CORBETT ROAD
WEALTH MANAGEMENT

MACRO MUSINGS

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Charting the Course 2022

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SUMMARY

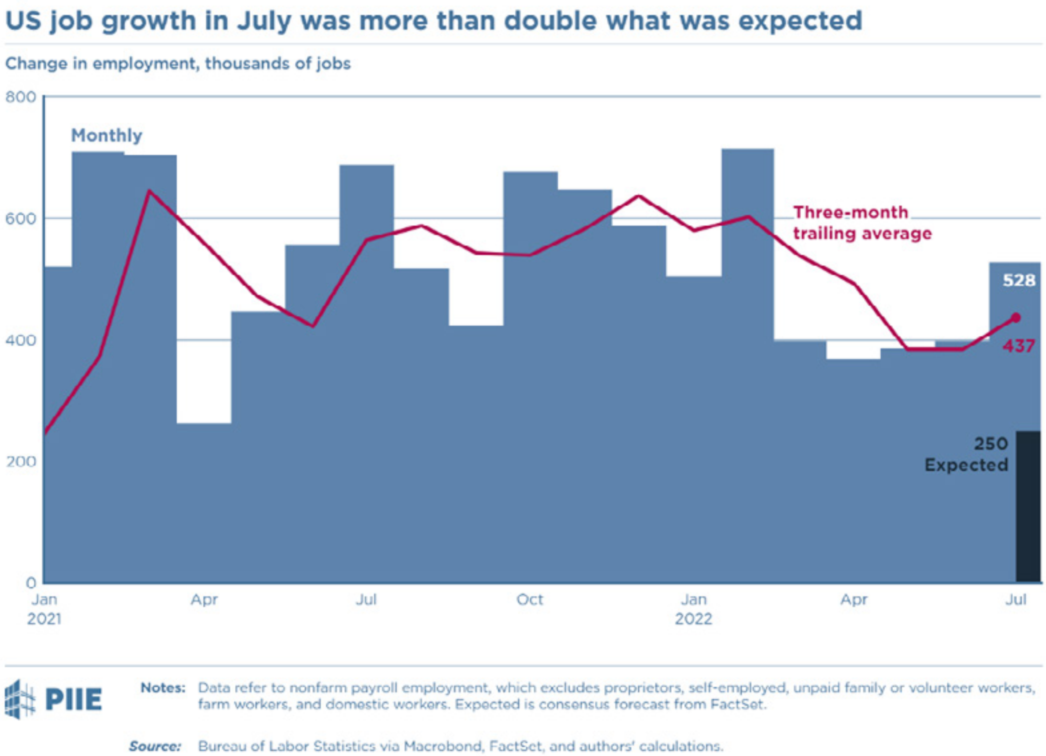
- The **macro**cast™ score suggests the probability of a recessionary bear market has increased, and the defensive position of **micro**cast™ indicates market conditions remain volatile. The combination of both risk models suggests we remain in a challenging market environment, which we expect to persist through the second half of the year.
- Every August, we "Chart the Course" by reviewing a series of charts that illustrate key trends in the economy and markets. The data depicted in these charts is consistent with what we see in **macro**cast™. We hope you enjoy these, and we will resume publication of our regular commentary in September.

CHARTING THE COURSE: **macro**cast™

macrocast™ ***remains negative.*** The negative score reflects the elevated recession risks, which implies a higher probability of a sustained bear market.

CHARTING THE COURSE: **THE ECONOMY**

Within labor markets, job growth remains strong. Last week's employment report exceeded expectations. The US added 528K jobs in July, and the unemployment rate edged down to 3.5%, a 50 year low (Chart from Peterson Institute):



