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Mitch on the Markets

Portfolio Manager Investing Insights

Are You Waiting for a Stock Market Correction Before Investing? Read This First.

The U.S. stock market remains strong. Mega-cap technology companies have propelled index returns higher since last October, but the rally has also gained breadth recently. The S&P 500 equal-weighted index, for example, has also risen to a record high, and approximately 20% of S&P 500 stocks are trading at or near 52-week highs. That's the highest percentage we've seen since May 2021.[1]

In late February, I wrote a column about strong market returns making investors worried. I wrote that seeing headlines about new all-time highs can easily "*give the impression that share prices are getting too frothy—especially considering that interest rates are still high, inflation is still above target, many Americans don't feel great about the economy, and the geopolitical outlook is one of uncertainty and instability*."

In that column, I debunked the idea that it is dangerous to invest in a stock market trading at an all-time high. All-time highs tend to lead to many more all-time highs, I argued and empirical data suggests that investors can experience solid 1-year average forward returns even when investing at all-time highs.

Some investors still prefer to wait.

The thinking is that the market will surely deliver a correction or a sizable dip to follow such a strong rally, which would then afford investors a better entry point than investing at all-time highs. This thinking is also backed up by data – since 1980, the S&P 500 has experienced an average intra-year decline of -14.2%, even as the index finished positive in 33 of those 44 years.[2] Corrections are normal, natural, and common.

So then, what's the harm in waiting for a correction to "buy the dip," instead of committing capital to a strong stock market trading at all-time highs?

ABOUT MITCH ZACKS

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The answer is that this approach means engaging in short-term market timing, which I think is the antithesis of how long-term investors should approach the markets. If your long-term goals are to generate growth or income or both, then what will ultimately matter is how much time you spend invested in the market – not how well you *time the market.* In my view, trying to time entry and exit points based on short-term market fluctuations will hurt total return over time more than it will help. Investors are far more likely to be wrong more often than they are right.

There is also the matter of what happens when you miss the best days in the market, which can of course happen if you're frequently attempting short-term market timing. Consider the performance of the S&P 500 over the 20-year period from January 1, 2004 to December 29, 2023, versus what happened to an investor who missed the best 10 or 30 days in that period[3]:

- Fully invested: +9.7% annualized return
- Missed the 10 best days: +5.5% annualized return
- Missed the 30 best days: +0.7% annualized return

Recall that remaining fully invested during this 20-year period meant absorbing the entire downside shocks of the 2008 Global Financial Crisis, the 2020 pandemic bear market, and the 2022 bear market. Yet missing just the 10 best days in the market meant having annualized returns nearly slashed in half, and missing the 30 best days meant earning basically no return. It's difficult to fathom how short-term market timing is worth the risk, in my view.

Bottom Line for Investors

Here's another way to critically think about the decision to wait for a market correction before investing. Let's say your goal is to wait for a -10% or a -15% dip, which historically is a healthy correction range. Given current levels (call it 5,100 on the S&P 500), this means you're waiting for the S&P 500 to fall to 4,590 (-10%) or 4,335 (-15%). The S&P 500 traded at those levels in June and November of 2023. Were you also waiting on the sidelines then? At what opportunity cost?

At the end of the day, I understand the difficulty of investing when the market has been rallying strongly for what seems like a long period. There's the difficult feeling that you may be investing at a local top, which is a tough pill to swallow *especially* if the market enters a correction just as you invest. But if your goals are long-term, and you're investing this money for the next 10, 20, or even 40 years, then timing does not matter as much as our minds lead us to believe, in my view. It's time in the market, not timing the market.

