MOMMAERTS MAHANEY
FINANCIAL SERVICES, INC
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989 W Washington St., Suite # 101
Marquette, MI 49855
(906) 226-8711
www.mommaerts-mahaney.com

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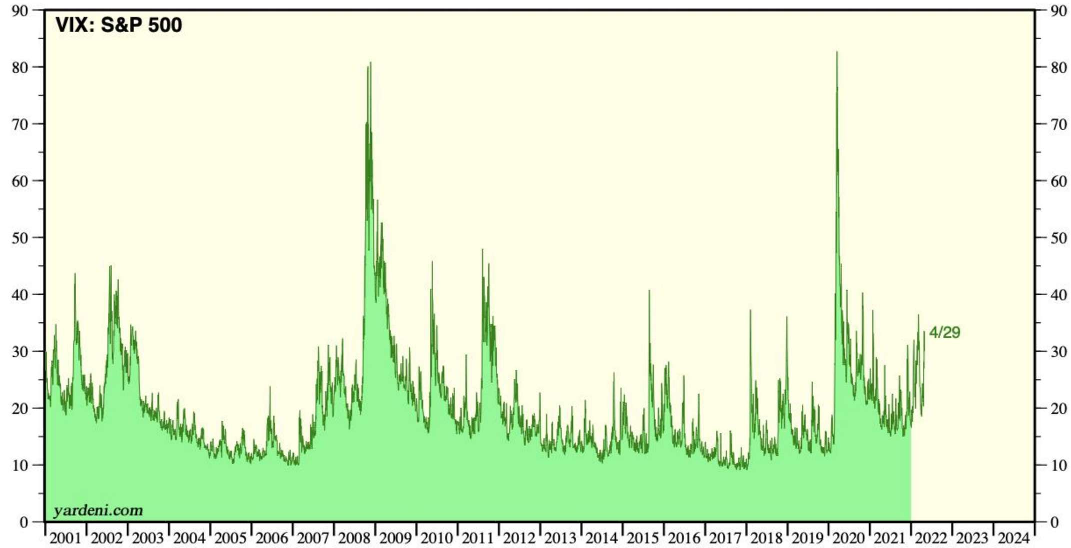
Quick Thought and Observation

Jon C. Mommaerts	Robert Kea	J. Matthew Tuccini	Jason J. Rolling
Certified Financial Planner®	Chartered Financial Analyst	Certified Financial Planner®	Financial Advisor

During turbulent markets, we believe it is important to communicate more frequently. We also recognize the need to balance frequency vs. over-communicating, or more specifically, annoying you with too many emails. We've recently sent some rather *thorough* (you might argue *long* is a more appropriate adjective) and detailed notes regarding economics and our market outlook. We end each note with a reminder that you can reach out anytime should you want us to expand on our thoughts. Replies are generally on the lighter side. This means we are either incredibly efficient at proactively identifying and explaining your topics of concern, or you are dozing off before reaching our valediction.

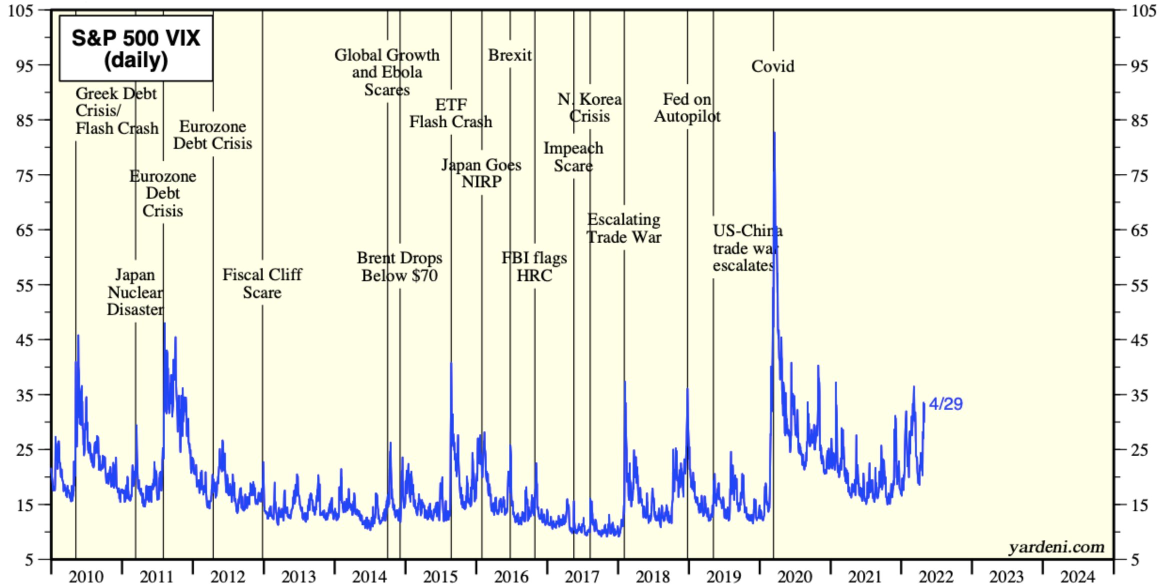
Markets are likely to remain turbulent for a while, and we continue to believe that frequent communication is an important investment tool during volatile periods. Until things calm down a bit, we will balance our desire to communicate more frequently with the promise of brevity. This allows us to communicate about rapidly changing economic and market conditions without overly burdening the reader. Here is a quick thought;

