Fight Or Flight?

S&P 500 Index vs. CBOE S&P 500 Volatility Index

1. The volatility/sell-off in the stock market over the past couple of days is understandable, in our opinion. The backdrop was ideal for profit taking.
2. Year-to-date through 6/17, the S&P 500 posted a total return of 16.07%, or an annualized pace of 38.25%. Since 1926, the average annual return on the index was 9.84%, according to Ibbotson Associates/Morningstar.
3. The Federal Reserve's slightly more optimistic tone about the state of the U.S. economy following its latest FOMC meeting (6/19) was bound to spook some investors, even if it stopped short of announcing an end to its easing initiatives.
4. We believe that some investors have mistakenly attributed all of the credit for the strong performance of stocks to the Federal Reserve's highly accommodating monetary policy and commitment to artificially low interest rates.
5. We encourage everyone to read Brian Wesbury's (Chief Economist at First Trust Advisors) research report from 6/19 titled "Fed Slightly More Optimistic" at www.ftportfolios.com for a different take.
6. Anxious investors should take comfort in knowing that the S&P 500 gained an average of 16.0% over two years the last four times the Fed started raising rates, according to Bloomberg Businessweek.
7. The chart paints a 20-year picture of the relationship between volatility (VIX Index) and the price movement of the S&P 500. Volatility, for the long-term investor, is little more than background noise.

Source: Bloomberg. Data is monthly from 5/31/93 through 5/31/13.

This chart is for illustrative purposes only and not indicative of any actual investment. The illustration excludes the effects of taxes and brokerage commissions or other expenses incurred when investing. Investors cannot invest directly in an index. Past performance is no guarantee of future results. The S&P 500 is a capitalization-weighted index comprised of 500 stocks used to measure large-cap U.S. stock market performance. The Chicago Board Options Exchange Volatility Index (VIX) reflects a market estimate of future volatility, based on the weighted average of the implied volatilities for a wide range of strikes.