February 6, 2018

MARKET VOLATILITY HAS RETURNED

We view the recent stock market volatility as a correction rather than the start of a prolonged bear market. We would stress the following points as the market undergoes its first significant correction since the summer of 2016.

- The selloff began after the stock market had a historic move higher to start the year, and had become "over-bought" on many technical measures.
  - *Corrections and consolidations are common after major moves in stocks. Corrections are a difficult but normal part of the stock market cycle. Over the last 30-years, the typical year has seen an average intra-year drop of 14% while ultimately producing a positive return of 10%.*
- The selloff also corresponded to Treasury bond yields moving higher with investors becoming concerned that higher interest rates would choke off the economic expansion.
  - *We view higher bond yields as a sign of a healthy economy and that we are a long way from choking off the economic expansion with higher interest rates.*
- The selloff accelerated as the employment report showed signs of wage inflation, which could cause the Federal Reserve to quicken its pace of interest rate increases.
  - *We have been expecting wage gains to move higher for some time and view this as a healthy response to a strong economy and job market. This should also cause inflation measures to move higher toward the Federal Reserve's target levels – levels that we have been undershooting since the financial crisis.*
- The Federal Reserve has been running a very easy monetary policy since the financial crisis in order to stimulate economic growth and ultimately job and wage growth.
  - *We are still far removed from tight monetary policy that would choke off the economic expansion and cause the next major bear market.*

We Remain Favorable towards Global Economic Growth and Stocks:

Major bear markets are typically associated with recessions and we still aren't seeing signs of one. We remain encouraged by the global economic data. Recent global business surveys continue to point to solid economic growth, while global business and consumer confidence readings are making new cycle highs. This has led to synchronized global economic growth, which is supporting growing corporate profits and ultimately supporting stock prices. All of this has been augmented by the pro-business tax reform plan signed into law late last year by President Trump.

We would therefore use the current sell-off as a buying opportunity. We continue to favor global stocks and prefer cyclical exposure through Financials, Industrials, Materials, Energy and Technology.