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THE BULL MARKET'S MID-LIFE CRISIS

In the past few days, the S&P 500 has given up virtually all of its gains for 2014. So is it time to worry? Not based on the picture we see:

- US ECONOMY: US economic data throughout Q3 has been reasonably good, especially when you look past the monthly volatility at year-on-year improvement. There's no evidence to suggest an imminent economic downturn.

- FED POLICY: The end of QE has sparked fears of rising interest rates. But as yet, there is no sign of accelerating inflation that would force the Fed to raise rates in the immediate future.

- STRONG DOLLAR: A strengthening dollar cuts both ways; yes, earnings of US multinationals may be dented, but lower oil prices and other inputs are like big tax cuts for the domestic US economy.

- GLOBAL GROWTH: There is lots of concern about faltering Germany and China. These surplus countries, however, do not drive US growth, any more than Japan drove US growth in the 1980s; when Japan's growth faltered in the 1990s, the US economy did just fine. To the contrary, the US stands to benefit from a long-overdue shift in these economies from surplus production towards greater (net) consumption.

- VALUATIONS: Earlier this year, we voiced concern because the market was up but earnings were not. Now it's just the opposite: earnings have risen but the market has not. Valuations have fallen more than a full multiple since the start of the year (from 17.2 to 16.0, 12-month trailing P/E). With earnings improving steadily and interest rates remaining low, valuations should be rising, not falling.

Not that long ago, people were saying, "I wish I had bought at the beginning of the year." Well, now they have their chance. Prices have reset, but nothing material in our outlook for the US economy has changed - if anything, it looks stronger now than at the start of the year. This bull market is having a mid-life crisis. The key word is "mid-life".

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