Walnut Peak Financial Consulting

Summit Up

JANUARY 2023

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EDITION #1

WALNUT PEAK FINANCIAL CONSULTING

First and foremost...

2022 could be remembered for many things in which the U.S. and even the world were changed and shaped economically and politically. It seems to me the market's fortitude in the face of all of the obstacles and adversity is the main story.

- We saw Russia invade Ukraine. This led to massive global implications, including but not limited to a massive rise in oil and gas prices, and a rise in the price commodities.
- That combined with continued transportation issues, increased wages and persistent inflation reaching a 40 year high.
- In an effort to combat that inflation, The Fed became historically aggressive. With three modest rate hikes to start the year, three rate hikes of 75 basis points and finishing the year with 50 basis points and signaling more to come.
- The chain reaction to The Fed's behavior at such a pace has been home prices having a reverse course of direction with prices as interest rates have doubled in a year and drastically altered the housing market in short order. Student loans were forgiven, then they were not, then some were again. I think they gave me some back.

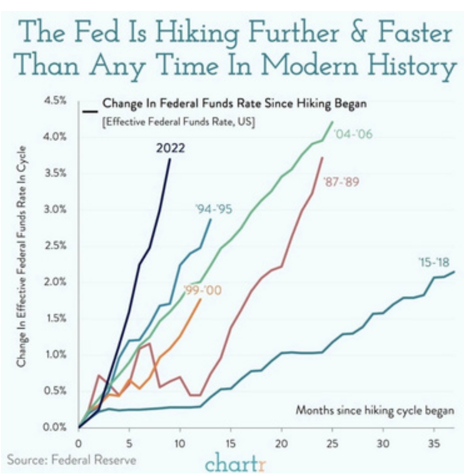
Continued...

- These on their own make the market move and cause investors to get skittish yet simultaneously did not completely dismantle the market entirely. The high for the S&P for the year would be on the 4th day of the year and gradually decline until being down 27% on October 13th. There came heavy volatility with swings up in April and August, both followed by massive drops. There was two-month positive charge in October and November the recouped 14%. At the time of writing this on the 27th of the December the market was down 19.5% after having been down three consecutive down weeks. That looks bad but considering where the market was in October, perhaps it will be remembered for its resiliency. The momentum moving out of the year however could make 2023 different.

Some observations from the top down seem to be a move to de-globalization. Over the course of the last couple of decades, there has been a focus on shrinking the world in a sense. Nations relying on one another for each one another's commodities and natural resources. The pandemic seems to have pointed out some rather large inefficiencies in the event there are disruptions to foreign suppliers, or the shipments. One such example has led Apple to explore other options for microprocessors as they landed on a shortage for phones. A shortage also happened with cars driving up the prices not only on new cars but on used cars earlier in the pandemic. This could have various outcomes as it plays out. Do those types of jobs become plausible locally? That would be great for jobs, bad for the price of electronics and cars. Long travels to see how this plays out.

Enter 2023

Out of the gate the FOMC (Federal Open Markets Committee [post on WPFC Facebook]) will meet at the end of January, which should set the tone for interest rates. through the year. While the continued push in interest rates should prove to be effective in slowing inflation, it should also be effective in slowing the economy. The continued stated goal is for a "soft landing", meaning no recession but many feel we are past that point.

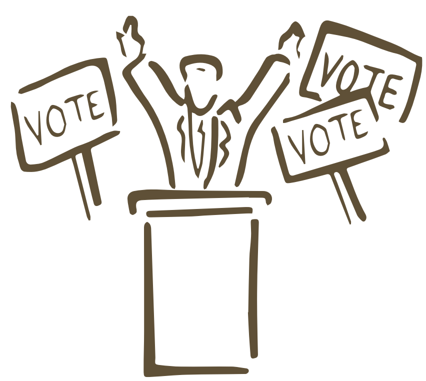


This isn't a stimi check!

It seems likely that unemployment numbers will grow. The Fed has come right out and said they want to see a higher unemployment number. Too many people are at work. Put another way, people are not even happy with what they make, much less that they have a job; they want more money. The government wants to shorten money supply not make more available, so if less people are working, less money is in the economy. Additionally, it would seem rational they would want to help companies get leverage in forcing employees back to office buildings and commerce back to cities. On its face it is a painful proposition to have more people out of work while the economy gets worse, but it is a correction. Like giving yourself a haircut and you take more off one side and try to even it out and make the same mistake on the other side. Just cannot quite get it.

