metric financial

lower costs. better results.

Metric Financial Q&A – Inflation and The Federal Reserve

This Q & A was conducted on December 15th, 2022, one day after the Federal Reserve's December meeting and rate announcement. All answers and opinions reflect the views of our Founder & CEO, Tim Baker, CFA.

Q: Before we start on what happened yesterday and where we are now, can you give us your general view of what has gone on in 2022?

A: As I've mentioned before, what has happened to the economy and financial markets this year is completely natural, although unfortunate. I said back in 2020 that we were creating a "man-made" major economic event by shutting down businesses and forcing work-from-home. That created lopsided demand for things like technology and lack thereof for things like restaurants, hotels, fuel, etc. On top of all of that, we created incentives for people to leave or not join the workforce. Here we are a little over two years later and all the demand is back, and companies are struggling to ramp supply back up, which is made more difficult by people not rejoining the work force. This creates inflationary pressures, and it is one of the Federal Reserve's primary directives to control those pressures, mainly through raising short-term interest rates.

Q: Thank you for that. With that as backdrop, what happened with the Federal Reserve yesterday?

A: Well, clearly investors have been expecting a 0.5% rate hike ever since Federal Reserve Chairman Powell spoke recently. That's exactly what they got. However, and we are now calling this "The Powell Effect", investors were also told that their target rate is higher than previously thought and the outlook for employment is dim.

Q: What do you mean by "The Powell Effect"?

A: I mean it somewhat tongue in cheek. I've said all this year that I have the utmost respect for him, but he doesn't have great bedside manner. So, the Fed always announces at 2 pm EST and the markets generally turn positive when he first starts speaking and then plummet by the time he is done. That is essentially what happened yesterday. The S&P 500 was in the green for most of the day, fell off a bit at 2 pm, rallied pretty significantly, but then faltered and finished the day lower by about 0.6%.

Q: And how do you read that reaction?

A: I think stocks are always going to react negatively, not based on the announcement, but on the outlook. And investors never want to hear "we're going to raise interest rates more than you thought we were." That said, it's important to note that the 10-year US treasury, a good gauge for borrowing rates, especially for mortgages, took everything in stride. The yield was little changed and remains about 0.83% off its high this year. The drop in stocks yesterday should also be viewed bearing in mind that, since the beginning of October, the S&P 500 is up almost 12% through yesterday.

Q: So, you don't read anything out of the ordinary. Final thought – where do you see us going from here?

A: As you know, we don't believe in predictions or forecasts. They're a waste of time and a distraction. That said, we are still in a delicate state and investors should be prepared for bumps since day-to-day data will have outsized effects on financial markets. My personal view is that the Federal Reserve ought to be less stern with their language and more open to keeping their actions "data-dependent". By delivering these messages that they're going to keep rates higher for longer, they are themselves predicting where the economy will be next year. The other challenge we face is what happens if the unemployment rate starts moving upward. With so many people not even participating in the workforce, a job loss for someone who actually wants to work is a big negative. Some potential positives though: a negotiation of peace in Ukraine, a containment of Covid outbreaks in China, and/or a "soft landing" in the US (i.e., the Federal Reserve can slow or reverse rate hikes without pushing the economy into a deep recession). My biggest fear is not an economic recession, but rather an earnings recession. It is earnings that drive stock growth, and the more companies miss on estimates, the harder it is to justify a big market rally. We saw this in the early 2000s. But like that time, we will get through it. Good investors need to keep saving, have a plan, and let their financial needs drive their investments, not predictions or fears about what financial markets might do tomorrow.

*All return information sourced from MarketWatch and Morningstar metric financial

lower costs. better results.

Disclosures

Metric Financial, LLC is an Investment Adviser registered with the State of Connecticut. All views, expressions, and opinions included in this communication are subject to change. This communication is not intended as an offer or solicitation to buy, hold or sell any financial instrument or investment advisory services. Any information provided has been obtained from sources considered reliable, but we do not guarantee the accuracy or the completeness of any description of securities, markets or developments mentioned. We may, from time to time, have a position in the securities mentioned and may execute transactions that may not be consistent with this communication's conclusions. Please contact us at (860) 256-5895 if there is any change in your financial situation, needs, goals or objectives, or if you wish to initiate any restrictions on the management of the account or modify existing restrictions. Additionally, we recommend you compare any account reports from Metric with the account statements from your Custodian. Please notify us if you do not receive statements from your Custodian on at least a quarterly basis. Our current disclosure brochure, Form ADV Part 2, is available for your review upon request, and on our website, www.metricfin.com. This disclosure brochure, or a summary of material changes made, is also provided to our clients on an annual basis.

Past performance may not be indicative of future results. Different types of investments involve varying degrees of risk. Therefore, it should not be assumed that future performance of any specific investment or investment strategy will be profitable or equal the corresponding indicated performance level(s). Moreover, you should not assume that any of the above content serves as the receipt of, or as a substitute for, personalized investment advice from Metric Financial. Please remember to contact Metric Financial if there are any changes in your personal/financial situation or investment objectives for the purpose of reviewing/evaluating/revising our previous recommendations and/or services. Please also advise us if you would like to impose, add, or to modify any reasonable restrictions to our investment advisory services.

Historical performance results for investment indices and/or categories have been provided for general comparison purposes only, and, unless otherwise noted, do not reflect the deduction of transaction, custodial, or investment management fees, nor the impact of taxes, the incurrence of which would have the effect of decreasing historical performance results. It should not be assumed that your account holdings do or will correspond directly to any comparative indices.