

Will Santa Be Coming to Town?

by John E. Chapman

The Santa Claus Rally Tradition

While it's part folklore, part statistical oddity, the Santa Claus rally tradition still serves as both a short-term trading cue and a soft read on investor sentiment heading into the new year. In its classic form, the anticipated rally refers specifically to the last five trading days of December and the first two trading days of the new year, a seven-session window. Over this period, broad U.S. benchmarks such as the S&P 500 have historically shown higher odds of positive returns, which have been materially more frequent than in a typical random seven-day stretch.

Since 1950, studies summarized in the Stock Trader Almanac and subsequent research show that this Santa trading window has produced gains in roughly three out of four to about four out of five years, depending on the exact sample. This observation alone reinforces the Santa Claus rally's reputation as "real" rather than a piece of folklore. However, the gains have proven to be relatively modest in nature.

The Tradition Offers No Free Lunch

Analyses from LPL Financial and others show that in the relatively few years when the Santa Claus rally finishes in the red, the following January—and at times the year as a whole—has tended to be weaker. There are, however, notable exceptions, reminding us that this is more a sentiment signal than a predictive tool.

As with many "seasonal" market patterns, fundamental macro conditions dominate any calendar effect. This has been the case in recent years due to Fed monetary policy surprises and other shocks such as the global pandemic.

Generally, the Santa Claus rally phenomenon is better understood in the context of holiday liquidity and thinner trading volumes. In any given year, it is more a reflection of investor risk appetite. A strong Santa window signals that investors are comfortable carrying risk into the new year, while a weak or negative one might be seen as an early yellow flag. At best, the Santa Claus rally is a probabilistic sentiment tell, not a reliable forecast tool.

The Macro Environment for a New Year

Recent economic indicators continue to paint a mixed picture for the economy heading into 2026. While supportive fiscal and monetary policies suggest continued economic expansion over the next twelve months, other indicators appear to be more consistent with late-cycle economic conditions. There is a degree of concern over the strength of the labor markets, given the interruption in U.S. government data due to the shutdown.

Positives for the coming year could include less tariff uncertainty, a new Fed chair bringing less monetary uncertainty, and visible returns relative to AI capex investment. These, and other tailwinds, indicate that a

constructive outlook for the economy is reasonable.

The questions for investors will be different, given that capital markets are currently priced for perfection.

Happy Holidays!

As we move deeper into the holiday season, your team at Clearwater Capital wishes you and your family the very best. We look forward to serving you in the New Year.

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