WASATCH CAPITAL MANAGEMENT OF RAYMOND JAMES®

"There was an unexpected correction on Wall Street today after a leading analyst used the word 'irregardless' instead of 'regardless.'"

JULY 2022

INSIDE THIS NEWSLETTER

- **JULY COMMENTARY: A MATTER OF PERSPECTIVE**
- **WASATCH TEAM UPDATE**

A Matter of Perspective -Article by Mark Lazar

Mark Lazar is an independent writer with Pathway to Prosperity and is not affiliated with Raymond James. Views expressed by this writer are the current opinions of this author and not necessarily those of Raymond James & Associates.

***You cannot spend your way out of a recession nor borrow your way out of debt.* Daniel Hannan**

Item	YTD Change
Dow Jones Ind Avg	-15.31%
S&P 500 Index	-20.58%
EAFE Foreign Index	-20.97%
Emerging Market Index	-18.78%
Barclays Agg Bond Index	-10.35%
10-Year Inflation Forecast	2.31%
Unemployment Rate	3.6%

**Market index data as of 6/30/2022*

The “R” word has been creeping into the headlines with greater frequency as of late. But what is a recession and what does it mean to you? During his 1980 presidential campaign speech, Ronald Reagan proclaimed, “A recession is when your neighbor loses his job. A depression is when you lose yours.” While that's probably as good a definition as any, in technical terms a recession is defined as two consecutive quarters of negative or declining economic (GDP) growth, whereas a depression is simply a long, deep, and pronounced recession.

According to the NBER, since WWII, the typical recession has lasted 11 months and has occurred, on average, every six years. It’s important to understand that recessions are a normal and inevitable part of a business cycle, and this is true for market as well as centrally planned economies. Nothing in life is linear and economic cycles are no exception. Fortunately, recessions tend to be short-lived, usually lasting three or four quarters, at which point the economy tends to rebound.

One might ask why recessions are inevitable. Ironically, recessions are almost always the result of policy error: monetary, fiscal, or social. Historically, central banks tend to be too accommodative for too long, which leads to inflation. Inflation is typically "remedied" by tighter, often ill-dispensed monetary policy that results in negative growth rather than the intended slower growth (i.e., soft landing). Similarly, populist anti-growth fiscal policies, such as higher taxes, increased regulation, and trade restrictions, all serve to discourage hiring, spending, and investing, effectively undermining the business cycle and paving the way to the next recession. Lastly, social engineering policies, such as the federal government’s 1992 Affordable Housing Goals, compelled Freddie Mac and Fannie Mae to lower credit standards for home loans to absurd levels and set the housing market on a path of inevitable collapse.

While each business cycle is unique, the current cycle is in many ways similar to the recession of 1945. At that time a sharp decline in government spending brought about by a rapid transition to a peacetime economy led to a 13% drop in GDP, but with little change in the rate of employment. Subsequently, over the following two years inflation surged, hitting 18.1% in 1946 and 8.8% in 1947 before dropping to 3% in 1948.

2020 COVID lockdowns kneecapped a robust economy, causing a 5.1% and 31.2% drop in Q1 and Q2 GDP. Since policymakers always feel compelled to “do something,” the federal government and central bank “rode to the rescue,” and pumped nearly $7 trillion dollars into the system, inflating Q3 GDP growth to 33.8%. Analogous to the aforementioned post-war recession, the sugar high created by the ~$7T COVID stimulus was also temporary, and the economy is clearly slowing. Furthermore, unemployment has thus far remained low, while price levels (inflation) are significantly and stubbornly elevated. In other words, inflation is both worse than expected, and clearly not transitory.

We expect policymakers to both know more than we do, and to organize society for us in ways that improve quality of life. But it’s difficult to have faith in bureaucrats who were so obviously wrong in their predictions and policies. We were initially told in spite of the lockdowns and government giveaways that inflation would be benign. When CPI clocked in at nearly four times Fed Chair Powell’s forecast we were then told that, well, okay, inflation is worse than expected but it’s *transitory*. When, contrary to their assurances otherwise, inflation increased and remained elevated, they finally admitted it wasn’t transitory, but not to fret; the economy is strong and a recession isn’t in the cards. Now, almost every economist on the planet is conceding we’ll likely be in a recession sometime next year. And to rub salt in the wound, there hasn’t been a single policymaker who has taken responsibility for ill-conceived, ill-dispensed policies that put us in this pickle.