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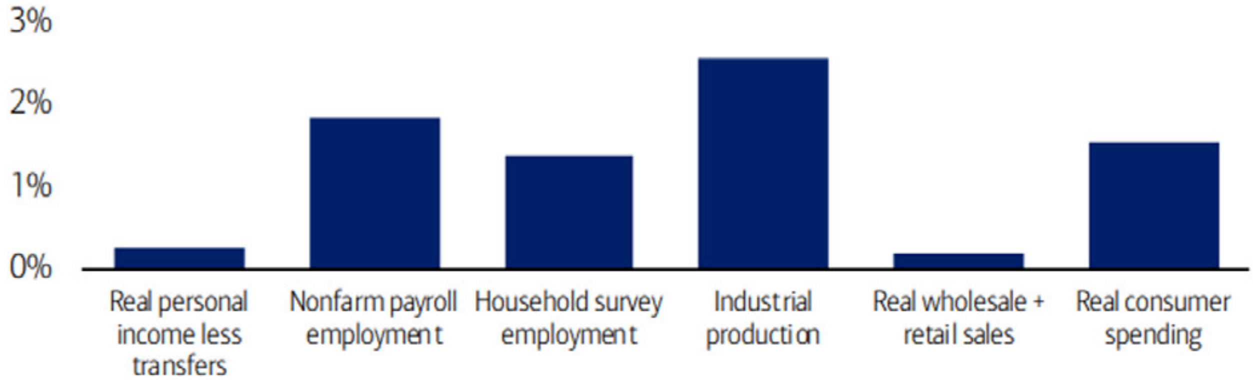
But initial claims are beginning to rise, suggesting slower job growth in the months ahead. Initial claims for unemployment bottomed earlier this year and have since risen back to levels seen last fall. Although still low on an absolute basis, claims are steadily rising. If this trend continues, we believe a higher unemployment rate is likely as we head into 2023.

The factors officially used to determine a recession were all positive in the first half of the year. The National Bureau of Economic Research (NBER) looks at several variables, aside from GDP, to determine whether a recession has commenced. Although we've had two consecutive quarters of negative GDP growth, the six factors NBER considers were all positive in the first half of 2022, suggesting the economy was not in a recession through June (from Bank of America):

Exhibit 1: Variables used by the NBER in making its recession determination (% chg. From Dec '21)
All six variables used by the NBER to make its recession determination have expanded since Dec '21



Source: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve Board, Haver Analytics. Latest month difers by indicator
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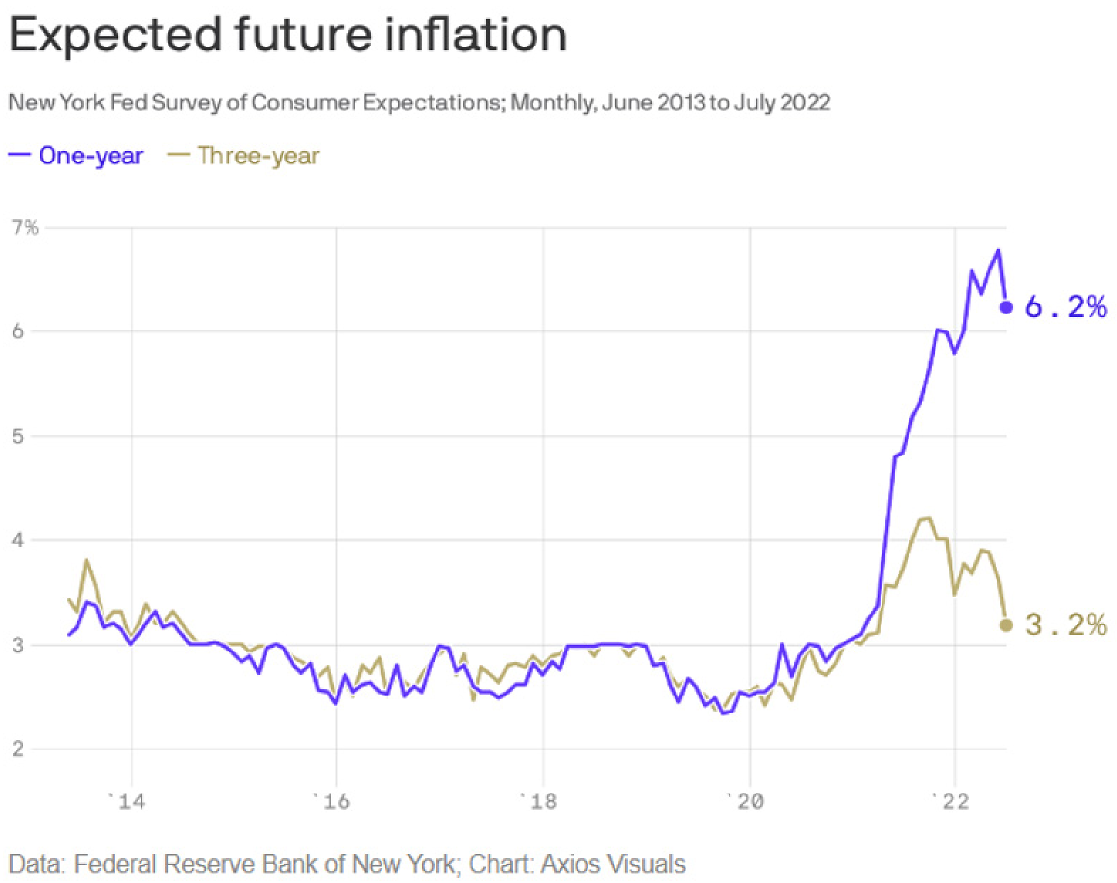
CHARTING THE COURSE: **INFLATION**

