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Despite Wall Street's 2016 slide, don't 'head for the hills' just yet

The Dow Jones industrial average dropped 390.97 points Friday, eliminating the gains from a rally Thursday and then some. Stock trader Gregory Rowe worked at the New York Stock Exchange during Friday's sell-off.

By Mark Davis

Has Wall Street got you scared, or just worried?

In the first two weeks of the new year, according to various reports, we've witnessed stocks' worst start to a year "since 1999," "back to 1897," "since sliced bread," "in two decades," "since 1930," and finally, as of last Wednesday, to their worst start "on record."

A rally Thursday amounted to a day off for good behavior. Friday turned the screws again. A 390.97-point drop in the Dow Jones industrial average took back all of the rally and then some.

"Markets have to go through several stages and right now they're just holding their head and crying," Krishna Memani, chief investment officer at Oppenheimer Funds Inc., told Bloomberg.
Through Friday's downdraft, the Dow has shed 8.3 percent in just 10 trading days. The Standard & Poor's 500 index has dropped 8.0 percent and the Nasdaq 10.4 percent.

For a little calming perspective, historians need not dig very far into the past to find an even sharper and quicker market dive.

Last August, all three major stock market indexes suffered sharper declines in only eight trading days. The Dow fell 10 percent, the S&P 500 fell 10.4 percent and the Nasdaq dropped 10.5 percent. Each was large enough to register a market "correction," according to Wall Street's informal dictionary.

And the market fell then for pretty much the same reasons as now, China's weak economy and oil's steep price slide. The Federal Reserve has raised interest rates more recently, but last summer that was more a question of when, not whether, it would happen.

So why does the drop of the last two weeks feel so scary? What's the difference?

"You have a lot of emotion in the market" now, said Sandi Weaver, senior adviser at Petrovic Weaver Financial Services LLC in Prairie Village.

A survey by Bank of America Merrill Lynch even put numbers on it. Its Bull & Bear Index asks investors, on a scale of 1 to 10, to rate their outlook for stock prices. A 10 would be euphoric.

We're sitting at a collective 1.3, or at the "extreme bearish" end of the scale, roughly in the same neighborhood as August's panicked plunge.

This sharp slide in stocks has shaken investors' psyche not because it happened but because it happened again.

Last summer's swoon was overdue. Stocks had suffered only one correction in roughly four years. Now — and perhaps especially after the bright start of a new year — investors weren't ready to go through it again just five months later.

Thing is, now is a better gauge of what it's like to invest in stocks. Not the calm before August leading up to these back-to-back corrections.

"What we're seeing now is normal volatility," said Diane Dercher, adviser and economist at Wealth Management Advisors Inc. in Leawood. "People haven't been used to that lately."

At least for now, investors will need to learn to live with volatility.

OLD STORIES

There are reasons to worry.

The market's slide began with a report that China's manufacturing sector had slowed more than expected. Its stock market fell by 7 percent before officials halted trading.

All that happened before U.S. markets opened for the year, but prices here quickly followed the trend.

Finger pointing then shifted to China's decision to let the value of its currency drop relative to other countries' money. The move helps China's manufactured goods compete in world markets, an effort to shore up a slowing economic engine, but at the expense of rival exporting nations' economies.

China's stock market went through a second trading halt and government also put limits on selling by big stockholders.

Then there's oil.

Oil prices have plunged more than 70 percent from a high at $110 a barrel. Economist David Rosenberg called it a bubble, like the ones that wrecked technology stocks 15 years ago and housing markets eight years ago.

"As it stands, the burst of the oil bubble is the third most acute burst of any bubble in modern times," he wrote this week to clients of Gluskin Sheff + Associates Inc.

Oil prices — which fell to $29.42 Friday — have hit parts of the U.S. economy hard.

A Wolfe Research report offered that as many as one third of America's oil and gas producers could be heading toward bankruptcy or some kind of restructuring by the middle of next year, the Wall Street Journal reported. The financial newspaper also carried an opinion piece from one investment analyst who said low oil prices will cause a global economic recession.

Rosenberg sees no U.S. recession, oil-induced or otherwise.

Economists will agree, however, that cheaper energy overall provides a boost to America's economy. Lower gasoline prices, cheap home heating oil, and lower natural gas bills act like a tax cut, putting dollars in consumers' pockets. Airlines and car makers feel the benefits, too.

Those gains will accumulate over time. Meanwhile, the economic pain happens quickly.

New headlines on old stories, is how Bill Greiner sees the events seemingly shaking U.S. markets so much so early this year.

"I don't think there's a lot of difference" between now and last summer, said Greiner, chief investment strategist at Mariner Holdings in Leawood.

NOT SO FAST

Wall Street's worry over the oil patch and China is missing another big economic scene, namely Main Street. And it's doing better.

The economy added 292,000 jobs in December. Automakers reported record car sales for 2015. Housing activity has increased, and even manufacturing shows strength outside the beleaguered energy sector, said economist Chris Kuehl of Armada Corporate Intelligence.

Applications for credit are climbing as are sales, according to a survey of companies' credit managers that Kuehl does with the National Association of Credit Management. A survey of smaller manufacturers found plans to increase hiring and capital investment this year, he said.

Yes, fracking technology led to a boom in U.S. oil production and in the economies of states with large shale deposits. Job hunters flocked there.

"Now, they're all leaving North Dakota and buying cars," Kuehl said.

This isn't to say everything's rosy. But Kuehl said it puts the tailspin in stock prices into perspective.

Not long ago, Main Street was lagging as Wall Street rollicked. Now, it's more the other way around.

WHAT TO DO

This year's rocky debut is a strong reminder that investing involves risk. Maybe more risk than some stockholders realized.

Many retirees say they have turned to stocks out of frustration over the next-to-nothing interest rates they were getting from bank certificates of deposit. They've picked up dividend checks by risking a decline in what their stocks are worth.

Money managers say institutional investors, such as pensions and foundations, similarly have taken greater investment risks to boost sagging returns caused by low interest rates.

Advisers urge investors not to change investment choices based on the quick fall in stocks this month.

“Investors should ... take the opportunity to review their overall investment strategy, current holdings and make adjustments where it seems prudent,” Scott Anderson told clients of Bank of the West in a note Friday morning. “But, chances are, now is not the time to dump everything and head for the hills.”

A balanced strategy combines different kinds of investment such as stocks, bonds, low risk alternatives to cash, exposure to economies outside the United States and other venues.

Diversification within each category further reduces risks. Advisers routinely say to own stocks of many different companies in different industries, perhaps through mutual funds, to avoid the risk that one company or even one industry can falter, as energy companies are now.

And understand how much risk your plan involves.

“If the (plan’s) risk level is where you wanted it three weeks ago, I think you just sit through and ride this one out,” Weaver said. “You certainly don’t want to sell out at the bottom.”

Not that there’s any certainty that this is a bottom in U.S. stock prices. Stock values may have gotten better, but it likely is too early to start catching bargains.

Markets in Europe have taken a harder tumble, enough that Greiner says their slide is closer to its conclusion. In Japan, stocks had fallen by 15 percent through midweek. In Germany, 18 percent. And London, almost 16 percent.

Oil’s fall also seems long in the tooth. A bit of stability in the oil market could be a sign that shares of oil producers may have hit bottom. Once that comes, Greiner said he’ll be ready to look for bargains in the wreckage.

“I start to dig,” Greiner said.

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