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WEEKLY PERSPECTIVE ON CURRENT MARKET SENTIMENT

Volatility Can Be Your Friend, Not Your Enemy

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Last Week's S&P 500 Index:
-5.2%

Key takeaways

» *Volatility often creates opportunity. For those with sidelined cash, be ready to step in and execute your plan to take potential advantage of the pullback.*

» *Uncertainty surrounding Federal Reserve (Fed) monetary policy and wage pressure on corporate margins should result in additional opportunities to put money to work in coming weeks.*

After last week's steep selloff, this strategist broke out his calculator and quickly determined that the S&P 500 ended Friday 8.8% lower than its all-time record closing high on January 26. But boy, it sure doesn't feel that way. Even many of the so-called professionals in this market are reacting as though stocks have crashed and the bull market is over. Multiple big names in the equity-strategy and money-management businesses have been on the television networks telling viewers they were shorting equities, or at least reducing exposures, over the course of last week. And as far as regular investors are concerned? Based on our view, most of them sat on their hands and did nothing but watch the market go down. Even though many of them are sitting on cash they have intended to invest in stocks, they froze as 1,000-plus point swings in the Dow Jones Industrial Average made their stomachs churn. Not exactly what we have been recommending they do.

As regular readers of this piece know, we have been waiting, anticipating, and yearning (yes, yearning) for increased volatility in the market for some time, but stocks have not cooperated. Equities have pretty much made a determined, gradual march higher over the last 14 months with hardly a stumble along the way. In fact, until last week, the last time the S&P 500 experienced a 10% pullback was two years ago. Historically, that is a long time between decent corrections.

But the time seems right for a more volatile period in the markets. Confusion reigns supreme over whether the major central banks will more aggressively drain excess liquidity from their financial systems now that growth has improved. The question as to whether the Fed will make a mistake and raise rates too far too fast was a big factor in last week's selloff. And personally, this strategist would not want to bet against the Bundesbank (Germany's central bank and basically the holder of the keys to European monetary policy) having drawn up an elaborate and ultimately effective plan to meaningfully slow liquidity growth well in advance of any hint of a potential jump in inflation. In addition, fear of U.S. wage gains negatively impacting high corporate margins was also a huge factor in last week's drubbing.

We will likely continue to see a few good potential buying opportunities in the equity markets in coming weeks (and maybe longer). But trying to pick the bottom in any pullback, as always, is not going to be easy. Our forward outlook on the economy and inflation is positive. Our outlook for the international economies is also good. While that might not exactly be a bold prediction, we feel the need to once again point out the importance of having a plan to invest sidelined cash in the market on the way down. Ideally, we believe investors should step in and gradually execute that plan as opportunities arise. This strategist will not be able to tell you where the precise bottom will be.

Take advantage of what the market is giving to you. Potentially, in the nearer term, more opportunities will present themselves. We may have had a bounce off Friday's low, but it is unlikely the market will be all clear sailing from here. Volatility can be your friend—don't treat it like your enemy. Use it to your advantage.

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