Inflation expectations for the next year remain high, but consumers don't think it will last. Inflation expectations are important. If they remain elevated, they could put upward pressure on actual inflation by creating a vicious cycle where consumers expecting higher inflation adjust their spending patterns to get ahead of higher prices. Companies, reacting to the increase in demand, can then raise prices, leading inflation expectations to become a self-fulfilling prophecy.

While one-year inflation expectations remain elevated, the three-year figure suggests consumers do not expect inflation to become entrenched over the longer-term (Chart from Axios):



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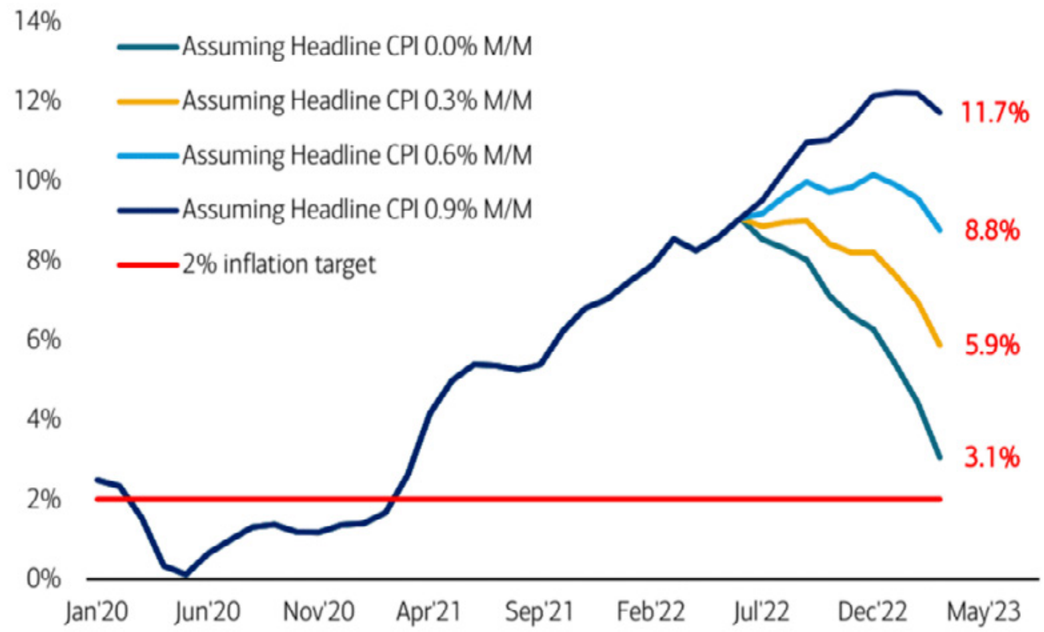
But it may take a while for the reported inflation rate to return to the Fed's target. This chart from Bank of America shows various scenarios for inflation in the coming months. As illustrated below, it will take several months of little to no inflation for the annual rate to drop below 5% and even longer to reach the Fed's 2.0% target:

