CADARETGRANT

February 2018

Market Volatility Perspective

"During such scary periods, you should never forget two things: First, widespread fear is your friend as an investor, because it serves up bargain purchases. Second, personal fear is your enemy. It will also be unwarranted." ~ Warren Buffet

Dear Friend,

Recent volatility may be making you restless. I want to reassure you that what you're seeing is a natural progression of being invested in the stock market—the market goes up, the market must come down, and the cycle repeats itself. It's the nature of investing. The circumstances that lead to each part of the cycle may be different. Here's some explanation of what we're seeing and what the future may hold.

What happened? On Monday, February 5, the Dow Jones Industrial Average dropped 1,175 points. On Thursday, February 8, the Dow entered correction territory after falling another 1,032 points, extending the week's selloff to more than 10%. Monday's drop represented the largest intraday point fall in history, and Thursday's was a close second. But by percentage, neither decline even approaches the top 20. While headlines shout of record breaking falls and speculators are spooked by the sudden spike in volatility, smart investors with a long-term focus have identified an opportunity to buy.

What caused the drop? The January 2018 labor report indicated that wages had increased 2.9% year over year, which was both more than expected and higher than the labor market had seen in some years. This surprise caused investors to fear that inflation would also rise more quickly than anticipated. Investors became nervous that the reappearance of inflation would encourage the Federal Reserve to raise interest rates more quickly within the next two years, causing the cost of capital to become more expensive. These leading indicators caused the bond yield to increase.

The market ascent of the past 18 months resulted from the artificial calm created by the Federal Reserve. In order to inject cash into capital markets during the Great Recession, the Federal Reserve adopted a policy of "quantitative easing," in which the Federal Reserve purchased securities as a measure to lower interest rates and encourage spending. However, the economy is now in its ninth year of expansion and doesn't need the additional support of the Federal Reserve. The end of quantitative easing means that the Federal Reserve is no longer purchasing securities and is raising interest rates. As the economy continues to show signs of growth, the Federal Reserve is likely to accelerate "quantitative tightening," and interest rates will rise.

Experts are saying that this correction is normal. The bull market has continued unchecked without correction since 2016, and stocks have become overvalued. Historically, equity markets experience a correction of at least 3% twice a year and 10% annually. The markets have been overdue for a correction and have been abnormally free of volatility. The

correction—an investor reaction to the prospect of rising interest rates—indicates that markets are entering a new period of volatility. Markets may rise or fall at any time, but it's not expected that the immediate future will include descent into a bear market.

What does the future hold? Is the market foreshadowing a recession? Experts remind investors to consider the fundamentals. Global economies are enjoying a period of strong synchronized growth. Corporate earnings are strong, and U.S. companies should enjoy additional cash flows in 2018 from the Tax Cuts and Jobs Act. Unemployment rates are low, and wage growth is gaining momentum, which will allow consumer spending to fuel economic growth. Deutsche Asset Management commented on the correction in terms of the greater economic landscape: "We remain constructive for equities, due to the synchronized global recovery, which we expect to underpin strong earnings growth. Given that until recently, investor sentiment was near record highs, we think that some sort of correction was indeed overdue. For stock pickers, such phases can certainly bring opportunities."

The nearly unanimous sentiment is that volatility is here to stay, and that it's healthy. Volatility is an unpredictable force, and investors can't let short-term fluctuations spook them. Historically, volatility in the markets can lead to greater returns for investors. Many will take advantage of the opportunity to identify companies that are poised for significant future growth and buy shares at a discount. An active strategy can be an asset to an investor's portfolio during a period of volatility.

A key takeaway for investors is that it's essential to maintain a long-term focus. While the indices may rise and fall, history suggests that the market will recover and climb to new heights. Corrections and volatility can bring discomfort in the short term, but your portfolio has been carefully designed to protect you from undesired levels of risk. The urge to react to fluctuations is natural, but impulsive adjustments can cause investors to miss out on the market's best days.

I'm monitoring the markets closely and am here to offer perspective and coaching through market fluctuations. The markets are always testing us, and now could be a good time to revisit your risk tolerance. If you wish to discuss the positioning of your portfolio, I'd be happy to review your financial goals and strategy with you. For perspective, ask yourself this: Knowing what you know now, what, if anything, would you have done differently in 2008, following the last significant correction?

Please don't hesitate to contact me with questions at (717) 533-6243.

Sincerely,

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