[1] Wall Street Journal. March 11, 2024. https://www.wsj.com/finance/stocks/it-isnt-just-big-tech-propelling-gains-in-the-stock-market-anymore-1b861482?mod=hp_lead_pos3

[2] J.P. Morgan. 2024. https://am.jpmorgan.com/us/en/asset-management/adv/insights/market-insights/guide-to-the-markets/

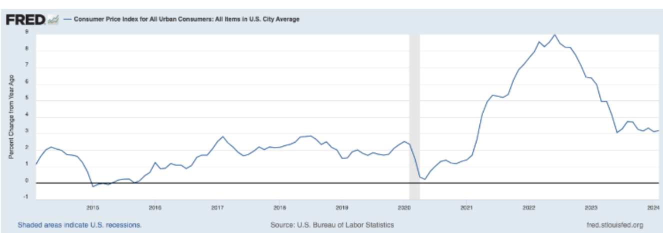
[3] J. P. Morgan. 2024. https://am.jpmorgan.com/us/en/asset-management/adv/insights/retirement-insights/guide-to-retirement/

STEADY INVESTOR WEEK

- **Inflation picks up to 3.2%**
- **Growth in the U.K. economy**
- **Americans are more hopeful about retirement**

Inflation Slightly Hotter Than Expected, But Doesn't Change Rate Outlook

The U.S. Labor Department released the latest inflation data on Tuesday, and prices ran a bit hotter than expected. According to the consumer price index (CPI) measure of inflation, prices increased by 3.2% in February from a year earlier, which was slightly higher than consensus expectations for a 3.1% rise.[1]



Source: Federal Reserve Bank of St. Louis[2]

Digging into the numbers a bit more, we find that gas prices and 'shelter costs' accounted for over 60% of the monthly increase, which we would argue helps explain why the stock market rallied after the CPI report's release. Gas prices are notoriously volatile, and do not factor much into the Fed's thinking on underlying inflation. And we've written before that shelter costs play a much bigger role in the CPI calculation than they do in the Fed's preferred inflation measure, the PCE price index. All told, the latest CPI release likely does not move the needle on the Fed's outlook for rates, reinforcing the market's expectations for three rate cuts in 2024. The equity market has also taken some level of solace in the recent jobs report, which included downward revisions to December and January payrolls and showed decelerating wage growth.

The U.K. Economy Appears to Be Turning a Corner

The U.K. economy has been in something of a rut over the past few quarters, still struggling to fend off high inflation and experiencing a much less compelling post-pandemic recovery than the U.S. The tides may be turning. In January, the U.K. economy finally returned to growth, with GDP rising by 0.2% month-over-month – better than the 0.1% expected. This modest growth follows a contraction in the second half of last year, which was unique among the Group of Seven large rich countries – all of which saw expansion over that period. Flipping back to growth is an important development not only for the U.K. but also for the global economy, a signal that economic growth is broadening. The U.K. has a services-based economy where consumer spending is crucial, much like the U.S. It helps that real wages (adjusted for inflation) are rising again, up 1.8% in the three months through January.[3]

Americans are Feeling Better About Retirement

Many stories about retirement tend to highlight Americans' overwhelming lack of preparedness. These stories still ring true today. But there are also some positive developments to highlight, which point to an improving retirement picture for many Americans. One study released this week from Vanguard illustrates these improvements. It found that Americans are saving into retirement accounts at record rates, with 43% of workers increasing the percentage of their paycheck saved into a 401(k) – compared to just 8% who decreased the percentage saved, and 2% who stopped altogether. One key factor that has been helping the retirement picture is automatic enrollment, which Vanguard says about 60% of its plans have. Of those plans, 60% of employees keep the deferral rate of 4% or higher. These trends, combined with a strong stock market in 2023, have led to average account balances at Vanguard increasing by 19% over the past year.[4]

[1] Wall Street Journal. March 12, 2024. https://www.wsj.com/economy/inflation-february-cpi-report-interest-rate-b827c0e7?mod=economy_lead_pos3

[2] Fred Economic Data. March 12, 2024. https://fred.stlouisfed.org/series/CPIAUCSL#

[3] Wall Street Journal. March 13, 2024. https://www.wsj.com/world/china/u-k-economy-returned-to-growth-in-january-73eaef0d?mod=djemMoneyBeat_us

[4] Yahoo Finance. March 13, 2024. https://finance.yahoo.com/news/americans-are-feeling-hopeful-about-retirement-according-to-two-new-reports-090003455.html

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