Market volatility makes a comeback

For investors, 2017 was an unusually calm year. The S&P 500 stock index never changed by 2% in a single day, either up or down. There were only eight 1% days all year.

2018 is shaping up to be a very different story. CNNMoneyInvest reports that in the first quarter we've already had six 2% days and 23 1% days. Should this pace continue through the year, we'll have the most volatile year for stock prices since 2008.

Two economic factors may be contributing to these wild swings. The U.S. economy is at, or nearly at, full employment. Labor shortages have appeared in some parts of the country, raising questions about how much more economic growth we may expect. As important, by some measures stocks have become expensive compared to their earnings. We might be approaching a market top. This is an environment that investors have not seen before, and they seem uncertain about which way to jump. Will the federal tax cuts result in a surge of economic growth, making this a good time to increase equity exposure? Or will external factors—perhaps a breakdown in international trade, or a new foreign conflict—trigger a selloff? No one can know for certain.

The way to calm volatility in an investment portfolio is by diversifying among asset classes—adding more bonds, for example. The bond markets also can be volatile, but at times stock and bond prices move in opposite directions. Having a well-diversified portfolio may bring steadier investment returns.

(April 2018)

© 2018 M.A. Co. All rights reserved.