Expect Volatility

by Sue Stevens

The past two years have seen an unusually low level of volatility in the stock market. That can lead to complacency. Last week, we started to see bigger "air pockets" emerge, which can be jolting to your system.

To put Friday's market drop in perspective, the Dow fell about 2.5 percent. It was down 4.1 percent last week. Monday saw an additional 4.4 percent drop for a total of 8.5 percent down within a week.

A 10 percent drop is normal. We're just out of practice. Don't let the media throw you off balance.

So What Happened?

The jobs report came out and showed more people are working. That sounds good, right? But some people read that to mean that the Fed will "tighten" more quickly — or raise interest rates more often. The prediction is that it will do so four times this year. We already knew that. It's basically a sign of an improving economy. No real problem there.

But that can mean inflation can be on the move, too. It's not a problem now. And most projections show it picks up, but not dramatically so.

Bond interest is rising as well. Again, that was expected. Last week the 10-year Treasury jumped to paying 2.85 percent. This week, we're back closer to 2.6 percent. We've been waiting for it to rise above 2 percent for quite a while. Economists predict it may hit 3 percent by year-end. 4 percent is more of a historical level, but 3 percent is more likely in this environment for some time.

What Should You Do?

Right now, do nothing. If the market continues to drop, that's in line with a normal correction. Many stocks were on the pricy side, so this can be a good buying opportunity. The last correction, in January 2016, was only about 5.5 percent to 6 percent. And everybody got all excited then, too. Most economic signs now show healthy growth worldwide.

Indications are the U.S. stock market will perform in the single digits going forward (of course, we never know what will happen in the future). The dollar has been weaker this year, even though President Trump is hoping it will strengthen. Both of these factors support including international equities in your portfolio.

As interest rates rise, yield-hungry investors will probably move from dividend-paying stocks to fixed income. People jumping ship from dividend-focused funds could lower the funds' net asset values (NAVs). You should also be sensitive about where you hold these types of funds for tax reasons. If you are sitting on large capital gains in taxable accounts, your advisor should be thoughtful about when and how you take those gains. In some cases, it may be wiser to take some gains, pay the tax and rebalance your portfolio.