months, the new jobs created have declined sequentially. The unemployment rate fell 0.3 percent, as over 664,000 workers left the workforce; the labor participation rate declined.

Fed speakers had been out in force on the rubber chicken circuit declaring that rates were going up and that the economy was strong and growing stronger. The economy was gaining steam, they said, with employment near capacity. That scratching sound you hear is the Fed members rewriting their speeches. Chairwoman Janet Yellen took to the speaking circuit as well to calm the markets, but conceded that plans had changed. She still forecasts one more rate increase this calendar year. As we have learned many times, the market does not operate on a monthly or yearly basis.

Because a rate increase was considered imminent, the dollar strengthened. In spite of the strong dollar, share prices and oil prices both rose, with the S&P now less than 2 percent from making a new high. With a weak jobs number and a presidential election near, it is unlikely the Fed will risk a rate increase. The chance of a rate increase in July fell to 37 percent from about 59 percent late on Thursday. The Fed will not likely cut rates, because to do so would be to admit that the economy is in trouble and challenge its own credibility and further undercut the Obama-Clinton thesis that things are going well.

Growth stocks were the place to be in May. "Cheaper" value stocks underperformed. The 10-year Treasury yield ended May at 1.85 percent, only slightly higher than it started. The two-year yield had its biggest monthly gain of the year, as traders factored in a June or July rate hike. The pattern of short-term rates rising faster than long-term rates is known as "flattening" of the yield curve, which often is a sign of concern for the economy. So, the market was seeing something the Federal Reserve was not seeing. The economy is not strong.

Information technology was the May sector leader, gaining 5.28 percent in the month. Energy was the biggest loser, with its funds falling 1.31 percent – even as oil passed $50 per barrel for the first time since November. Turmoil in Nigeria and fires in Alberta caused the price of oil to rise, as supplies were reduced. On the other hand, Iran is boosting production; OPEC is holding production firm and U.S. rig count increased.

Commodities were down. Natural resource funds dropped 2.79 percent. Gold funds plunged 10.75 percent.

Historically, June has been a good month to invest, with funds posting a gain in the S&P 56.8 percent of the time, with an average gain of 3.24 percent. But when it is down in June, the market averages a 4.63 percent loss.

With the U.S. equity valuations around the 70th percentile of their long-term historical range, stocks appear more vulnerable to short-term corrections. Risks abound from an overaggressive Fed rate increase, the possibility of a "Brexit" (the U.K. leaving the European Union), worsening of the immigration crisis, a slowdown in global growth and more. Long-term equity returns recently have been subpar. The average annual return since 1926 has been 10.09 percent; but in the last 15 years the average annual total return has been 5.56 percent.

The market confounded the experts in May, proving once again that it does not care what you or anyone else thinks. Mr. Market dances to his own tune.

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