Beware the Witching Season

The 60 days following Labor Day have traditionally been among the most difficult of times for the stock market. Indeed, October has been Ground Zero for the biggest market drops of the last 100 years. Yet, despite the fact that this has been a period of increased volatility, it has often been a time when weakness has been followed by a significant rebound. But let's not jump the gun. There may be no weakness and there may be no rebound.

This year got off to a rousing start, appearing as a continuation of the steadily higher path of 2017. While prices were climbing, so were valuations, almost to a point of excess. Then a new era of volatility showed up, with daily changes in the leading averages often running into the triple digits. For most of the months that followed, it was a matter of up, down, and a net result of little progress.

More recently, shares are again on the rise, as earnings jump in reflection of the substantial reduction in the U.S. tax rate. This year's bottom lines will probably be up 20% or so. The hitch is that much of this gain is nonrecurring, so the likely advance in 2019 will be far more moderate. That may not please investors.

What's more, the Fed has made it quite clear that further increases in interest rates are on tap. Thanks to a prospective combination of more costly credit and less robust gains in profits, it seems increasingly probable that next year will not be an extension of the Goldilocks economy.

With the midterm elections little more than two months away and continuing concerns about the chaotic and dysfunctional goings-on in the nation's capital, one would be well advised to keep a sharp eye on the horizon and opt in the direction of greater portfolio protection. What lies directly ahead may be a rocky road.