PWMG Perspective: Planning, Pandemic, Putin and Prices – Fall 2022

9/7/2022

Dear Clients, Family, and Friends,

We hope that you enjoyed a fabulous summer. From our conversations with many of you, it has been a wonderful time to reconnect with family and friends and to travel once again. Given the market and economic volatility this summer, we have been working hard to reach out, review plans, rebalance portfolios and harvest tax losses where appropriate. In this newsletter, we will update you on our current perspective and we invite you, as always, to call or email us if you have any questions, concerns or family/business updates.

Market perspective

Both the bond market and the stock market have been quite volatile this year thanks to a toxic mix of news flow. The S&P 500 Index fell 23% thru mid-June, while the NASDAQ Composite Index fell 33%. The market rallied to recoup about 50% of those losses by mid-August, but has recently begun a retest. Meanwhile, a 10 Year US Treasury Bond now yields almost 3.4%, up from 1.3% a year ago.

In large part, we believe this price action is due to:

1) The **pandemic** is still greatly impacting our health and supply chains worldwide. When the pandemic first hit in 2020, the economy and the markets froze. Very fortunately, our prediction in our March 18, 2020 newsletter came to fruition. We wrote: *"our best and brightest scientists, physicians, technologists and corporations are singularly focused on both treating and, ultimately, eradicating the virus. We have no doubt that they will be successful. When they are, and when Americans can get back to work, we would expect a very rapid recovery in the economy and the markets."* More recently, government monetary and fiscal stimulus has helped create excess demand while a challenged supply chain is still curtailing supplies. This has contributed to a spike in inflation. Monetary stimulus is now, prudently, being withdrawn.
2) **Putin** and his attack on Ukraine have unsettled the world order, as well as energy and food supplies. This remains a disturbing and unpredictable challenge.
3) **Prices** of energy, food and housing have brought on inflation the likes of which we have not seen in many years. The Consumer Price Index hit a 41 year high at 9.1% in June. As a result, global monetary authorities, especially the US Federal Reserve Board, have made it their priority to fight inflation. We very much support their efforts.
4) All of the above items have combined to create the lowest Consumer Sentiment reading since the University of Michigan Consumer Sentiment survey was started in the 1960s.

An interesting side note is that, if one were to look back to the eight prior lowest readings of the Consumer Sentiment Survey since 1973, the S&P 500 Index was +24% on average over the following 12 months. Conversely, if you were to look back to the eight times when consumer sentiment was highest, the average return for the following 12 months was only +4%. The moral of that story is what we all know to be true about investing: that it is generally better to buy low when others are fearful than to wait until feeling that all is well.

Will we have a recession?

Recessions are a natural part of the economic cycle. Many economists believe that we are already in (or are about to be in) a recession. While we are closely monitoring the data, we do not believe that a recession, even if it occurs, will be particularly severe in terms of either length or depth. The reasons for this are as follows:

1) Consumer and corporate balance sheets are quite healthy.
2) There is a lot of cash around.
3) Demand should stay strong as Governments, schools, businesses and consumers continue to resurface from COVID lockdowns.
4) Supply chains are already improving and will get better still.
5) Interest rates normalizing is a sign that the world economies are healing.

Are interest rates really that high?

Our view, at The Prentis Wealth Management Group, is that a more normal (higher) interest rate environment should be welcomed. Zero-percent interest rates of the past years were the exception and are no longer warranted. It is important that the world economies heal and normalize without the emergency-level stimulus provided to support people and businesses through the initial phases of the pandemic. We feel it is also very important that the US Federal Reserve maintain a focus on price stability. Inflation is an illness that can harm us all.

A quote from one of our favorite economists, Dr. Edward Yardeni, comes to mind: *"Wouldn't it be swell if the Fed truly normalized monetary policy and we found that the economy can do just fine with a federal funds rate of 3.00%-4.00%? It has happened before, and it can happen again."*

Speaking of cash

There is a lot of cash around. We would like to share the following observation from Jim Paulsen at the Leuthold Group (8/31/22):

“Consumers always raise cash when they’re nervous. But the amount of dry powder accumulated alongside the pandemic is one for the record books … Still, never in the post-war era have household rainy-day funds exploded as fast and dramatically as the last couple of years. Cash holdings as a percent of debt have ballooned to 25%—the most since 1970!” “This cash hoard may meaningfully temper the severity of a looming recession. In our view, it is more likely that, as inflation moderates and confidence increases (which is already occurring), the redeployment of dry powder—as animal spirits again emerge—could revive economic growth next year. Renewed strength in consumer spending could also improve company profitability and brighten CEO outlooks.”

The rise in interest rates presents an opportunity. We suggest that you review your idle cash balances. The average interest rate on bank savings and checking accounts is less than .25%. Meanwhile, money market funds are yielding over 2.3% and US Treasuries in most maturities yield over 3.2%

When interest rates were near 0%, what you did with your cash balances did not matter that much. Now, it pays to review and become more resourceful. Please review your bank balances and give us a call. We can help get your money put to work safely, efficiently and cost-effectively.

Is your estate plan all set? Now, let’s plan on living a happy, healthy and long life!!

Much of our focus as financial advisors is making certain that our clients have a strong plan. That plan should include contingencies for when you are alive, when you pass away and, equally important, provide for you if you have any sort of incapacity (physical or mental).

The most obvious and first goal, for many of us, is to gain comfort that we have enough. Do we have enough income to maintain our desired lifestyle throughout our lives? Do we have enough assets to pass along to our heirs and/or to fulfill our philanthropic goals? As we hope our clients have come to realize, these plans should, and do, assume that the economy and markets will fluctuate. Neither a recession nor market volatility should shake our plans out of balance. Our focus is on the horizon, not intraday charts.

Don’t forget!

While it is a challenging topic, we would like to take a moment to remind all of our readers (which include our clients, friends, family, as well as their accountants and lawyers), to think about and solidify their plans in case of any sort of incapacity. One of the most difficult topics we encounter is around failing mental capacity. This can happen at any age and is very rarely predictable. For some, it is slow and recognizable. For others, it comes out of the blue and, to those inflicted, they may not even be aware of it. Unfortunately, we have witnessed this impact many of the families we have helped over the years. As such, we implore you to check your plans, talk with your families and speak with us. Please do it now, while you are capable and it is front of mind. Whether it is for yourself, your parents or your children, let's make certain that you (they) have someone who can step in manage your (their) affairs. Do you (they) have a Durable Power of Attorney (POA) and Healthcare Proxy? Does the POA know where the document is? Also, please make sure that we know who to contact in case you (they) become incapacitated. Yes, this is a grim topic and, for many, it is a difficult conversation to have. We are here for you. Please let us know if you have any questions or if you would like our assistance in facilitating a family conversation.

Focusing forward

Recessions are part of a normal economic cycle. Great managements and strong businesses capitalize on growing throughout expected and unexpected economic fluctuations. Likewise, as portfolio managers, we are focused on having the flexibility to be opportunistic in volatile market environments. Whether it is with cash, bonds or equities - our goal is to take a balanced, risk-adjusted, tax-efficient approach to growing our client's wealth over many market cycles. We continue to be optimistic about the future and stand ready to help our clients navigate uncertainty, no matter how market conditions evolve moving forward.

Focus forward, stay calm, and carry on.

Peter, Mike, Stuart, Andrew, Joe and Edita

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