Scotty C. George
Chief Investment Strategist

October 17, 2022

Market Outlook:

Dealer's Choice

Anyone who invests knows, or should know, that *up precedes down* and *down precedes up*. Volatility is a part of the game and must be embraced. Quantitative scientists measure the magnitude and duration of cycle phases from which are derived predictions about the future course of events. Bemoaning the condition of the financial markets or the economy is uninspiring rhetoric because whichever cycle we're in is merely precedent for whichever one follows.

That's not to say that human nature must be ignored simply by wishing it isn't there. Losing is real, as is winning, and nobody likes to lose. But it is mostly a matter of choice, and facts, about how one choses to assess the current state of affairs and adapts to it. In financial matters that job falls to money managers to allocate funds according to risk tolerances, time horizon, and expectations about the future.

The current debate revolves around whether or not we are in a recession; whether the financial markets are entering a bear phase; and whether or not we perceive opportunity or disaster is in the offing. Above and beyond essential evaluation of the objective data, there are those for whom those answers derive from a personality predisposition. If a black cloud follows you always then things look bleak. Overly optimistic investors tend to see the bright side. As a client fiduciary (a term one hears on television a lot lately) I am always aware of the pitfalls embodied in the data, but optimistic about finding solutions to my client's objectives. That is what asset allocation is all about. As carpenters say, *"measure twice, cut once".*

Undaunted

As quarterly earnings season got underway last week it appeared from the diverse sample size that we are not in a particularly precarious position, rather a relentless one. The *pace* of economic acceleration was abating from that which occurred immediately following the worst pandemic in a century. The market jitters and gyrations in recent weeks were sourced by uncertainty concerning *rate of decline in earnings*, not the earnings themselves.

Recall that we were all encouraged to spend our way out of our despair by bankers and politicians who kept interest rates artificially low and who passed legislation extending benefits and offering cash incentives. Today, the tide has turned....at least for the bankers who are progressively increasing interest rates as a means to stem unyielding spending and to quell inflation anxieties. If, indeed, the past is prologue, then we know that when this phase is over we will reach an inflection point from which the next growth cycle will emanate.

Our current baseline assumptions are that modest increases in employment, marginal slowdown in demand, post-Covid supply chain shortages, and higher interest rates will narrow profit margins (earnings) in the near term, making stocks significantly less attractive for risk reluctant investors. Similarly, we see opportunity in short term bonds as a means of enhancing portfolio total return. We want our portfolios to be "balanced", but as risk averse as possible. Expected slowdowns in the economy will probably be perceived as negatives to overall confidence readings...a cycle of pessimism that feeds upon itself. Right now, micro is more important than macro for most investors.

We are holding a healthy level of cash in our portfolios as a buffer against daily volatility. While portfolio valuation declines are never acceptable they must be tolerated until the end of this upheaval is completed. However, there are, and will continue to be, opportunities for capital gains in socially responsible investments (SRI) such as agriculture, healthcare, alternative energy, infrastructure, and transportation.

The pandemic was a once in a lifetime (negative) phenomenon. Its traces will be felt for generations. But if this is indeed our "down", then there is hope that the next "up" will be even more handsomely rewarding.