Market *Alert*

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STANDARD & POOR'S

Heightened Volatility: The "New Normal" for Stocks?

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It was a cruel summer for investors. Washington kept Wall Street on "pins and needles" throughout much of the past few months with the contentious debate over the federal debt ceiling. A last-minute deal to avoid a Treasury default was finally struck, but lawmakers were unable to protect Treasuries from losing their AAA credit rating with Standard & Poor's.

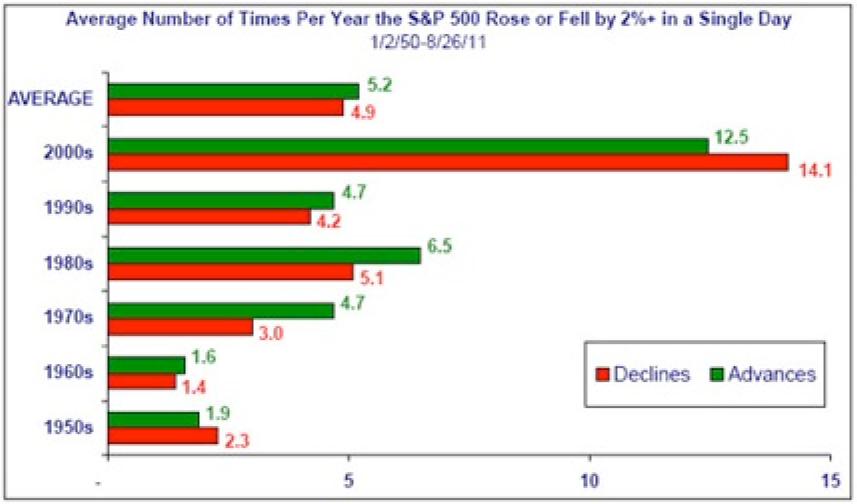
In the weeks following the downgrade, the markets have been volatile. Fears of a double-dip recession in the United States, a slowing global economic recovery, and the European debt crisis and possible contagion have dominated investor thinking.

In August, the S&P 500's percentage spread between intraday highs and lows reached 18.7% -- the widest since the 24.9%-mark registered during March 2009.[1] By August 24, the S&P 500 was down 13.6% since July 22 and 7.6% year-to-date.[2] Yet stocks rallied during the 5.8 magnitude earthquake that sent cracks down the Washington Monument, and the market all but ignored hurricane Irene as it prepared to barrel up the eastern seaboard. During the final full week of August, the S&P Global 1200 rose 3.3%, while U.S. large-, mid-, and small-cap indexes advanced from 4.7% to 6.1%. However, since the April 29 recovery high for the S&P 500, the benchmarks were still off 9.2% to 17.7%, with 37 of 40 sectors still in the red.[1]

What do the market's summertime zigs and zags imply for September, October -- and beyond? Perhaps that heightened volatility is now part of "the new normal," whether you rely on the recent past -- or historical evidence -- to make your case.

A Historical Perspective

Historically speaking, the market today is about three times more volatile than it has been in the past. Specifically, the S&P 500 rose or fell by 2%+ an average of 5 times per year from 1950 until 1999. Since 2000, however, that average jumped to 12.5 times per year for advances and more than 14 times for declines.[1]



Source: Yahoo.com

Who or what deserves the blame for heightened market volatility is difficult to say. On the economic side, uncertainty about when and how fully the economy will recover is a major factor. So are factors such as the heightened reliance on government monetary policy, unsustainable fiscal trends, and the apparent lack of collaboration among legislators in Washington. On the investment side, high-frequency trading, hedge funds, and inverse and leveraged ETFs all contribute to the volatility.

Takeaways for Investors

Regardless of the drivers, heightened volatility requires individuals and their advisors to exercise specific investment strategies. While many of these strategies are basic investing concepts that can be applied at any time, they are particularly important in a volatile environment.

- Don't panic. Don't sell into a rapidly declining market and don't buy into a rapidly rising market. You'll just be following the herd and locking in losses. Panic selling also runs the risk of missing the market's best-performing days. For example, missing just the 5 top-performing days of the 20 years ended December 31, 2010, would have cost you more than $19,000 based on an original investment of $10,000 in the S&P 500. Missing the top 20 days would have reduced your average annual return from 9.14% to 3.00%.[3]
- Take advantage of asset allocation. During volatile times, more risky asset classes such as stocks tend to fluctuate more, while lower-risk assets such as bonds or cash tend to be more stable. By allocating your investments among these different asset classes, you can help smooth out the short-term ups and downs.
- Keep a long-term perspective. It is all too easy to get caught up in the stock market's daily roller-coaster ride. This type of behavior is natural, but can easily lead to bad decisions. Instead, focus on whether your long-term performance objectives, i.e., your average returns over time, are meeting your goals.
- Consider buying opportunities. Although many of you may be rightfully gun shy in the wake of the recent market turmoil, one strategy you should seriously consider is selectively adding to your portfolio. This is especially true when prices are low versus historical averages. Barring a double-dip recession or a Lehman-like credit event in Europe, we believe the S&P 500 offers compelling value, as anything short of that has likely already been priced in by recent relentless selling.[2]

[1]Source: Standard & Poor's Equity Research Services, "Shaken and Stirred," August 29, 2011.

[2]Source: Standard & Poor's Equity Research Services, "Cruel Summer," August 24, 2011.

[3]Source: Standard & Poor's. For the period indicated. Stocks are represented by the S&P 500, an unmanaged index that is generally considered representative of the U.S. stock market. Past performance is not a guarantee of future results.