



Bring on the Recession!

November 2022

*“The worst thing that happens to you may be the best thing for you if you don’t let it get the best of you.”
– Will Rogers*

Last year we forewarned that recessions are a natural yet painful part of every business cycle. But politicians (both red and blue) successfully prevented one from occurring in 2020 and 2021, seemingly without worrying about the consequences. So, we also reminded everyone that the markets had moved up to extremes that could be unsustainable, and the longer you postpone the natural order of things the more painful the inevitable lesson may be. Which is why I say, please, bring on the recession - if for no other reason than to get through the tough times sooner than later and return us to a natural business cycle.

The natural order of things means that there will always be some “inevitables”. For instance, interest rates have trended down over the last forty years; inevitably, especially since rates went to 0%, they were going to go back up. Unfortunately, the Federal Reserve stuck to their “transitory” inflation narrative for too long, a story we didn’t believe back then and was in fact incorrect. Turns out inflation has been very sticky. Finally, the Fed realized they were behind the ball and has been increasing rates quickly such that the federal funds rates went up more than 3.5% year-to-date! Which explains the terrible bond market performance (remember, yield and value have an inverse relationship such that when rates go up value goes down). This in turn helped cause the stock market to fall precipitously (another inevitable event).

To add insult to injury, seemingly everything (real estate, etc, etc) has been doing poorly this year, not just the stock and bond markets. Further, the order of events has been different this time as well. It seems over the last forty years if/when the economy or stock market did poorly, then interest rates would go down (boosting bond values and helping the economy find it’s footing). This time the bond market started doing poorly, and then the stock market reacted in kind. So that’s what *has* happened; now what *will* happen?

Unfortunately, we believe more of the same. I’m sorry to depresses you, but for several reasons we thoroughly believe we are only in the fourth or fifth inning of this multi-faceted correction (although we hope we are wrong!). First, please remember that rates have been trending down for forty years, so try as the Fed might, we can’t just get back to normal (whatever that may be now) in just one year. And the stock market was a bubble in the making for two solid years, if not longer when you see the covid correction as just a six month event in 2020. So, just as the U.S. economy is like a massive cruise ship that can only turn around very slowly, the markets cannot adjust to huge abnormalities (bubbles, etc) that were years in the making.

Add to this the fact that the government, for better or worse, possibly went well beyond what should have been done to get us through the pandemic. Specifically, we still have people that are not paying their mortgages or rent, knowing that the court system is clogged and just trying to catch up. We have well over a

trillion dollars in student debt that still is not being repaid, and now the government is trying to transfer some of that debt to the taxpayer (without being political, please remember that there is never a free lunch and if one person's debt is "forgiven" it just means someone else has to pay for it). We also know that, as reported by the Wall Street Journal two weeks ago, U.S. households still have around \$1.7 trillion in savings that they accumulated through mid-2021 above and beyond what they would have saved if income and spending had grown in line with the pre-pandemic economy.

Long story made short, there's still a massive amount of liquidity that allows people to forego jobs, etc, which could explain the still tight labor market. And don't even get me started on Congressional spending that goes far beyond what current revenue can support, which explains the growing deficit (and, oh by the way, as the Fed moves interest rates up that debt gets more expensive). Add to that the scary fact that two-thirds of federal spending isn't even voted on by Congress. Instead, so-called entitlements such as Medicare/Medicaid and Social Security, are automatic, nondiscretionary costs that will most likely increase when Congress finally admits that those programs are simply running out of money. Last but not least (and I know, depressingly), although interest rate increases are what is top-of-the-mind for most people, we cannot forget that the Fed is also in the midst of trying to reduce its own balance sheet of approximately \$9 Trillion, more than double what it was pre-pandemic (this is known as Quantitative Tightening, a new and untested process, as opposed to Quantitative Easing which has been employed in prior crises).

So where's the upside, you ask? Well, when given a choice about the unknown future, we always choose to be optimistic. The United States has been in dire straits before, and I'm convinced we will again emerge from these challenges better and stronger. In the meantime, we not only recommend you stay the course with a previously designed strategy, but review making lemonade from lemons. Review strategies such as tax loss swaps, Roth conversions, or other strategies that may work well in down markets (please consult your tax professional as well before employing any tax-related investment strategy).

Finally, the only thing you should ever learn from falling down is to get back up. So if/when things get worse before they get better, remember that the natural order of things means, as day follows night, that good times should inevitably follow tough times, recessions included. More importantly, please make sure to remind yourself of what life is really about. Use Thanksgiving as an opportunity to not only give thanks for what you have in life, but even more so who you have in your life; money will come and go, but love of, and time with, family and friends is what life is all about!

Happy Thanksgiving, and thank you so much for being part of our lives!!

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