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Forecast Financial Report 2023

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Questions?

info@concordwealthpartners.com

Introduction

Gary Aiken

CIO at Concord Asset Management (CAM)

Gary joined the CAM team to design, implement, and lead the firm's turnkey investment management program.

With over 21 years of investment experience, Mr. Aiken holds an undergraduate degree in economics from the University of Maryland and an MBA from The George Washington University School of Business. Prior to joining Concord, Gary was Chief Investment Officer for a trust company and Chief Risk Officer for a mutual life insurance company.

We know what's on your mind...

Inflation

Stock & Bonds Markets

Recession

Agenda

- Where we've been
- Where we are
- What may be ahead
- Final thoughts

Where we’ve been

Fighting inflation amid geopolitical uncertainty

Let’s talk about inflation

“You can lead a horse to water, but you can’t make him drink.

You can force money on the system in exchange for government bonds, its close money substitute; but

you can’t make the money circulate against new goods and new jobs.”

Paul Samuelson

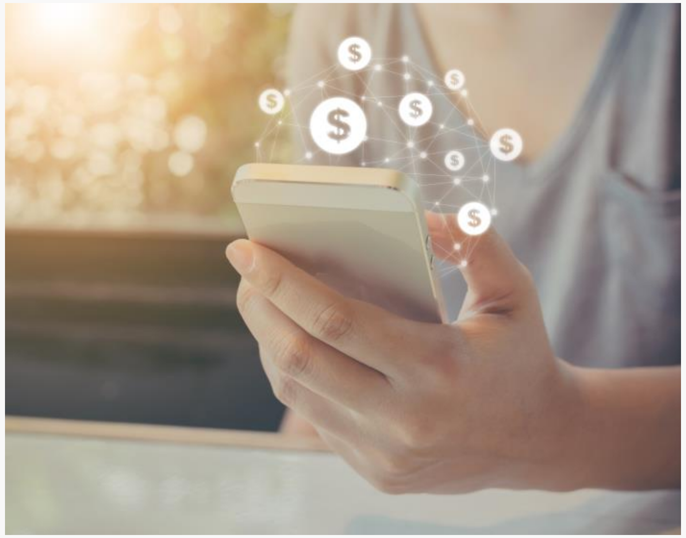
- Ph.D., Economics, Harvard University
- 1970 Nobel Prize in Economics
- Wrote *the* Econ 101 textbook in 1948 used in most universities today!

Photo Credit: The Nobel Foundation

25 years of printing didn't cause inflation?

Velocity (the churn of that money in the system) kept falling.

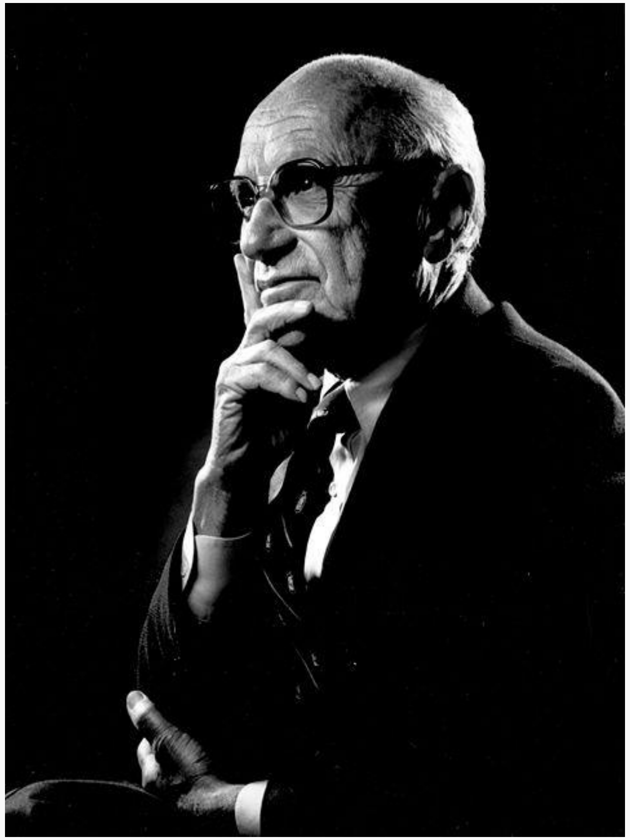
Excess money was chasing assets, not goods and services.



Technology and Globalization were disinflationary forces.

