

Stock Market Corrections: Unsettling But Not Unusual

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With U.S. stocks falling more than 10% from their April peak, the market has officially entered correction territory for the first time since the cyclical bull market began in March 2009. The Greek debt crisis and flagging confidence in Europe more generally have been the catalysts that punctured investor confidence. Europe is staring at the prospect of either further financial instability or at best a period of severe fiscal austerity that will likely serve to depress economic growth. Either way, Europe's turn for the worse has caused most analysts to ratchet down their expectations for global growth in 2010.

Outside Europe there is also plenty to worry about. The developing world has grown at a fast clip, but it is now facing rising inflation and is reining in stimulus policies. China, India and Brazil all have moved to tighten lending or raise interest rates. While U.S. policymakers are not expected to raise rates anytime soon, there have been plenty of unsettling headlines, from uncertainty about the impact of the crude-oil spill in the Gulf of Mexico to the details of financial sector reform legislation.

Perspective on recent correction

Whether this confluence of events will continue to drive the market lower in the near term is impossible to know, but there are two things that investors may want to keep in mind.

First, the global economy went into this latest period of financial market volatility in much better shape than in early 2009. The strength of the economic recovery during the past year, particularly in the United States and Asia, has continually surprised on the upside. While that momentum will undoubtedly slow, it does not automatically mean a reversal back to global

Historical Stock Market Corrections
(1928-2010)

	All Corrections		First Corrections in Bull Markets	
	Magnitude of Correction	Length of Correction (Days)	Time to 1st Correction (Years)	Gain Before 1st Correction
April 23 - May 20, 2010 (recent correction)	-12%	27	1.2	80%
Median	-12%	54	1.5	57%
Maximum	-19%	252	7.0	233%
Minimum	-10%	3	0.3	21%

Bull and bear markets: a 20% or more increase (bull) or decrease (bear) in the S&P 500® Index. Corrections: a decrease of 10% or more that does not exceed 20%. "Length of Correction" refers to the amount of time (calendar days) between the index peak and trough of the correction. "First Corrections in Bull Markets" only includes data to the first correction in a bull market since the end of the prior bear market. "Time to 1st Correction" refers to length of time after a bear market ends to first correction in new bull market. "Gain Before 1st Correction" defined as S&P 500 index price return from end of prior bear market to the peak established at the start of the correction. All references to the stock market represented by the S&P 500 Index. All returns are calculated using closing price return data from 1/3/1928 - 5/20/2010. Source: Bloomberg, FMRCo. (MARE) as of 5/20/2010.

recession [see MARE's May U.S. Economic Update: *Payroll Gains Offer Hope Recovery is Not Jobless*].

Second, while the stock market correction so far has been abrupt and painful, it actually has been relatively typical of what might have been expected to happen given historical patterns. Consider:

Timing of correction was typical

It's been about 14 months since the current bull market began on March 9, 2009, which is in the neighborhood of the average length of time that has passed from the start of prior bull markets to a first correction (17 months, see table).

Early bull market's gains were above average

The stock market gained 80% before the recent correction. Historically, the first correction in a new bull market has come after average gains of 57%,

implying the current bull market was overdue for a correction on a price appreciation basis.

Correction pace fairly quick

The main factor that has differentiated this recent correction is that it has taken place at a fairly swift pace compared to history. It took 27 days for the market to surpass the 10% decline threshold, which is half the time it's historically taken on average for a correction to occur (54 days).

Investment implications

Since 1926, there have been 20 stock market corrections during bull markets, meaning 20 times the market declined 10% but did not subsequently fall into bear market territory. Whether the market recovers again from here and avoids a bear market remains to be seen, but at the very least the more surprising development based on historical patterns would have been a continued bull market rally without a 10% pause. ■

Historical Stock Market Corrections (1928-2010)

Start	Length of Correction (Days)	Time to 1st Correction After Bear Market Ends (Years)	Gain Before 1st Correction
23-Apr-10	27	1.2	80%
28-Nov-02	103	0.4	21%
16-Jul-99	91	N/A	N/A
17-Jul-98	45	N/A	N/A
7-Oct-97	20	7.0	233%
9-Oct-89	113	2.2	61%
10-Oct-83	249	1.8	69%
13-Feb-80	43	N/A	N/A
5-Oct-79	33	N/A	N/A
12-Sep-78	63	0.7	23%
28-Apr-71	209	1.5	51%
25-Sep-67	162	1.4	57%
3-Aug-59	218	2.4	56%
23-Sep-55	18	N/A	N/A
5-Jan-53	252	N/A	N/A
12-Jun-50	35	1.1	43%
5-Feb-46	21	N/A	N/A
14-Jul-43	138	1.6	69%
6-Apr-36	23	N/A	N/A
12-Jun-33	3	0.3	97%
14-May-28	36	N/A	N/A

Total # of Bull Market Years Since 1928 (out of 82)	Total # of Corrections	Frequency of Corrections
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57	20	one every 2.8 years
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Bull markets can have multiple corrections: **brown shaded areas** on left table represent first corrections in a bull market; **non-shaded areas (N/A)** on left table represent corrections that took place after the initial correction in a bull market; **blue shaded area** on left table represents most recent correction. See prior page for bull market, bear market, and correction definitions. "Gain Before 1st Correction" defined as S&P 500 index price return from end of prior bear market to the peak established at the start of the correction. Number of bull years (above) is total years from 1928 to 2010, excluding bear market periods. All references to the stock market represented by the S&P 500 Index. All returns are calculated using closing price return data from 1/3/1928 - 5/20/2010. Source: Bloomberg, FMRCo. (MARE) as of 5/20/2010.

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All references to stocks or stock market performance in this article represented by Standard & Poor's 500SM Index price returns.

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