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THIS SCARY INVESTMENT STRATEGY MAY JUST WORK GOING INTO 2023

By Arin Ruttenberg, Financial Planner, Brenthurst Wealth Sandton

There are many investment strategies one can employ, but only one is as spooky as the mystery surrounding it, namely the 'Halloween Effect.'

This strategy urges investors to exit stocks on the 1st of May and to return to the market on the 31st of October (Halloween). The strategy suggests that one must switch into alternative asset classes for the period of May until the end of October, whereafter buying back into stocks. It's closely related to the age old saying: "Sell in May, go away, come again on St. Leger Day.''

In 2022, the first part of the strategy has proved true, as leaving the market in May would have avoided the approximate 10% decline in stocks in 2022.

The biggest mystery of it all is why this approach works. There are many theories, from taxation to the weather, to high profile Wall Street executives going to the Hamptons on holiday, but it is difficult to pinpoint the drive behind this effect.

Professors Cherry Zhang and Ben Jacobsen published a report in the American Economic Review that specifically studied the performance of stocks during the period November to April, and called it 'The Halloween Indicator'.

They studied the trend extensively and found it to have strong success over longer time periods and across countries. On average, stock markets have historically returned materially more during the November-April period than May-October. And, when I refer to a long period of time, the success rate is 80% over 5 years and 90% over 10 years, suggesting that it may certainly fail in any given year, but can add around 4% to performance compared to the buy and hold strategy.

IN THIS ISSUE

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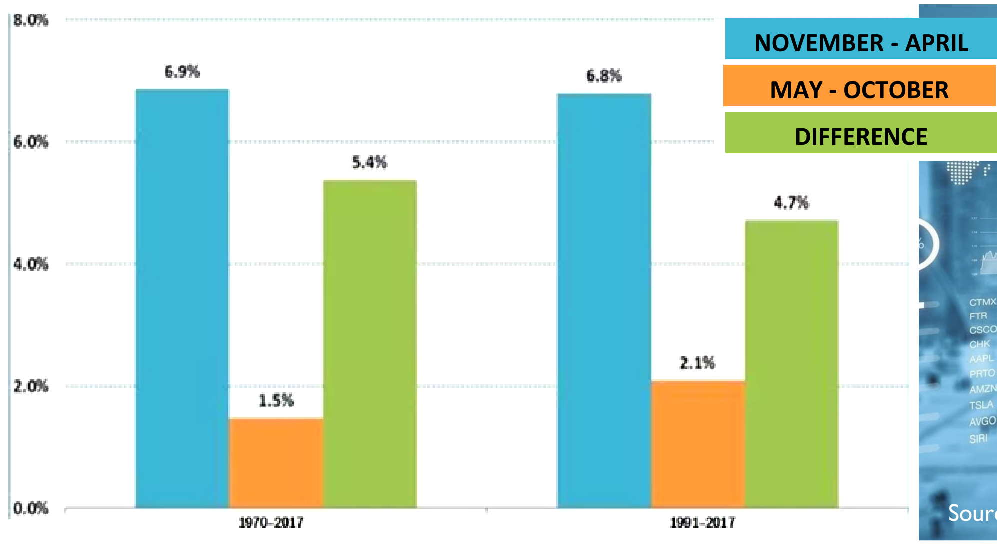
The graph below depicts the Halloween Effect on the S&P500 for the periods 1970–2017 and 1991–2017.
IT INDICATES THAT THE RETURN ON THE S&P 500 INDEX IS MUCH HIGHER FROM NOVEMBER THROUGH TO APRIL THAN IT IS FROM MAY THROUGH TO OCTOBER:

S&P500 INDEX - THE HALLOWEEN EFFECT



Source: Bloomberg

This strategy certainly can work in 2023, with the US [entering a midterm year, which has been positive for the U.S. stock market historically]. So, there are two indicators suggesting US stocks may be set for a reasonable run over the coming months.

CHALLENGES

The challenges according to Jacobsen are tough. As mentioned above, it doesn't work every year. In fact, the chances of this working in a given year are surprisingly close to 50/50. However, the returns during good years can be sufficiently high, resulting in an average return which is quite impressive.

For me, another challenge is the tax aspect. If one is constantly trading in and out of markets it could trigger income tax, a far less attractive tax. In addition, which "other asset classes'' should one be investing in? Thus far, from 1 May 2022 to date, the answer would be USD cash. But the opportunity cost of not holding some of the energy sector, even as a tactical play, would have been 18% in USD terms. In future, this could be anything from tech to property.

With it being a coin toss each year, personally I am happy to leave this Halloween mystery unsolved and stick to the traditional strategy which has proved reliable in my career, which is dollar cost averaging and holding on to a globally diversified set of asset classes, mainly shares, which include a satellite such as Crypto. This may be dull, but dull can be effective when it comes to figuring out how things will play out during a bear market.

ADVISOR PROFILE ARIN RUTTENBERG |Financial Planner, Brenthurst Sandton

ARIN is based in Brenthurst's Sandton Office and has been in the financial services industry since 2013.

He started his career with Investec and thereafter became a financial advisor under supervision at Brenthurst Wealth Management. Arin also consulted as an Investment Specialist for Momentum Wealth and Wealth International, before re-joining the Brenthurst team as a Financial Advisor in 2020.

Having obtained his BCom and Postgraduate Diploma in Financial Planning from the University of the Free State, he continues his passion for Financial Planning by continuously learning, challenging himself and, most importantly, assisting clients in taking ownership of their financial affairs and long-term wealth.

Email: arin@brenthurstwealth.co.za **Phone:** +27 10 035 1391 **Mobile:** +27 84 582 8581

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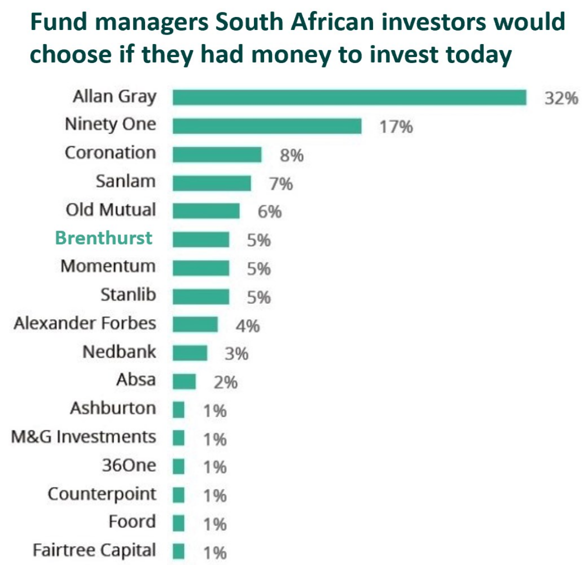
DAILY INVESTOR researched the most recognised brands in financial services and ranked awareness of the Brenthurst brand in 6th place, alongside the much larger Momentum and Stanlib. Read more >> https://www.news24.com/



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