Email Body 6-21-2022

**What is Happening in the Economy and Where Do We Go From Here?**

It is June and summer is all around. Schools are out and the beaches here in San Diego are full. Anecdotally, traffic is heavy, it is difficult to get a restaurant reservation within 3-4 days of your desired date and time and plenty of people are out shopping in all the venues. I went to a Padres baseball game a couple of weeks ago (e.g., against the Cubs) and Petco Park had 40,000+ attendees. Cub’s fans do not travel although the Padres are doing well for the moment. Sure does not look like a recession, even if some polls suggest a plurality of people think it is.

THE ECONOMY

The broad stock markets entered bear territory last week as the Federal Reserve (the Fed) met and delivered a 0.75% rate increase when a 0.50% increase was expected. The Fed was responding to an elevated inflation report earlier in the week which created significant market volatility.

Inflation has not moderated as much as expected in the first five months of the year. A combination of rising energy costs, continuing production disruptions the Covid shutdowns and the war in Ukraine have all significantly contributed to this issue. The Fed’s action clearly indicates that its goal is to reduce demand pressure while simultaneously trying to encourage employers to reduce hiring and raising wages to prevent a wage-price spiral.

Core inflation has likely peaked meaning goods prices are already starting to decline, although rising energy and food prices may make the next several months feel like a plateau rather than a decline. Markets have priced in significantly more tightening from the Fed although moderating as the year progresses, and the Fed itself expects short-term rates to rise to 3.25% to 3.50% by the end of this year. Between now and the end of the year I expect data on jobs openings, wage growth and other measures of price inflation to slow and provide the Fed with ammunition to reduce rate hike expectations. May jobs reports showed strong jobs creation, an expanding labor force and moderating wage growth. Retail spending in May absent autos, increased in line with expectations. Post-WWII, a recession has never occurred without rising unemployment and falling aggregate demand. Neither of which we have at this moment in time.

Median forecasts for GDP in 2022 are now at 1.7% which is in line with my previous statements that we are likely heading back to normalized growth patterns of 1.50% to 2.00%, annualized. Recession risk remains elevated and largely depending on inflation dynamics and whether the Fed must raise rates significantly beyond the projected 3.25%-3.50% range. Given the current economic factors I would expect any recession, should it develop, to be relatively mild compared to what we experienced in 2008-2009.

THE MARKETS

As I am sure you are aware, market conditions have not been friendly to diversified portfolios in 2022. Both stocks and bonds have declined significantly enough to erase most of the gains experienced in 2021. The good news is that the market decline in stocks has moved valuation levels close to or below 25-year averages. This suggests that we may be through the worst of the decline if no recession develops or if it is mild.

Since 1950 there have been eleven bear markets (i.e. more than 20% decline from the peak) lasting from as short as one month to two and one-half years. This time period covers from peak to trough to surpassing the previous peak. One other interesting tidbit is that post-WWII, there have been sixteen (16) times the Fed has hiked interest rates. In the one-, two-, and three-year periods following the start or the hikes, the S&P 500 has risen over eighty percent (80%) of the time. With respect to the two-, and three-year periods, none of the declines when they did occur, were greater than 5.1%.

I continue to recommend that for long-term oriented investments, maintain your current allocation strategies if your risk profiles and time horizons remain consistent and not subject to expected changing circumstances.

As I have previously said, make sure that funds you know you will need in the short-term are safe to relatively safe from volatility and that your long-term oriented investments are well diversified and subject to risk and volatility levels you are able to be comfortable with. If you have any questions or concerns about these things, please call me to discuss them further.

I have attached a brief commentary on the current situation by Brad McMillan. Brad is managing principal and chief investment officer at Commonwealth Financial Network®, where he chairs the Investment committee and is the primary spokesperson for the firm’s investment divisions. Check out the attachment to this email.

I am always available to you via phone, zoom conference or in person. I look forward to talking with you over the next few weeks. If you have any questions or if we can be of any help, please do not hesitate to contact Linda or me.

*Certain sections of this commentary contain forward-looking statements that are based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. Past performance is not indicative of future results.*

Christopher L. Phelps, CPA/PFS, CFP®, AIF®

Principal

Phone (858) 485-1919   Fax (858) 487-0355   [chrisp@financiallifeconcepts.com](mailto:chrisp@financiallifeconcepts.com)



16935 W. Bernardo Drive, Ste. 228, San Diego, CA 92127  [www.financiallifeconcepts.com](file:///C:\Users\chrisp_mhbfc.com\Desktop\Restore\Docs\Mass%20Client%20E-Mails\www.financiallifeconcepts.com)