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THINGS YOU SHOULD KNOW ABOUT STOCK MARKET VOLATILITY
By Joel Sullivan, Partner

At this point you are probably suffering from whiplash from the stock market's roller coaster ride since the first of August. Volatility has been quite high this summer. Since the first of August till today, there have been 37 trading days. Of those 37 days, the Dow Jones Industrial Average has had 18 intraday moves of 300+ points. That is a lot of volatility. And high volatility usually results in high anxiety for investors, or maybe high anxiety results in high market volatility.

In either case, the question is… what is the best way to respond to the volatility we are experiencing? It is important to realize that we are bombarded with information on the economy and the stock market on a minute by minute basis. I consistently tell my clients not to overreact to short term market fluctuation. The best approach is to step back and look at the market over a longer time frame than day by day. Secondly it is helpful to look at things from a historical context.

We all know that markets go up and markets go down. However sometimes, when you are in the middle of a down period it feels like markets only go down. If we look back over the last 41 years, the S&P 500 was down an average of 119 times a year, or 47% of the trading days. That's all fine, but some may say that is ancient history, things are different now….right? Wrong! Things really haven't changed much over the years. As a matter of fact, from 1990 to 2010, the market closed down 47% of all trading days; less than one half of the time, and right in line with the historical average. The one thing that is probably different is the amount of media attention every piece of economic and market news receives. This can make us feel worse than we should about our investments.

The frequency of down days doesn't dictate annual performance. So even though the market finishes lower almost 50% of the days, the annual performance has trended up over the years. From 1970 through 2010, the S&P 500 had positive returns 31 of 41 years. Given that ratio, it would not be wise to bet against the long term trend of a rising market.

We only have to go back to 2010 to get an example of the up and down nature of the stock market. From May to July of last year, the Dow Jones average fell 13%, only to rebound in the 4th quarter and finish the year up 11%. Now, from May of 2011 thru today, the market has fallen 16%, very similar to last year. Of course we don't know how the year will finish, but we only have to look to last year to see how quickly markets can turn around.

Remember, investing isn't always going to be a smooth or pain-free ride. But history shows us the next wave of down days has little to do with what the market does the rest of the year.

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