Volatility: Welcome Back to Normal

By Gregg Biro

So that's what market volatility feels like! It has been a while since we've had dramatic swings in stock markets across the globe. But these past few months have been a reminder of how volatile markets can be.

U.S. stocks returned just over 21% last year. As measured by the Center for Research in Security Prices (CRSP), 2017 was the 32nd best performing calendar year return for U.S. markets going back to 1926; or, said another way, one out of every three years has produced returns at least as good as 2017. From a return perspective, it was well within the range we should expect. Where it was a bit unique, however, was from a volatility perspective. The VIX, a standard measure of market volatility that gives us data back to 1990, was at historic lows for most of 2017. See the VIX chart (*Figure 1*) below.

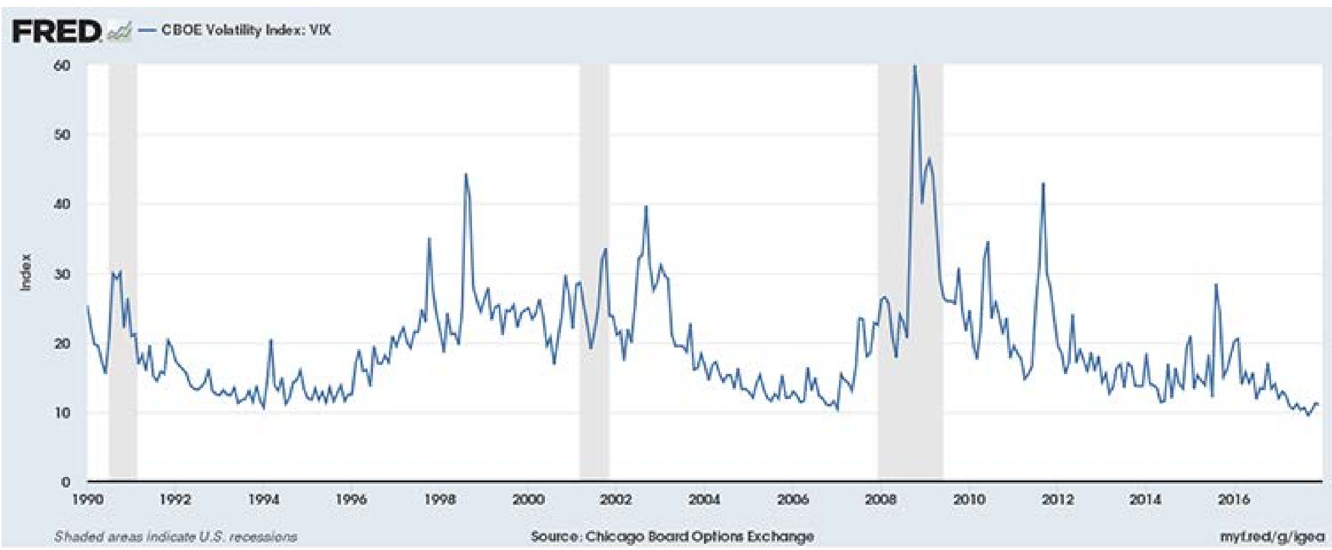

Figure 1

2017 was not unprecedented from a volatility perspective, but levels that low are rare. All of which is to say that what we've experienced the past couple of months is far closer to historical norms for market volatility. Below (*Figure 2*) is the same graph as above with the inclusion of the first 6 weeks of 2018. You can see the spike back to normal ranges.

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Integrated Wealth Management Since 1988
301 East Pine Street | Suite 600 | PO Box 4930 | Orlando, FL 32802-4930
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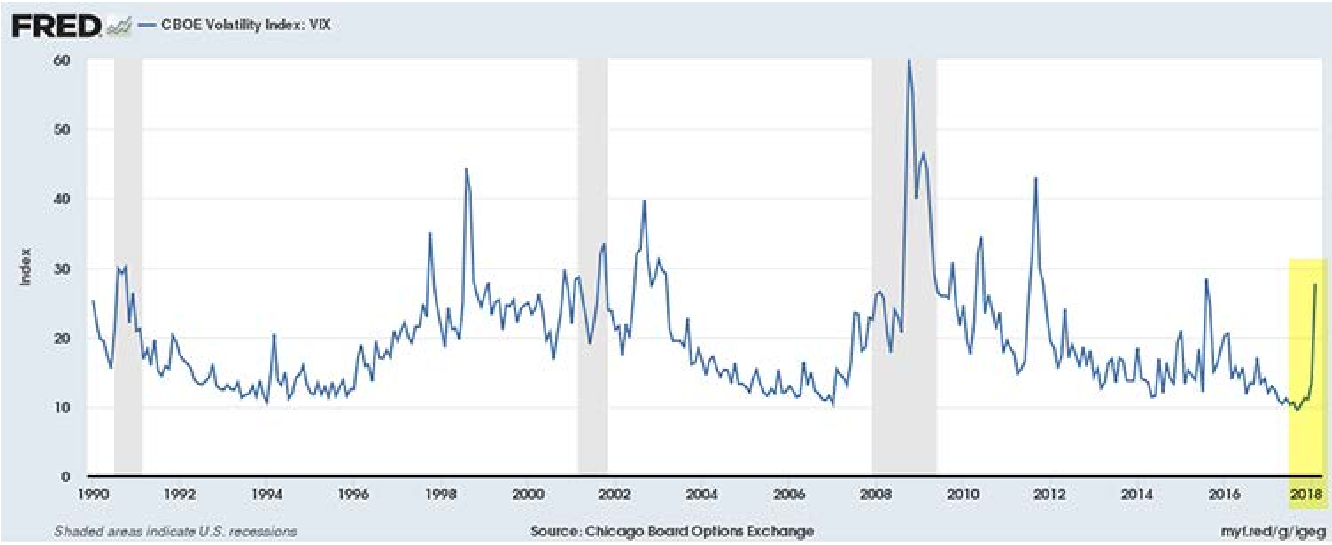

Figure 2

As a long-term investor with a portfolio allocation established to meet your long-term goals, it's important to remember that markets like these are expected and accounted for in your plan. The easiest way to negatively impact a plan is to react to sensational headlines and there are some doozies out there.

There are two big sensational themes that show up more often than others. Remember, the headline writer's goal is to get readers to read or click.

Theme #1: The DOW Has Its Biggest Point Drop Ever

First of all, the DOW is not the most appropriate benchmark relating to a globally diversified portfolio – just because it's a familiar name does not make it appropriate. Second, relativity matters. A 1000-point drop in the DOW is different now from what it was ten, twenty, or thirty years ago when the index level was lower. The percentage change is more relevant. The DOW's largest point drop ever of 1032 points on February 7, 2018 was the 100th worst percentage drop in history. In other words, days like that happen on average once per year.

Theme #2: These Daily Swings Matter and You Need to do Something About It

They do not, and you shouldn't. It sounds tempting to do something, but these swings are inevitable. Regarding the bumpy ride associated with stocks, a 2013 USA Today article quoted Warren Buffett as saying, "Don't beat yourself. Beating yourself is half the problem."

Long-term Focus

These headlines will continue well into the future. The essential point is that the recent volatility we've experienced is relatively normal. The low volatility in 2017 was not the norm. The allocation you and your advisor have selected gives you the best chance of meeting your long-term goals. Sticking to your plan is what matters most and nothing that has transpired lately should change that disciplined approach.

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