4.10.18

HISTORICALLY LOW VOLATILITY TO HISTORICALLY HIGH VOLATILITY… WOW!

We reduced our portfolio risk from 18% to 13% last week. The majority of our risk is in two ETFs (exchange traded funds) that track the S&P 500 and the Russell 2000 stock index. We are keeping these strategic trades in place for the near-term as we see a high probability that markets will bounce upwards into mid-April before pulling back again. Each day we are assessing our economic outlook and deciding whether to sell, hold, or increase our equity position. In this whipsaw market, the goal for these trades is to get take advantage of a 2% to 3% market gain and then to sell. With the tools and investments we have at our disposal, we can invest in the market with a multitude of objectives, ranging between growth and preservation. In addition to the funds set aside for these short-term strategic trades, we have our core portfolio which is intended to be held for much longer periods. On Friday, we added a 10% longer-term position in the PIMCO Enhanced Short Maturity ETF (MINT). This fund features a yield of 2% and very minimal volatility. We see this investment as an alternative to holding cash and at this juncture we are looking to add additional funds with this type of stable return in the near future.

“I have never seen a market this volatile to this extent in my career. Now that’s only 66 years, so I shouldn’t make too much about it, but you’re right: I’ve seen two 50% declines, I’ve seen a 25% decline in one day and I’ve never seen anything like this before.”
- Jack Bogle, Vanguard Mutual Fund founder and retired CEO

Our sentiments couldn’t be any closer to this timely observation. Keep in mind that Bogle is a “set it and forget it” investor who heralded in an era called “passive investing.” Passive investing is an investment strategy that simply mirrors major stock and bond indexes, with very little portfolio optimization or risk awareness. Oftentimes the only way to get the attention of investors like Bogle is to get a sudden explosion of volatility, which is code speak for a rapidly changing environment with a tendency for shocking declines.

JPMorgan CEO Jamie Dimon chimed in with this quote from his epic annual letter to shareholders: **“Volatility and rapidly moving markets should surprise no one, volatility only shows up as a concern when it’s in a downward direction and it doesn’t take much to trigger it.”**

Over the last two months we’ve seen multiple triggers. Stock market leaders (with excessively high valuations) like Facebook, Amazon, Apple, Netflix and Google have all dropped between 6% and 15% in just the last month. Even with this decline, their valuations remain in nosebleed territory. More importantly, no other sector seems capable of replacing these stocks as market drivers, creating a leadership void for the time being. Another trigger lies in the fact that many corporations remain in a blackout period for buying back their own stock in the stock market, which is creating another vacuum of uncertainty. One more primary trigger is the ever-expanding debt markets coupled with the threat of higher interest rates. Interest on the 10-year treasury at this juncture stands at 2.8%, which still puts us precariously close to the 2.9% rate that initially tipped over the stock market’s apple cart in early February. With this in mind, obsessive focus has again been placed on the Federal Reserve and it looks like they will continue on their path of reducing extraordinary monetary stimulus regardless of the recent 10% market decline. Headlines about the risk of tariffs, tweets about Amazon, cabinet shuffling by the President – or possibly worse – have provided a temporary sideshow to the aforementioned issues. In fact, the President himself tweeted that "We are not in a trade war with China; That war was lost many years ago by the foolish, or incompetent people who represented the US. Now we have a trade deficit of $500 billion a year with intellectual property theft of another $300 billion. We cannot let this continue!"

In the first three months of the year, the S&P 500 has had 23 days with a 1% move. The historical average is for just 13 such sessions over a quarter. And… Over the prior two years, we actually reached the most complacent levels in history! As a percentage, volatility since the beginning of 2018 has increased in the range nearly 95% over the previous two years!

Last Friday, the markets were expecting new job creation across the U.S. to come in at 200,000+ but instead it came in at just 103,000. March nor'easters may be partly to blame having made it more difficult for individuals to look for work or get to work. One positive in the report was that hourly earnings crept up from 2.6% to 2.7%, but overtime and aggregate hours worked were little changed.

Other reports put a grey cloud over economic growth as Gross Domestic Product for the first quarter was ratcheted down to 2.3% while Consumer Credit Usage (credit cards, auto loans and student loans) rose significantly less than expected, foreshadowing a possible slowdown in consumption.

This week's economic news will be laser-focused on inflation reports for both producers and consumers. Additionally, earnings season kicks off on Friday with Bank of America, JPMorgan and Wells Fargo. We will be watching closely for any tailwinds from the Trump tax cuts to potentially start showing up throughout the next month of earnings. The Federal Reserve will release the minutes from its last meeting in March while no less than five speeches will be given from the Federal Reserve surrounding various components of monetary policy.

As always, we will continue posting articles that we believe to be of great informational value on our website, under the "Great Articles" tab, which is linked here:

http://summitplan.com/cgi-bin/htmlos.cgi/great_articles.html.

Additionally, the "Summit Planning Financial Hour" will be live this week on Radio 570-WSYR at 10AM on Saturday. Don't forget to tune in for a recap of the week's events. If you cannot tune in, check out our radio show archive on our website at http://summitplan.com/cgi-bin/htmlos.cgi/radio_shows.html.

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4. All performance referenced is historical and is no guarantee of future results. Index performance is not indicative of the performance of any investment.
5. Investors FastTrack is the source for all quoted performance data.
6. The fast price swings in commodities and currencies will result in significant volatility in an investor's holdings. Commodities include increased risks, such as political, economic, and currency instability, and may not be suitable for all investors.
7. Bonds are subject to market and interest rate risk if sold prior to maturity. Bond values will decline as interest rates rise and bonds are subject to availability and change in price.
8. The Dow Jones Industrial Average is comprised of 30 stocks that are major factors in their industries and widely held by individuals and institutional investors.
9. The Standard & Poor's 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.
10. The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on The NASDAQ Stock Market. The market value, the last sale price multiplied by total shares outstanding, is calculated throughout the trading day, and is related to the total value of the Index.
11. The Russell 2000 Index is an unmanaged index generally representative of the 2,000 smallest companies in the Russell 3000 index, which represents approximately 10% of the total market capitalization of the Russell 3000 Index.
12. CBOE Volatility Index is a measure of the implied volatility of S&P 500 index options, calculated and published by the Chicago Board Options Exchange (CBOE).
13. All indices are unmanaged and cannot be invested in directly.