I guess some politics

It seems safe to say as the Presidential candidates hit the road, each will have their own pitch for saving the economy, but at least a couple will be in favor of reversing rates. There is data to support performance during election cycles. It is up for dispute considering election cycles take place every four years and the results go from 1933 to 2015 so we are looking at limited data. However, the results do show that the 3rd year of a President's term is typically the best for market returns with an avg annual return over 16%.



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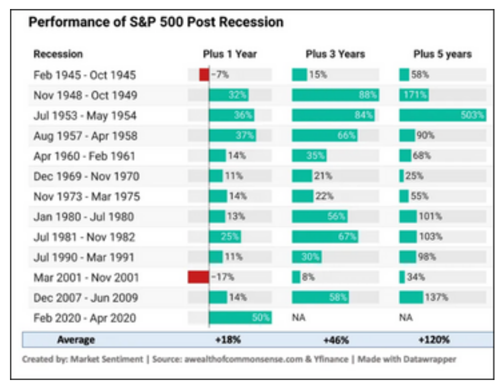
"Usually recessions sneak up on us. CEOs never talk about recessions," said Zandi. "Now it seems CEOs are falling over themselves to say we're falling into a recession. … Every person on TV says recession. Every economist says recession. I've never seen anything like it."
Mark Zandi, Chief Economistat Moody's Analytics.

The Shepherd Boy

I believe almost everyone is familiar with the fable of The Boy who Cried Wolf. Were you aware he was a shepherd?. I always pictured him more of a Paul Revere character, just stirring up trouble. Either way while that was designed to stop children from lying, if looked at through a different lens, perhaps it teaches a different lesson. If we take the story at face value on the day the wolf came, no one came out; not one. The collective looked out their windows and doors and saw no one else was going and decided they weren't going to be the one that went to help.. I read an interesting comment from an economist a couple days ago that was something along the lines of "normally a recession creeps up on people, everyone doesn't see it coming all at once." He is not wrong. It seems like everyone but The Fed, who can't, is saying guaranteed recession, it is just to what extreme. Herd mentality is very much a concept in our industry, and it is one I have discussed before. Our clients adopt the mentality, and it's partially responsible for why clients don't receive the same results as the market itself. A research study out of the University of Leeds in 2017 discovered it takes a minority of less than five percent to influence a crowd's direction – and the other 95 percent will follow without realizing it. Is there any chance the best in the world have herd mentality? Is it possible they are coaxing the retail to drive the market lower so they get a better price?

So what?

2023 is playing out as a table setting for years to come. Since 2008-2009, the economy has been driven by loose money policies and companies being able to borrow money for cheap to grow at rapid rates. When tested in 2018, the market could not handle the minor increases and reversed course. This surely was a tide lifts all boats scenario but as value stocks shared their rewards with investors and growth stocks redeployed and got bigger. With cash more expensive to borrow, things are shaping up for companies with cash on hand, and free cash flow, to begin outperforming once again which points in the direction of value. Some sectors that would fall into value side would be considered financials, energy, and consumer staples.



Performance of S&P 500 Post Recession

Recession	Plus 1 Year	Plus 3 Years	Plus 5 years
Feb 1945 - Oct 1945	-7%	15%	58%
Nov 1948 - Oct 1949	32%	88%	171%
Jul 1953 - May 1954	36%	84%	503%
Aug 1957 - Apr 1958	37%	66%	90%
Apr 1960 - Feb 1961	14%	35%	68%
Dec 1969 - Nov 1970	11%	21%	25%
Nov 1973 - Mar 1975	14%	22%	55%
Jan 1980 - Jul 1980	13%	56%	101%
Jul 1981 - Nov 1982	25%	67%	103%
Jul 1990 - Mar 1991	11%	30%	98%
Mar 2001 - Nov 2001	-17%	8%	34%
Dec 2007 - Jun 2009	14%	58%	137%
Feb 2020 - Apr 2020	50%	NA	NA
Average	+18%	+46%	+120%

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Quote - "Do not spoil what you have by desiring what you have not: remember that what you have was once among the things you only hoped for." - Epicurus