Why the <u>VIX</u> Index Is Important to You and the Stock Market

By Bob Deitrick, ChFC
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As you are aware, the market this year has been tumultuous and we have discussed the reasons for this volatility which include:

- ***<u>Oil being absolutely crushed in early-to-mid-January dropping 24% in two weeks.</u>***
- ***<u>Instability in the Middle East and Europe with the ongoing Syrian refugee crisis.</u>***
- ***<u>China devaluing their currency for the second time in six months.</u>***

These geopolitical events are beyond our control in the U.S.; nonetheless, they influence our markets daily. Another reason for this volatility is that fear has controlled the markets. This has been witnessed, in real time, by something called <u>the VIX</u>. <u>The VIX index has been higher than normal all year peaking intraday at 30.9 on February 11th. That is until last week when it closed below 20 for the first time in 2016.</u>

The S&P VIX is an index which measures the daily volatility of stocks. Steven and I watch this index very closely for you on a daily and weekly basis. The VIX, which is calculated by The Chicago Board Options Exchange (CBOE), is often referred to as the "<u>fear index" as it is a measure of the stock market's expectation of volatility.</u> Since its introduction in 1993, we believe that the VIX is one of the most viable barometers of investor sentiment. The VIX is similar to a golf score. The higher the score – the worse things are and the more instability which exists in the market (or your golf game). The lower the VIX, the more consistent and predictable the markets are and the greater the probability is that we have a stable and appreciating market.

This year the VIX has been higher than normal; in fact the VIX has been above 20.0 since January 4th. That is until last week. Last Thursday, the VIX closed at 19.36 for the first time so we are beginning to see signs that fear in this market may be beginning to melt. <u>On Tuesday, March 1st, the VIX closed at 17.93.</u> We need to see the price of oil stabilize as well and there are signs this is beginning to take place <u>with oil (the WTI or West Texas Intermediate Crude Oil Index) closing at $34.39 today</u>. If oil stabilizes or continues to move up - the VIX should move downward. The VIX moving down, as it did today, bodes well for the stability of the financial markets.

Tom Lee, co-founder of FundStrat Global Advisors, acknowledged last week that "investor confidence was shattered over the past few weeks" to start the New Year. He believes that could pressure the markets in the short-term. We continue to believe with Lee that the 2016 turmoil is a growth scare and that this is not a recession. Stocks started the month of March today with the best start to any month we have had in three years after a second-straight week of gains last week - quite a different story from January's dismal start. Last Thursday, the Dow and S&P 500 indices pulled out of correction territory and today the S&P closed at 1978.35 - well above its 50-day moving average of 1950

illustrating some strength to this market. Here is where the market closed today on March the 1st:

DJIA	***16865.08***	***+348.58***	***+2.11%***
NASDAQ	***4689.60***	***+131.65***	***+2.89%***
S&P 500	***1978.35***	***+46.12***	***+2.39%***
OIL	***34.39***	***0.59***	***+1.75%***

Mr. Lee also downplayed concerns about the possibility of a global recession saying that "major market internals like transports and small-caps are not pointing to a recession. If we were actually seeing worsening economic conditions, these indices should be on a death spiral." Lee also noted, "These indices have actually been improving over the last few weeks. The American consumer, who makes up 70% of our economy, is positive."

Anecdotally, when shopping at the Polaris Costco on Valentine's Day weekend, I found it was more crowded than at Christmastime. When I passed the new BW-3's in Westerville for its grand opening last week, there was not a single parking spot to be found. If we are entering a recession, someone needs to tell the American consumer because they aren't aware of it. In other words, things are not as bad as some make them out to be, so please consider the source when listening to commentary and political rhetoric.

Last week, St. Louis Fed President Jim Bullard stated he was not concerned about a world recession. Despite investor concern about a 2016 market downtown - after 6 years of strong returns, Bullard told CNBC that "U.S. equities are better priced at their current levels. If we had continued to go up, that would have created an asset pricing bubble. "We are now much closer to fair value today" according to Bullard.

Bullard attributed this year's market turmoil to traders factoring in all four interest rate hikes in 2016 taking place at once. "It was as if the December hike was 125 basis points instead of 25 basis points", he said, "citing concern about Greenspan's 17-straight hikes in the 2004 - 2006 cycle". Bullard conceded that four interest rate hikes this year is unlikely.

"We are growing at a lower trend growth rate," he acknowledged. We at Polaris Financial view this is a binary period of transition - one that marks we are closing in on a peak to this market expansion of 7+ years. But we are not in the negative spiral which many pundits predicted in January. If oil shows greater stability and the VIX declines into the low-to-mid-teens (12 to 15), a nice rally to this market could materialize as we saw today. Having said that, we are close to the peak in this cycle; therefore, being more selective in stocks and sectors and moving to more defensive positions will be important.

Please stop by the office or feel free to call us at 614.901.3400 with any questions. We will be having two Spring Market Update Luncheons in April on Tuesday the 19th at Brio and Friday the 22nd at Eddie Merlots. We encourage you to attend and you are encouraged to bring your spouse, a friend, co-worker or a neighbor as well. We wish you a terrific week!