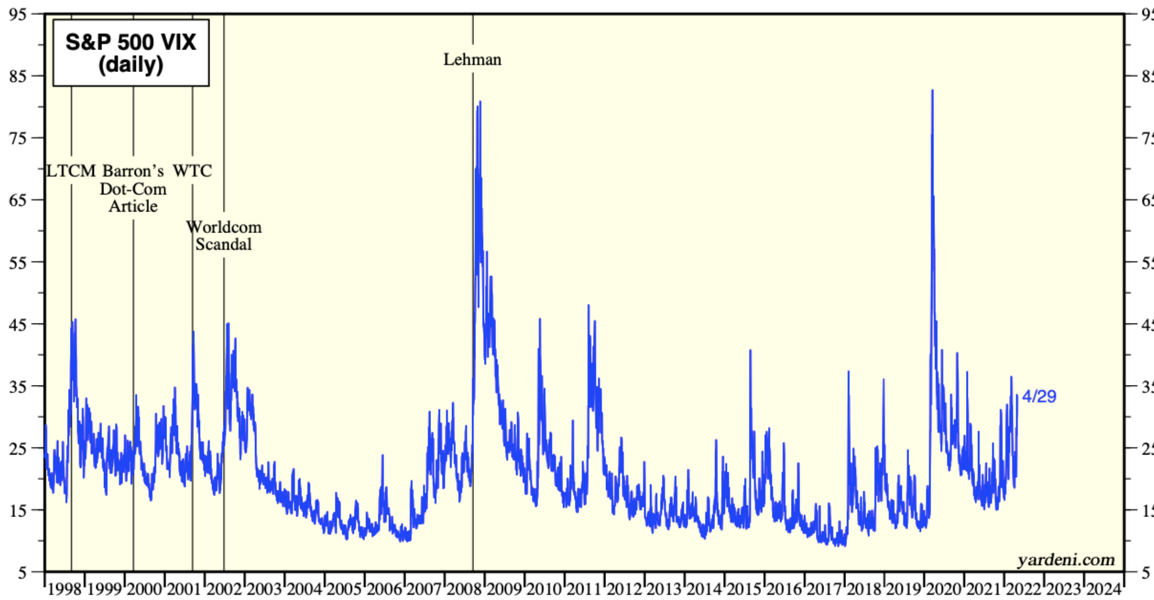
Several of you have written or asked why markets are so volatile. "What makes stocks go up 2% in the morning and then down 4% in the afternoon?" It's a question we struggle to give a definitive answer to. There is not a universally agreed-upon reason. There are lots of different opinions but none are provable. The reason for higher volatility is likely some combination of these various opinions. Let's start by looking at where current volatility levels are compared to historical volatility levels.