Result: 2.2% Annual Inflation Rate 1994-2019

Let’s talk about monetarism



“**Inflation is always and everywhere a monetary phenomenon**

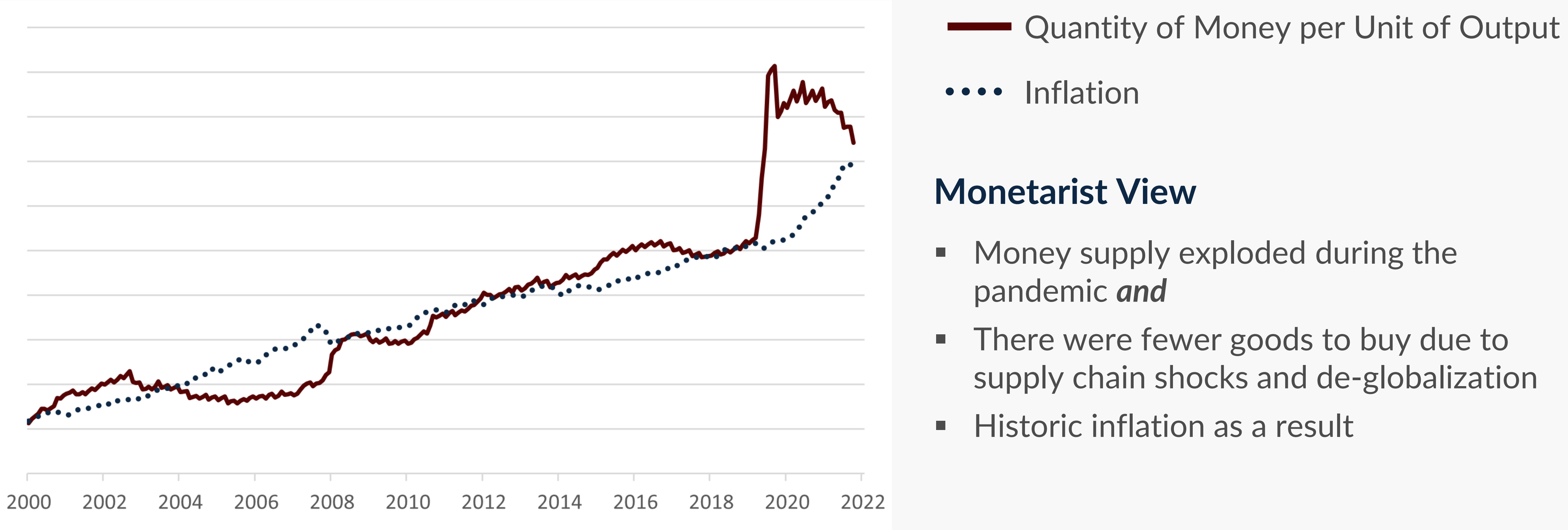
in the sense that it is and can be produced only by

a more rapid increase in the quantity of money than in output.”

Milton Friedman

- Ph.D., Economics, Columbia University
- 1976 Nobel Prize in Economics
- Work concentrated on consumption, monetary policy

Monetarism becomes mainstream



Monetarist View

- Money supply exploded during the pandemic ***and***
- There were fewer goods to buy due to supply chain shocks and de-globalization
- Historic inflation as a result

Source: Bloomberg Finance L.P., Bureau of Labor Statistics, Bureau of Economic Analysis, Federal Reserve

Removing *excess* money

Money Supply x Velocity   Inflation x GDP

$$M\ V = P\ Y$$

1

The Fed is **reducing the money supply** through higher Fed Funds interest rates and Quantitative Tightening

2

This lowers the churn of money in the system and **raises interest rates**

3

Which **slows overall economic activity** as saving becomes relatively preferable to investing and spending.

4

Leading to **lower inflation**

What's missing?