Chart 2: Headline CPI <5% in Q1'23 requires big drop in monthly print

Headline US CPI YoY projections



Source: BofA Global Investment Strategy, Bloomberg

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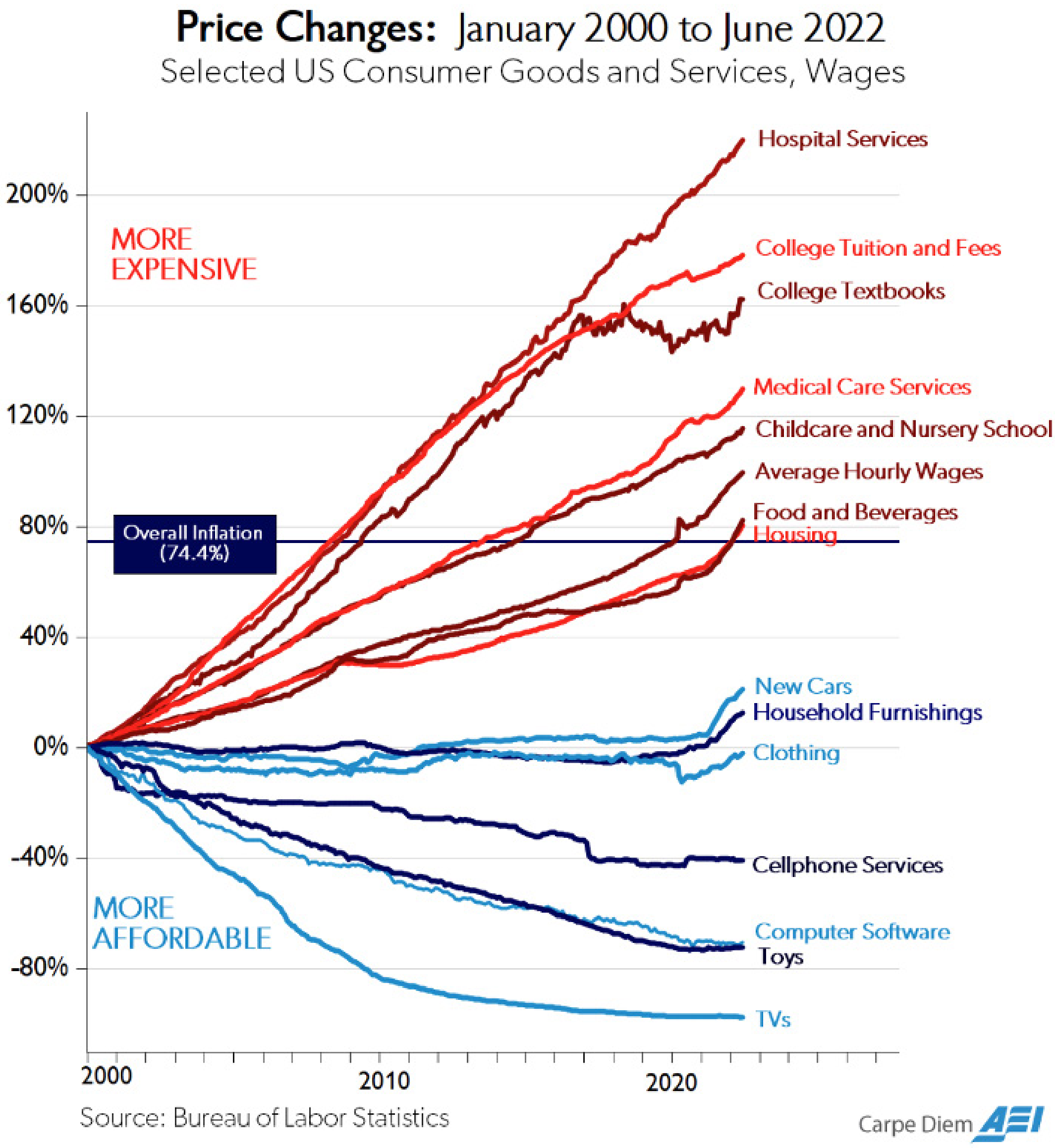
Taking a longer-term view, not all categories have seen prices rise at the same pace. Inflation for services has increased faster and more substantially, while inflation for goods is mostly lower. While overall inflation is up ~75% since the year 2000, categories related to services have seen prices increase significantly more than others. College attendance, hospitals, and daycare services are all areas that require more personnel to meet the needs of consumers and have seen the largest price increases. Meanwhile, many goods are much cheaper than they were 20 years ago, due mostly to technological advancements as well as cheaper labor overseas (chart from Mark Perry):



