Email Body 8/1/2023

The Economy, the Markets, and the Federal Reserve

Summer is in full swing complete with elevated temperatures and the sound of air conditioner compressors running full tilt. I am back from the Grand Tetons where Sheri and I had a close encounter with a brown bear (aka Grizzly bear). Fortunately, we beat a quick (although controlled) retreat down a path, across a foot bridge and off the trail and the bear, after coming across the bridge, went a different direction. Next time we get together, if you are interested, I have a video of the bear following us taken by some paddle boarders. Glad I did not have to use the bear spray.

The markets have been moving up over the last month or so reflecting positive trends in a number of economic, inflation and, employment data points. However, the big news last week was the Federal Reserve deciding to increase its fed funds interest rate another 0.25%. It did so while acknowledging that inflation was declining, however, it was not yet close enough to its 2.0% target. Fed watchers parsed Jerome Powell's after-meeting commentary noting that the Fed appears to anticipate one more rate hike this year, but that it depends on future inflation data.

Most economist and analysts I follow believe that absent a reversal of inflation trends (i.e., downward) that the Fed is likely done raising interest rates this year. My view is that the financial markets have already priced in the possibility of another rate hike. Instead, they are focused on the better-than-expected sales and earnings gains for the second quarter currently being reported by publicly traded companies. It is also reflecting the fact that second quarter GDP came in at 2.4% annualized growth and that a number of economic indicators came in better than expected over the last four weeks.

The bottom line is that the economy appears to be gaining strength and both the Federal Reserve and the markets seem to agree that the economy will likely achieve a "soft landing" (e.g., no recession) despite the Fed hiking interest rates to their highest level in twenty years. This means that gains incurred year to date by your portfolio(s) should hold going forward but note that there will still be volatility depending on the news of the day and depending on whether the Fed decides to continue raising interest rates in the near future.

Remember this, over the long-term the economy has historically grown most years with recessions occurring periodically for assorted reasons (i.e., over-valuation, over leverage, etc.). The markets reflect this growth by increasing in value three out of four years for the last forty-three calendar years. There are no guarantees this trend continues but it does show the relationship between the economy and the equity markets.

This is clearly an environment for long-term investors, and I strongly recommend putting as much risk into your portfolio as your goals and ability to tolerate volatility will allow. As an aside, one of the benefits of the Federal Reserve raising interest rates is that money market and short-term CD rates are near or slightly over 5%. If you have excess cash sitting around in a bank or credit union, check with those institutions to ensure that you are getting the best rate. If you are earning significantly below 5%, contact me to see what may be possible.

Please find attached to this email a short missive penned by Brad McMillan, Commonwealths' Chief Investment Officer. In it he provides his thoughts on the current state of the economy and the markets. I encourage you to read it to get another perspective.

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.

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