Money Supply x Velocity　　Inflation x GDP

$$M\,V = P\,Y$$

M
V

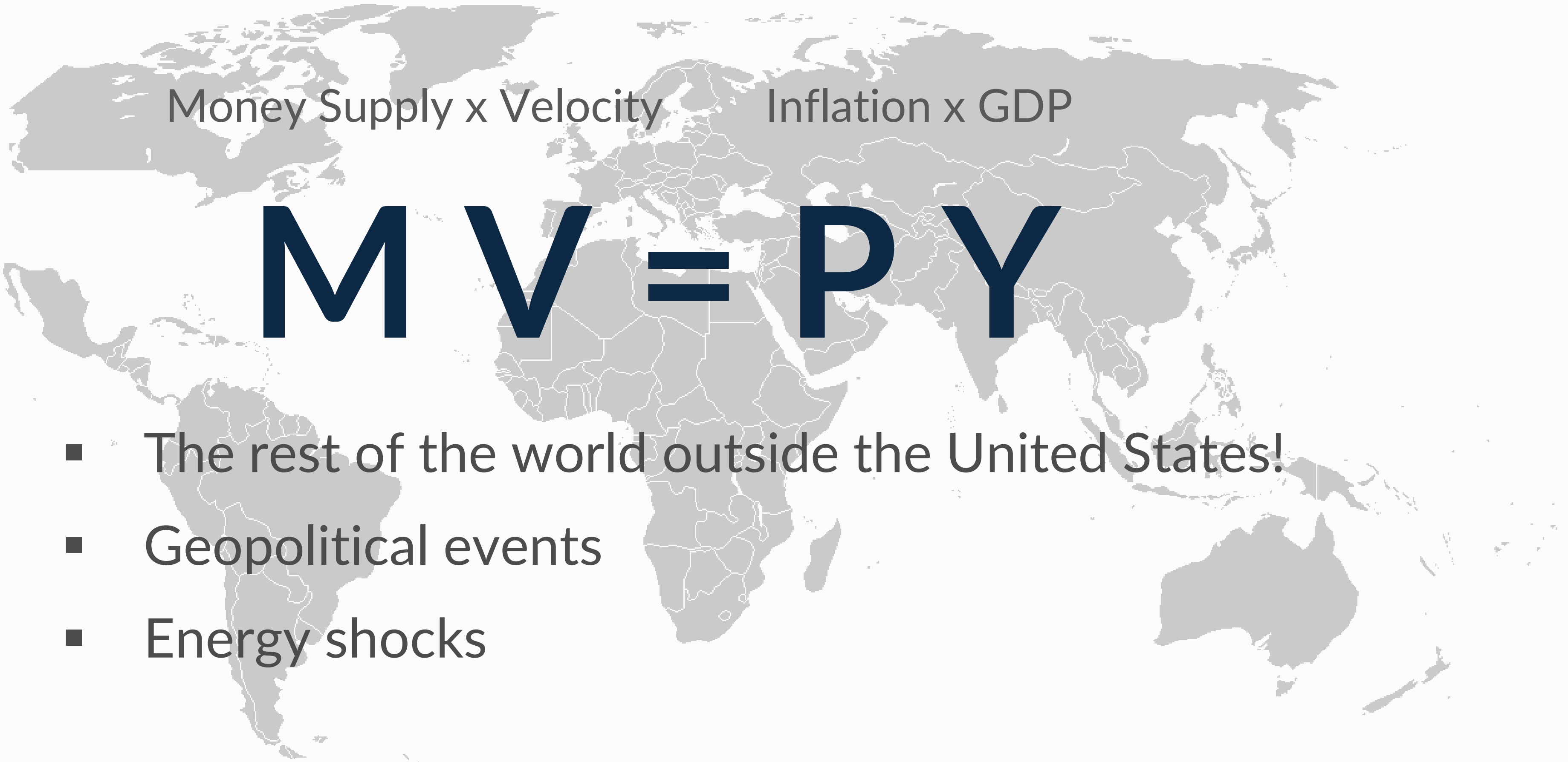
P
Y

Monetary policy acts in "long and variable lags"

Friedman analogized the "fool in the shower"

Time

What else is missing?



Money Supply x Velocity   Inflation x GDP

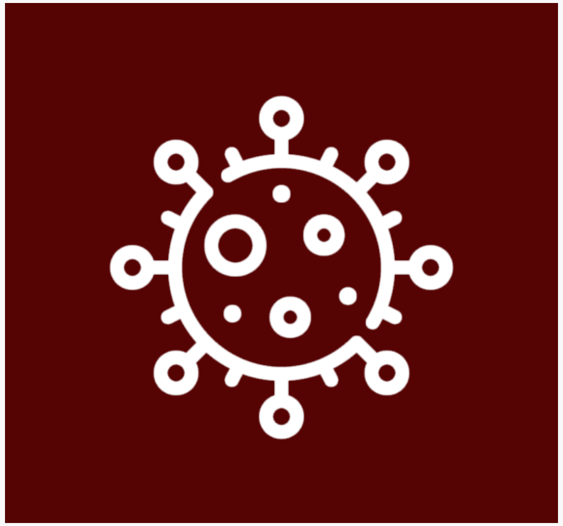
$$MV = PY$$

- The rest of the world outside the United States!
- Geopolitical events
- Energy shocks

