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Investment Institute

Market Commentary

Weekly perspective on current market sentiment **May 5, 2021**

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Last Week's S&P 500 Index: +0.02%

Potential opportunity?

Key takeaways

- While we don't know exactly what might create a potential buying opportunity in the stock market, the key is to have a plan to act.
- One potential opportunity source in coming months may be higher-than-expected inflation readings causing investors to worry about how the Federal Reserve (Fed) will respond.

Many investors with funds on the sidelines have been wondering when a pullback might occur that would give them an opportunity to put that money to work in the stock market. The short answer is we do not know when downside volatility may present a chance to take advantage of lower stock prices. And we can't be certain of the trigger. On top of that, a quick glance at a chart of the S&P 500 Index shows that anything approaching a meaningful pullback has not occurred since last October. We have had a relatively stable run higher as the major indexes have logged a long series of all-time record highs despite what some would consider a quite uncertain economic and investing environment.

But markets do not move steadily in one direction forever. There are twists, turns, and bumps along the way. Given our positive economic outlook over the balance of this year and into 2022, a strategy of dollar cost averaging into the market has been recommended over the last year with the thought that at some point the road might get a little more rocky and a more noticeable pullback might occur. After all, looking back over the last 80 years of stock market history, the S&P 500 has experienced a 10% pullback on average approximately every 11 months. That means, typically, there are opportunities to put sidelined funds to work on a somewhat regular basis. We want to be ready to take advantage of potential buying opportunities given our outlook.

We believe a key to being able to put sidelined funds intended for stock market investment to work is to have a plan. Know where the "holes" are in your portfolio and decide what you want to buy before the opportunity presents itself so that you are ready to act in a timely fashion. For example, if one's portfolio is lacking recommended exposure to the Industrials sector (currently rated favorable), figure out what individual stocks or exchange-traded funds (ETFs) you prefer to buy to fill that need. Or, if more broad exposure is preferred, determine what financial instrument you will use to meet that need. Once again, planning ahead and knowing what you want to buy before the opportunity presents itself is an important part of the puzzle.

While, as stated, we do not know exactly what will trigger a market pullback, we can make a guess at what might create a potential opportunity. In most cycles, rising inflation and what the Fed does about it have had a major impact on stock and bond prices. As the economy recovers from the pandemic, we are expecting a transitory jump in inflation. But the stock market will likely be very sensitive to any economic report that might imply an inflationary rise meaningfully in excess of what the consensus is currently expecting and cause concerns regarding what the Fed might do about it. This could offer a buying opportunity for stocks. Have a plan and be ready to act on that plan.

Risk Considerations

A periodic investment plan such as dollar cost averaging does not assure a profit or protect against a loss in declining markets. Since such a strategy involves continuous investment, the investor should consider his or her ability to continue purchases through periods of low price levels.

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors.

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