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CHARTING THE COURSE: **THE STOCK MARKET**

Stock returns are muted during economic recessions. We do not believe a recession has started yet, but the risks remain elevated in the months ahead. Over the past 50 years, stocks have been volatile during recessions, and returns over those periods have been mostly lower (chart from LPL):

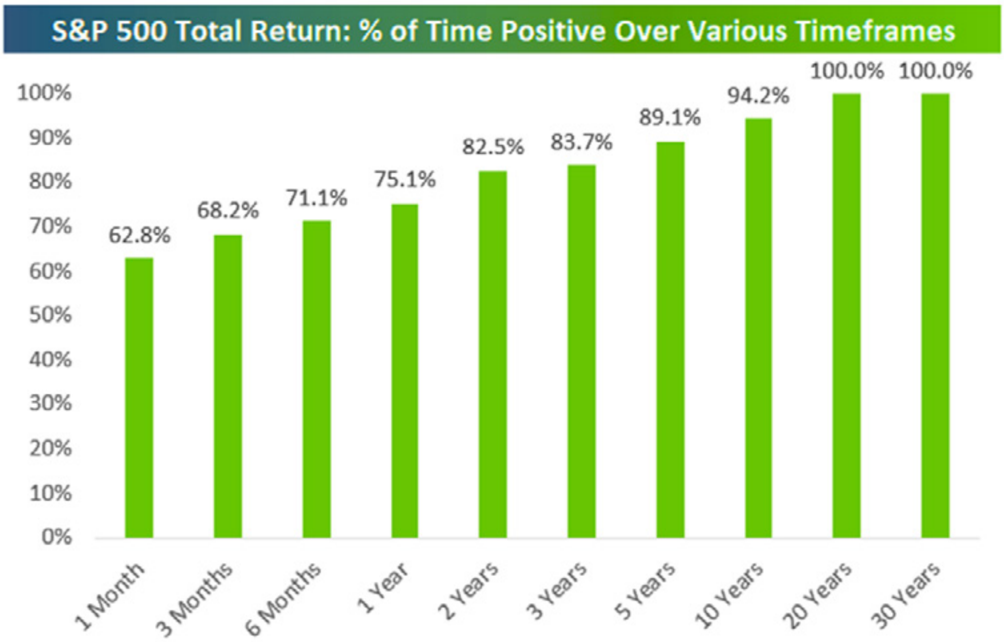
Stock Returns During Recessions

Not All Recessions Are Bad For Stocks

Recession Start	Recession End	Length of Recession (Months)	S&P 500 Index Return
March-45	October-45	8	16.4%
December-48	October-49	11	8.7%
August-53	May-54	10	17.9%
September-57	April-58	8	-3.9%
May-60	February-61	10	16.7%
January-70	November-70	11	-5.3%
December-73	March-75	16	-13.1%
February-80	July-80	6	5.7%
August-81	November-82	16	5.8%
August-90	March-91	8	5.4%
April-01	November-01	8	-1.8%
January-08	June-09	18	-37.4%
March-20	April-20	2	-4.8%
Average		11	1.3%
Median		10	5.4%

Source: LPL Research, NBER, 08/01/22
GDP = Gross Domestic Product

Despite any short-term turbulence, stocks tend to do well over the long term. We've stated our concerns about the economy in recent Macro Musings. While the current risks are reflected in both **macro**cast™ and **micro**cast™, it is important to not lose sight of the excellent performance of stocks over the long run. The following chart from Bespoke reminds us that over longer time horizons, equities tend to generate positive returns. Even looking out five years, stocks have been higher nearly 90% of the time. We believe this will continue to be the case despite any short-term market turbulence.



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This time of year typically serves as a reminder for many parents and grandparents that they are one year closer to their children or grandchildren shipping off to college. If you have any questions, thoughts, or would like to discuss establishing a plan to help your child or grandchild fund their education, please contact your Corbett Road Wealth Manager today!

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