2022 major themes persist in 2023

The Fed is ***still*** tightening monetary policy

The War in Ukraine is ***still*** ongoing

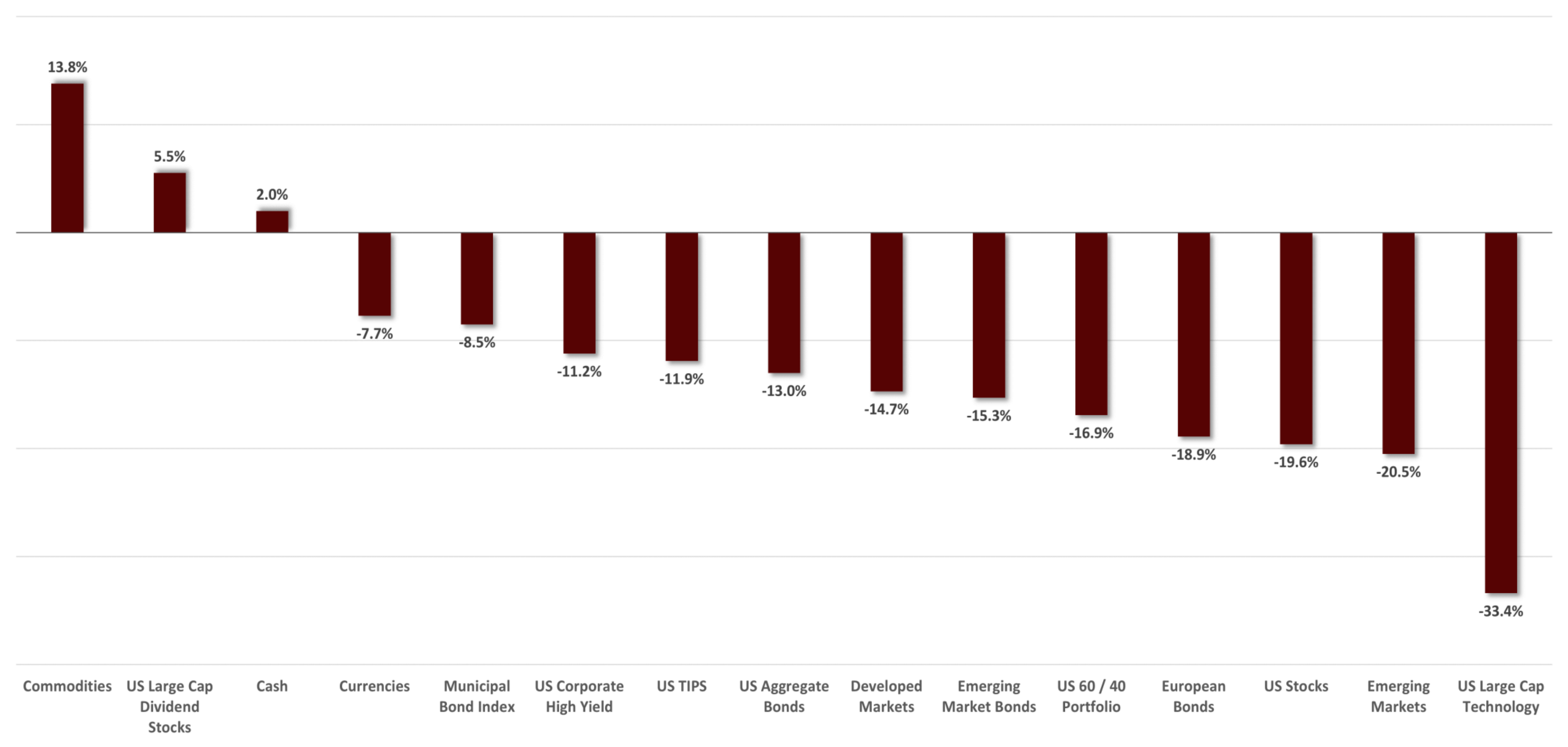


China is ***still*** emerging from COVID-19 lockdowns

