

Volatility Returns

May 24th, 2019

After last year's fourth-quarter meltdown, the stock market returned to its low volatility ways and was in rally mode during the first part of this year. We have gone more than four months since the last 3% correction. Not only was the current stretch abnormal from a duration perspective, it was unusual coming off a low. Perhaps it was the Federal Reserve "Pivot" that lulled the market into complacency. In January, the Federal Reserve made an unexpected 180 degree policy change from increasing interest rates and signaling the end of its quantitative tightening policy to contemplating an interest rate cut.

The recent pull back after the best first quarter in years is not surprising. The S&P 500 averages 3.4 corrections of at least 5% and 1.1 corrections of at least 10% in any given year. With the rhetoric on U.S./China trade negotiations ramping up again, volatility finally resurfaced.

***So what does it mean now?* Ultimately, the fundamentals matter. When you step back and look at the last 18 months, you will see that corporate earnings have grown (+25%) but the stock market is only up +8%. This means valuations are significantly more reasonable. Whether and when a trade deal is reached will determine the level of volatility. But the underlying strength of the market heading into the turmoil can have a say in the amount of downside risk.**

Since the beginning of the year, there have been no net inflows into equity ETFs and mutual funds. While corporate buybacks have driven the market higher, the lack of inflows into equity funds is an indication that there is quite a bit of demand building up on the sidelines from individual and institutional investors. When the all clear signal sounds, the next move higher in the equity market could be a powerful one. Your portfolios will be well-positioned to take advantage of the next leg in the cycle.

Happy Memorial Day. We would like to acknowledge those who gave their lives serving in the U.S. military. Thank you!

Best,

Dan Moskowitz, CFP