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FINANCIAL FORUM

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Market Commentary – Thoughts on Market Corrections

Where do we begin? If the first six weeks of 2018 are any indication, it's going to be a wild ride in the financial markets. After one of the longest streaks on record of low volatility and a one-directional (up) market, things may be getting back to "normal." For those of you who need a refresher, "normal" means a market that goes both up and down and suffers from the occasional correction, defined as a drop of at least 10%. In fact, history tells us that market corrections are quite common, occurring about once a year – or, in other words, they come around about as often as the Super Bowl; they're just less entertaining.

The month of January saw euphoria levels reach all-time highs, as investors poured record amounts of money into stocks, while reducing their cash holdings to their lowest levels in 18 years (December 1999 tech bubble). The savings rate fell to 2.4%, back to levels seen in 2007-2008 Great Recession period, while margin debt increased to another record high. Various investor/consumer confidence surveys reached record levels of (over) confidence, with the Investor Intelligence Survey reporting bulls to bears at a five to one ratio, historically very rare. As you know, when all your weight has shifted to one side, it can be easy to lose your balance and fall in the other direction.

This correction was as overdue as a septuagenarian going through a midlife crisis. Prior to last week, the S&P 500 had gone 404 trading days without as much as a 5% decline, its longest streak ever. But what made this decline noteworthy was that it wasn't caused by recession fears, but rather, by too much growth. To date, about 80% of companies reporting earnings have beaten estimates and, with tax reform now passed, many companies have raised their guidance for the remainder of this year and next. Additionally, the Atlanta Fed's GDP Now has increased its growth forecast for the first quarter to 4%, with tax cuts, a weak dollar, and strong synchronized global growth as reasons contributing to the upward revision.

All sharp market movements need a triggering event. For this correction, it was a rise in Treasury bond yields that occurred after the January jobs report showed that wages for the month increased by 2.9%, exacerbating fears that inflation will rise too quickly and that the Federal Reserve may have to hike rates more quickly than anticipated. Additionally, it is not just our Fed that is in a tightening cycle. Most major central banks around the globe are also indicating an end to the low-rate, easy-money environment of the last nine years. Therefore, with the concern that the U.S. economy is at full-employment (by historical measures), rates are still low (again, by historical levels), global growth is accelerating, and fiscal policy (i.e. tax cuts) is turning ultra-accommodative, the thinking goes that rates will have to increase at a quicker pace which could eventually cause a recession.

Bottom Line: Bear markets are caused by recessions. It appears that this correction was the result of euphoric stock market sentiment, as well as, a miscalculation that bond yields could rise more quickly. However, it is important to note, that corrections that occur during an economic growth period, tend to be shallow (average decline of 13%) and short-lasting (market makes back the money in under six months.) Of course, as a couple of old sayings go, past performance is no guarantee of future results and every bear market starts out as a correction. That's why we're here monitoring the situation very closely on your behalf.

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Wealth Management – Social Security Survivor Benefits

According to the Social Security Administration, there are about five million widows and widowers receiving social security benefits on their deceased spouse's earnings record. The decision as to whether to initially claim social security benefits under your earning's record or those of your deceased spouse is a very important one. In cases where the answer is not so obvious, the wrong decision could cost you thousands of dollars over your lifetime. So, let's review the basics. Those born between 1943 and 1954 can claim a full retirement benefit at age 66. You can also collect as early as age 62, but those benefits will be permanently decreased to 75% of your full benefit. Alternatively, you can delay receiving benefits up until age 70, with the benefit amount increasing 8% for every year you delay. Surviving spouses are eligible to collect a survivor benefit as early as age 60. As a surviving spouse, you are eligible to receive a benefit equal to 100% of your deceased spouse's benefit, as long as you wait until full retirement age to collect. This option usually is extremely beneficial if your spouse was a higher earner. For some, it may be better to start collecting the survivor benefit at age 60 or 62 and then switching to your own benefit at age 70.

Example: Jack and Jill, both age 62, are married. Jack's full monthly benefit at age 66 is $1,000, while Jill's benefit at age 66 is $800. Neither has started collecting benefits and Jack dies. What are Jill's options? (1) She can claim a benefit based on her own earnings at age 62 and later switch to a survivor benefit, or (2) she can claim a survivor benefit now, and perhaps switch to her own benefit later. Let's say that she claims her own benefit now. Because she is 62, it will be decreased to $600 (75% of $800) a month. At 66, she switches to her husband's benefit of $1,000 a month. Based on her life expectancy, she would receive just under $245,000. However, if Jill switches the order and starts collecting the survivor benefit first and then switches to her own benefit at age 70, she would receive just over $255,000 in total payments over her life expectancy.

Bottom Line: There are many variables that have to be considered to determine the best course of action for surviving spouses, especially if one spouse was a high wage earner. In addition to working with a qualified financial planner, we recommend that you schedule an appointment with the Social Security Administration. They should be able to assist you with this analysis.

Weekly Thought – Volatility

Since 1871, the market has risen or fallen by more than 20% two out of every five years. Volatility is the norm, not the exception. It should be planned for and diversified against because the average investor will experience about 10 to 15 bear markets during their lifetime. Have a great week.

All the best,

Dan

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