Where we are

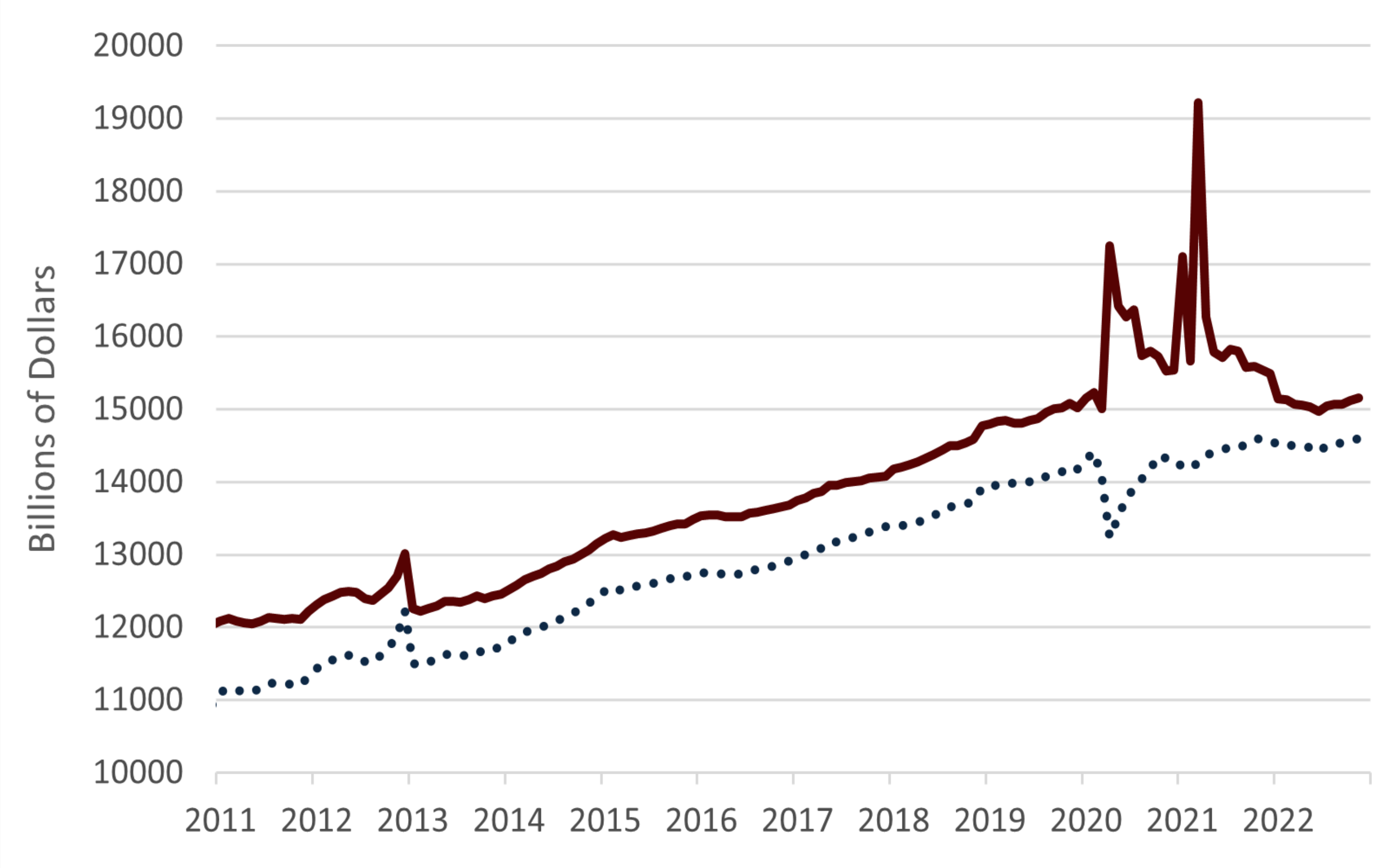
Setting the stage for 2023

Financial markets



Source: Bloomberg Finance L.P.

How are U.S. consumers holding up?



