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Bell Institutional

ECONOMIC OUTLOOK

The stock market continues to hold out hope for an economic “soft landing.” There’s no single definition of an economic soft landing, but we interpret it to mean that inflation returns to 2%, the unemployment rate remains low, the consumer remains upbeat, and the Federal Reserve is able to cut interest rates before economic growth potentially drifts into negative territory. Everybody is happy … what could possibly go wrong?

While we would love as much as anyone to see the soft-landing outcome, there’s not much history of the Fed accomplishing this result. It is hard to quantify all of the economic influences into one decision. Federal deficit spending in the last 12 months was $2.6 trillion, or 9% of gross domestic product. By most calculations, that is an unsustainable pace. Credit card and auto loan delinquencies are starting to rise, albeit slowly. Layoff announcements appear more regularly in news reports. Armed threats are forcing shippers to go around the Red Sea, increasing costs and adding weeks to delivery time. There is also an unknown impact from the multitenant commercial office space sector that goes beyond investment losses and migrates into big-city identities. Starwood Capital Group estimates that office asset valuation is probably worth $1.8 trillion – down from $3 trillion prior to the pandemic, when valuations were supported by the Fed’s ultra-low interest rate environment.

There are also geopolitical tensions: Russia-Ukraine, Israel-Iran, China-Taiwan, and the upcoming presidential election. I am no political historian, but I don’t recall ever seeing polls show that 70% of respondents didn’t want either candidate on the ballot. What will that mean when voters go to the polls? Will voters migrate away from a two-party mindset?

With all these concerns in the mix, should investors look to move their allocations? Fortunately, there is a well-known set of drivers establishing the framework for how investors position portfolios. Those factors are risk, return, time horizon, cash flow needs, legal constraints and other considerations that may apply to an investor. Note that nothing on this list requires predicting whether the economy will grow or shrink, guessing the Fed’s next move or foretelling the outcome of a presidential election!

If allocating investment portfolios is so straightforward, why does it seem so nerve-racking? To answer that question, I’d like to direct your attention to the “time horizon.” For many investors, the time horizon is 20, 30 or even 40 years – yet we feel compelled to check our balances daily, weekly and monthly. When we do that, we see the values moving all over the place. If values go up,

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we are happy and don't give it a second thought. If values are down, it can grind on us every waking moment – and we feel we must do something. Here's the good news: If nothing has changed in the personal investment profile you used to determine your initial allocation, you can ignore short-term market fluctuations.

To further push this point, let me tell you a story from my own experience. I started in the investment business in 1985 and joined Bell in 1992. I had a rude introduction to volatility on October 19, 1987 – a date that is now remembered as "Black Monday." The Dow Jones Industrial average fell 22.6%, and the S&P 500 fell 20.4% in one day – to date, still the single largest one-day percentage market decline. (For perspective, that would be like the Dow falling 8,693 points today.) Fortunately, at that time, all of the money I was managing was institutional, so I did not have to field phone calls from panicked investors.

It took almost two years for the Dow to return to the levels it had reached before the sell-off. I had the benefit of watching how calm institutional money was, in contrast with personal money. I thought to myself, "There must be something to learn here." I did my best to practice remaining calm in the face of volatility – to the point where I quit looking at my own investment statements to avoid the anxiety that comes with market fluctuations.

Fast forward to 1992, when I started with Bell. The stock market was in the early stages of its next prolific rally. This was the great tech stock run-up. In early 2000, one of my colleagues asked if I had seen the huge increase in our 401(k) plan. I remember this not because of the question, but because of my response: "I have seven years of unopened statements in my desk drawer." (As you might guess, in those days, our 401(k) statements were not just a click away.) Shortly after that, the tech stock bubble "popped" in the form of a two-and-a-half-year decline … and I continued to stuff my desk drawer with unopened 401(k) statements.

Watching volatility in real time is agonizing. Looking through the lens of 40 years, it's hard to find the greatest market sell-off in history without having a specific timeline on the axis as a reference. Even with that reference, it looks quite benign compared to where the market has gone.

Don't get me wrong. As your investment providers we are watching markets day to day with keen interest, tracking economic trends and looking to separate cyclical from secular themes. To the extent that secular themes appear to be developing, we adjust exposure in major investment classes of portfolio investment allocations. Our goal is to free you from the anxiety of day-to-day market and economic minutia, providing the peace of mind to enjoy other activities.

Happy 2024, and thank you very much for your business and confidence in Bell.