Policymakers would better serve their constituents by learning that they can neither manage nor control the economy any more than they can control the weather. Instead, they should focus on creating an economic environment that unleashes the productive capacity of a free market system then get out of the way. Economic cycles, including recessions, are both natural and healthy. Recessions serve to cleanse economic excesses (inventory, labor, asset prices, etc.), which sets the stage for the next leg up, and should neither be feared nor managed.

No matter how rosy the economy may appear today, a rainy day will eventually come. However, if you plan ahead, maintain a reasonable cash reserve, use debt judiciously, and live beneath your means, when the next recession shows up on your doorstep you will be just fine. It may not be pleasant, but you will be both financially and emotionally prepared to ride out the proverbial storm.

The good news—sort of— is that inflation should normalize over the next few years. How do we know this? The breakeven rate of inflation—the market's unbiased forecast of inflation—over the next five years is presently 2.56%. Over the next ten years is 2.32%. Similar to the post WWII period, inflation likely remains elevated in 2022 and 2023 then drops precipitously in 2024. Unfortunately, the factors that will ultimately tame inflation will likely be two-fold; initially, a reduction in aggregate demand (a slowdown in the economy and/or a recession) as well deflationary/disinflationary macro factors, such as an aging population, slowing population growth, globalization (think *outsourcing*), and technology (innovation/disruptive technologies that reduce costs).

Ironically, both Fed chair Powell and Treasury Secretary Yellen were both right when they predicted inflation would be transitory. However, the question then is what is the definition of *transitory*? 6-months? 1-year? 2-years? 3-years? If one takes a very long-term view then I suppose 2–3 years of soaring consumer prices is a temporary situation and this too shall pass. However, when a Benjamin is no longer enough to fill up the gas tank, and a weekly trip to the grocery store can be more than double that, transitory can seem like dog years. I guess it's simply a matter of perspective.

Mark Lazar, MBA
CERTIFIED FINANCIAL PLANNER™
Pathway to Prosperity

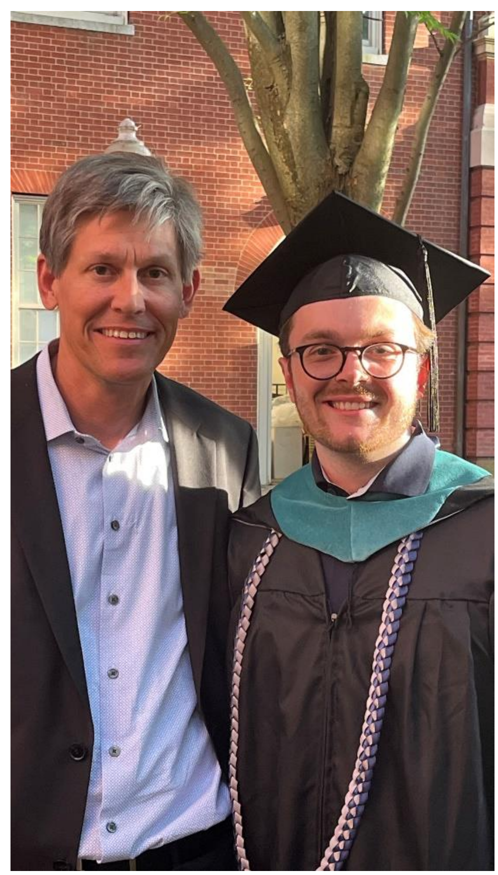
Wasatch Team Updates

Stan

Stan, his parents, 6 siblings and spouses in Costa Rica celebrating 50 years of marriage for his parents!

Rees

Rees, Lisa & Rachel walking at Deer Valley



John

John celebrating his son, Chase's, graduation from Georgetown!

Reed

Reed has been enjoying the hummingbirds this summer.

Nicola

Nicola with her kids & grandbabies at the Portland Zoo!

Matt

Matt & Sam with Matt's Mom at a Snow Pine Lodge Alta concert!

Jon

Jon and family at a family reunion!

Stan Goodell, CFP®, Vice President - Investments | 385-275-3792

Rees Petersen, CFA®, Vice President - Investments | 385-275-3607

John Clower, CFA®, Vice President - Investments | 385-275-3590

Reed Grant, Financial Advisor | 385-275-3797

John Bergerson, CFA®, MBA, Investment Portfolio Associate | 385-275-3608

Matt Brunner, Financial Advisor | 385-275-3795

Jon Metcalfe, MBA, Senior Client Service Associate | 385-275-3793

Nicola Palomo, Registered Client Service Associate | 503-944-5382

2750 E Cottonwood Parkway, Suite 520, Cottonwood Heights, UT 84121

1389 Center Drive, Suite 200, Park City, UT 84098

Raymond James & Associates, Inc. member New York Stock Exchange/SIPC