Craig DeMaio: Keeping a watchful eye on market volatility

By **Craig DeMaio**

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Volatility is defined as changeable, mercurial or flighty. And that certainly is an apt description of the stock market over the course of the past couple of weeks and what we can expect to see in the near future.

Although the wild swings of the first full week of February are likely past us now, there still is a lingering uncertainty about what comes next, and much of that uncertainty centers on the myriad explanations about what caused the volatility in the first place.

Some early comments placed the blame on fears of rising interest rates, due in part to increases in wages, which were thought to be the precursors of inflation.

Still others wrote it off as a long-awaited correction that some analysts say has been looming over the market for years. That speculation was compounded in the early phase of the market drop by references to the 2008 sell-off, which represented trading that amounted to trillions in investment value.

Investigation into that period of volatility showed that vulnerabilities in the U.S. financial system were exacerbated by intentional "bear" raids on the stock market by foreign investors, resulting in massive sell-offs that threatened the U.S. economy.

Whether a similar situation exists currently is not yet known, but one factor that existed a decade ago does not hold as much influence on markets today — the price of oil and its availability outside of OPEC. The U.S. has steadily moved from being a net importer of petroleum products to a major exporter at the same time the world demand for oil has dropped somewhat, and the U.S. could become a net exporter in the next five years or sooner.

When OPEC countries cut exports, the U.S. now responds by increasing exports by the same amount or slightly more, which lately has maintained oil prices in the high $50 per barrel to low $60 per barrel range. The increase in U.S. exports has been offsetting OPEC reductions for more than a year.

While the volatility appears to have smoothed somewhat, there still are events on the horizon that could either settle frayed nerves or lead to a new round of selling and buying. In the first two weeks of March, government reports will be issued on construction spending; manufacturing shipments, inventories and orders; manufacturing and trade and new residential construction, among others. And on March 20 and 21, the Federal Reserve Open Market Committee will meet and issue a summary of economic projections and a decision on if they will raise interest rates.

Regardless of what caused the extreme shifts in the stock market, it has nonetheless appeared to settle some 1,000 points below its recent high, and that in turn has resulted in some attractive buys for the well-informed bargain hunter. For instance, stocks listed in the S&P 500 index recently were trading at 16.5 times their earnings, while only two weeks earlier they were trading at 18.1 times those earnings.

Some stocks are trading lower due to the overall decline in the market, but some are trading lower for other reasons ranging from the health of the sector to the performance of individual companies. The key is knowing which is which, and the key to that is solid, informed research.

There are important questions to ask: “What’s more important to me, risk mitigation or performance?” “Have I established reasonable risk vs. return parameters in light of low-interest rates?” If already retired, “can I afford a big market downturn?” “With life expectancy increasing, how much is enough?”

As with any other state of the market, bull, bear or somewhere in-between, those who profit from these opportunities are those industrious individuals who take the time and effort to fully acquaint themselves with the new realities and make sure they are on solid ground before making their choices.

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