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A Quiet Summer Comes to an End

August Market Review From Your Portfolio Management Team—September 12, 2014

Stocks have continued to sail along (like a sailboat on the Chesapeake Bay) throughout the summer. A brief squall in July was easily reversed in August with the S&P 500 index rallying almost 4%. Small cap stocks also managed a strong return for the month, rising almost 5%. Foreign stocks, unfortunately could not keep pace with their U.S. cousins, as the average foreign stock rose only 1% or so. It was also a good month for the tamer bond funds as well, with the average bond fund rising 1% - 2%.

The S&P seems impervious to a serious drop, as any hint of stress—Ukraine, Syria, Fed Tapering, economic slowdown in Europe—is virtually ignored by the large-cap U.S. stock market (think S&P 500). Market volatility is also shrinking as these stocks continue to hit successive new highs. A popular measure of volatility is called the VIX, which measures the prices of a small basket of options. During periods of fear, the level of VIX can rise above 30 and can even spike above 50 for short periods. The average level of VIX over the past 20 years is 21. Over the past three years, VIX has been on a downward pace and currently sits below 12. These low numbers suggest a good deal of calm or complacency in the stock market.

These low numbers don't suggest that a correction is coming, necessarily, but they do suggest that investors are comfortable taking risk in stocks today, which could lead to some fireworks if something happens to spook investors from their complacency.

	2008 Return	2009 Return	2013 Return	2014 Return	Current Level
S&P 500	-37%	26%	32%	10%	2003
CBOE VIX	78%	-46%	-24%	-13%	12

Source: Fasttrack. Past performance does not represent future results. 2014 results are through August 29.

The table above shows the return of the S&P 500 over the past several years versus the return of the VIX index. As you can see, VIX tends to fall when the stock market rallies and rallies when the stock market falls. We have not seen VIX at these low levels since early 2007.

As we move from the traditionally calm time of the summer and enter the traditionally more volatile period of autumn, we want to stay vigilant for a return of more volatile times so that we can keep the portfolios on a consistent path and spare you from needless stress. These low readings of the VIX index suggest a high degree of complacency among investors, and high complacency is often the kindling that fuels a stock market correction. As the Fed winds down its 'tapering' actions over the next few months, and with mid-term elections looming, the pleasant times in the stock market that we have seen so far this year could easily take on a more ominous tone.

Please let us know if there are any changes to your personal situation that might suggest some changes to your investment objectives.

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