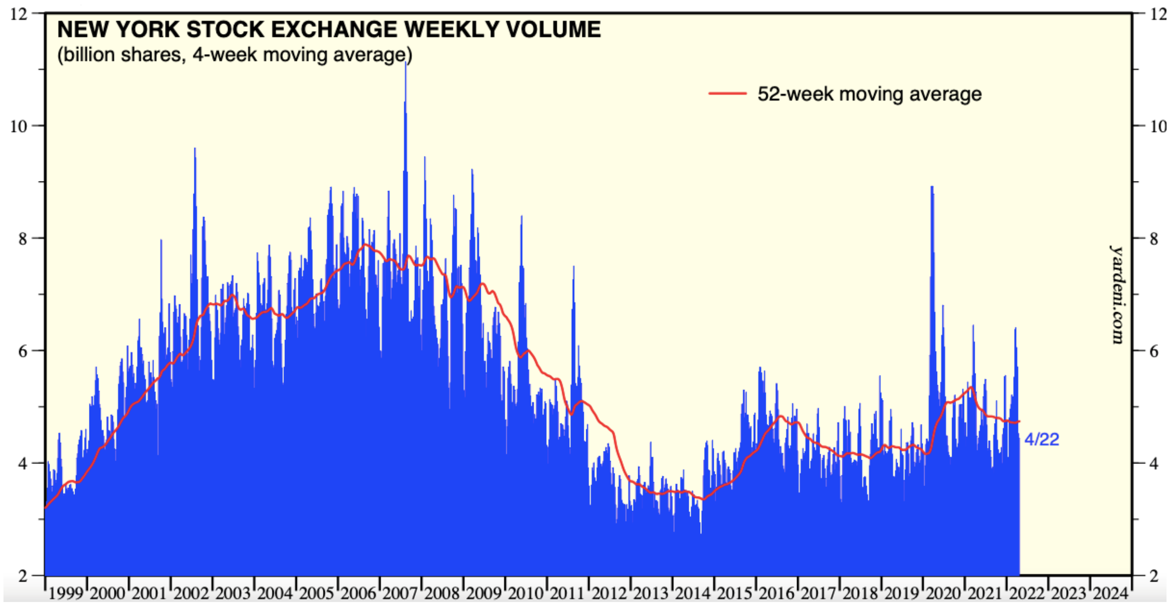
The perception that we are in a period of unusually high volatility is not completely accurate. Current volatility is higher than average volatility, but periodic volatility is not materially higher than historical volatility. The VIX Index measures volatility in the stock market. The level of volatility we are experiencing over the last few months is higher than long-term average volatility, however, volatility over the last few years is lower than long-term average volatility. When viewed as a period of time, periodic volatility is no higher today than it has been in previous decades. Believe it or not, this is somewhat normal.

Most humans, not just investors, are prone to *recency bias.* We tend to believe that the times we live in are unique within the context of history. It's why investors overreact to news cycles. It's why we may think today's world has become more dangerous despite an overwhelming amount of data indicating we are safer now than historically. It's why prognosticators consistently overestimate the long-term impact of geopolitical events. Wars and elections seldom achieve the dire consequences we are promised. A look at volatility storms over the last couple of decades is a timely reminder.





The question does remain though, what causes markets to fluctuate so dramatically on an intraday basis, even when there is no material news flow? Many blame the internet, day traders, and program trading. It's probably as reasonable as any other explanation, but we would add another reason. The first half of our investment careers were pre-internet. Nevertheless, there was plenty of volatility. So it's not entirely fair to blame the internet. What moved markets pre-internet were investment banks. They controlled the trading floors. When Goldman Sachs or Morgan Stanley put out an opinion, stock markets would instantaneously move to reflect this opinion. All trades had to run through a brokerage of some sort in order to make it to the trading floor. It was much easier to track who was moving markets. Of course, today, everything is electronic. Trades are executed over phones and laptops, it's not entirely clear who is trading. We think the following is an interesting observation regarding volatility. Exchange-traded volume has dropped considerably over the last decade. Less volume means less liquidity and more volatility. This lower volume is likely a reflection of an SEC initiative to change how financial institutions charged clients. Prior to the internet, clients were charged commissions. Stockbrokers made money by charging clients a commission on trades. The more trades, the more money they made. The SEC has worked to eliminate commission-based fees in favor of flat fees. Commission-based fees are becoming increasingly rare. The SEC's reasoning for initiating this change was to remove the incentive for brokers to "churn" accounts to create commissions. It's a viable reason and the SEC has been successful in accomplishing this goal. We'd suggest an unintended secondary effect was they also created lower-exchange volume, which decreases liquidity and increases volatility.



It's quite hard to isolate the root cause of volatility. ETFs likely play some role too. Many ETFs trade baskets of the same stocks. This is an operational necessity for ETFs to track indices. We wish we could give a more definitive answer regarding the causes of volatility, but we can't. Hopefully, this offers some clarification on this issue.

Embrace the Volatility,

The Mommaerts Mahaney Team

Jon C Mommaerts, CFP®: Jon is a Principal of Mommaerts Mahaney Financial Services, Inc. He has over 30 years of experience working with professionals and those about to retire. He is a member of the Financial Planning Association, as well as a member of the Preferred Financial Advisors.

J. Matthew Tuccini, CFP®: Matt has over 17 years of experience working in the financial services industry with vast experience in retirement planning, tax strategies, and financial planning.

Robert Kea, CFA: Bob has over 30 years of experience in portfolio management. He was a founding member and Co-Head on Putnam's Asset Allocation Group, which managed $12Bn in both retail and institutional assets.

Jason Rolling, Financial Advisor: Jason has been in the financial services industry for the past 15 years. His financial experience includes retail banking, consumer & commercial lending, bank management at the local, regional and SVP level, wealth management, and financial planning.

Mommaerts Mahaney Financial Services, Inc. provides advisory services through ERTS Wealth Advisors, LLC, a registered investment advisor.

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