Is the Sell in May and Go Away Really a Strategy?

If you base your strategy on a horse race in London, then the answer is yes

One of the oldest stock market strategies is to “Sell in May and Go Away.” But what does this phrase mean? Is there any historical reason for selling stocks in May and leaving the market? What are the risks?

The “Strategy”

“Sell in May and go away” is a well-known trading adage that suggests that investors should sell their stocks in May to avoid a seasonal decline in the stock market. An investor selling his or her stocks in May would then buy stocks again in November because the November through April period shows significantly stronger growth in the market than the other half of the year.

Where did this “Sell in May and go away” advice originate? Not on Wall Street, but rather in London’s financial district. The original saying, “Sell in May and go away, come back on St. Leger’s Day” refers to a horse race. That’s right, a horse race.

The St. Leger Stakes is one of England’s greatest horse races and is run in late September. London traders would sell their shares, enjoy their summer, and return to the market after the St. Leger race.

The idea is based on seasonality and with this strategy, traders are only invested in the stock market for about six months of the year (November through April). These months are typically the strongest period of the stock market. Investors sell their stocks in May, save their money in cash, bonds, or another safe investment, then buy stocks again in early November.

The Statistics on This “Strategy”

As it turns out, stocks have done better during the winter-early spring period. According to the Stock Trader’s Almanac, since 1945 the S&P 500 has gained a cumulative 6-month average of nearly 2% from May through October on a price return basis. And for the 6-months from November through April, the S&P 500 has gained 6.7%, on average.

Need more data? Well, the Stock Trader's Almanac also says that the price return for the S&P 500 from November through April has recorded the highest average price change of any rolling six-month period.

In addition, the S&P 500 has lost money in only 13% of the November-April time periods since 1945 and about 33% of the time from May through October. That success rate is remarkable. Maybe the horses are onto something after all? Or maybe we’re looking for correlations that don’t exist?

But, This Time It’s Different?

This is probably the most dangerous phrase in all of investing: “this time it’s different.”

In fact, if you are discussing investments, the markets, or anything financial related and someone says this, don't walk away, run.

- Most Recent Year: Looking at the S&P 500 from May 1, 2021 through November 1, 2021, the S&P 500 gained approximately 10.3%. So it didn't work.
- Year Before: Looking at the S&P 500 from May 1, 2020 through November 1, 2020, the S&P 500 gained 12.3%. Didn't work.
- Year Before That: Looking at the S&P 500 from May 1, 2019 through November 1, 2019, the S&P 500 gained 4.1%. Didn't work.

This time it's different? Utterly dumb.

Explanations for the November-April Success

The reality is that there is a lot of money moving throughout the economy, and the stock market, from November through April. Here are some examples:

- Holiday spending: Halloween, Thanksgiving, Christmas, New Year's Day, the Super Bowl, Valentine's Day, Mother's Day, etc. all come during those months.
- Back-to-school, Black Friday, and Cyber Monday sales.
- Employer contributions to employee retirement plans, almost all of which are invested in the stock market, through 401k and other retirement vehicles.
- Year-end employee bonuses.
- Tax refunds.

Limitations to This "Strategy"

Despite these favorable statistics, there are limitations to implementing this strategy.

- No one knows when to start: From 1988-2015, according to economist John Mauldin, the best strategy might have been "Sell in August, buy in mid-October".
- With any strategy based on averages, any given year might show an extreme high or extreme low, a wave that a buy-and-hold investor could ride out.
- Investors lose short-term gains to taxes because short-term gains are taxed at your regular rate.
- Investors face additional transaction costs due to selling stocks and mutual funds, followed by buying stocks and mutual funds later.

Why "bet the farm" on a simple seasonal strategy having its origins in a summer break before a horse race? That would be like gambling…

Working With Your Financial Advisor

The key to successful long-term investing, of course, lies in following wise strategies. Your financial advisor understands these strategies. It is generally best not to rely on interesting statistics that are not explained by actual market trends or economic analysis.

No specific investment strategy is foolproof. Your best strategy as an investor is not to base your plans on market timing or the season. Instead, focus on the traditional, sensible factors that include assessment of the business cycles, changing economic conditions, and news from the market.

Your financial advisor is the best source for information about how to handle your money. He or she can guide you in planning for the future.