US Disposable Personal Income

U.S. Personal Income Excluding Transfer Payments

- Government stimulus programs
  - Saved the consumer in 2020
  - Created massive inflation in 2021
- At the end of 2022, real purchasing power is still at the same level as pre-pandemic

Source: Bloomberg Finance L.P., Bureau of Economic Analysis

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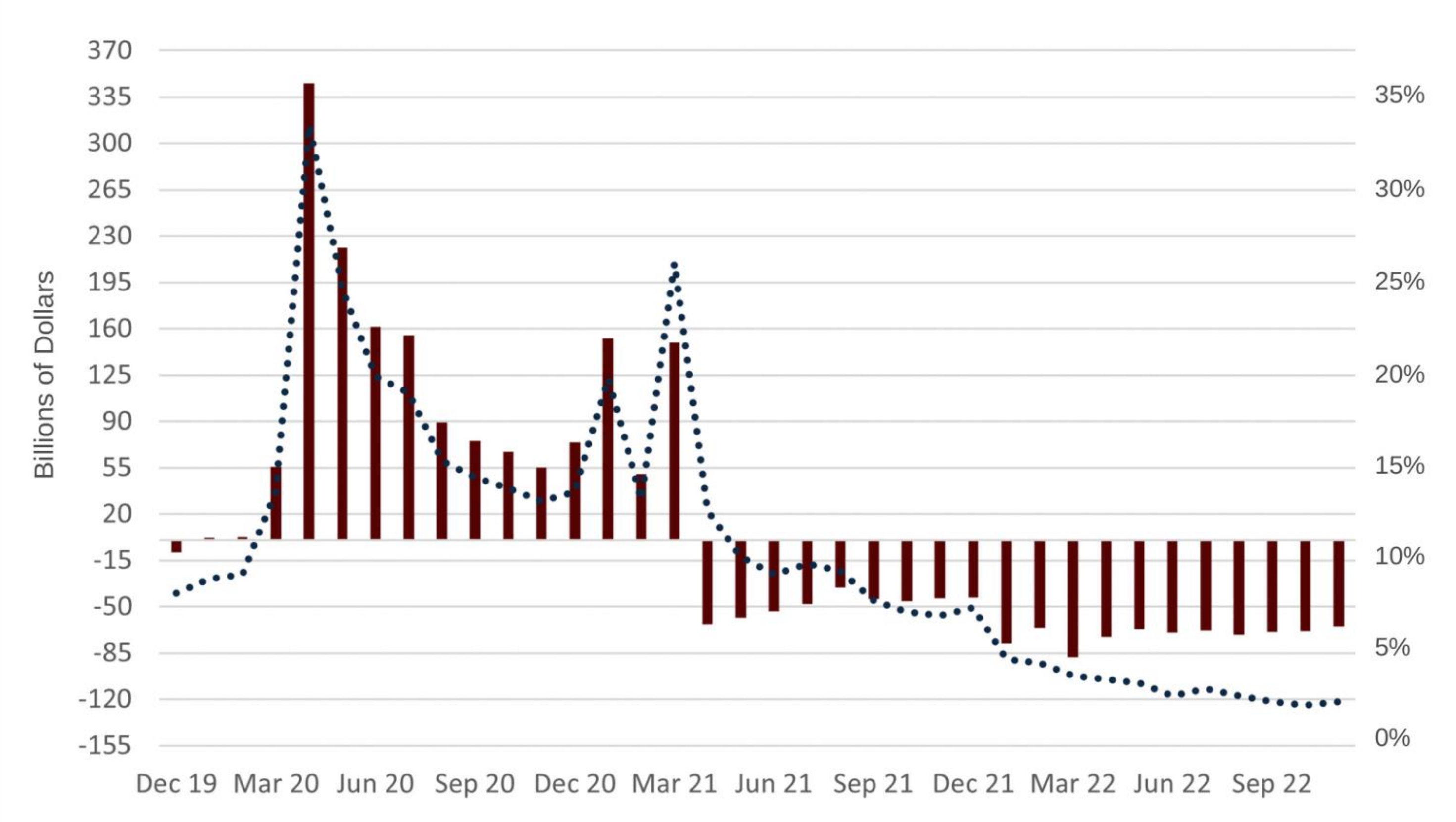
Consumers are depleting their savings



US Personal Savings YoY SAAR

US Personal Saving as a % of Disposable Personal Income

- Government programs enabled Americans to save
- Consumers have added drawn on their savings for 20 consecutive months
- The savings rate has only been lower once (July 2005)

Source: Bloomberg Finance L.P., Bureau of Economic Analysis

Consumers are leaning on their credit cards

- Credit card balances are 8% higher than pre-pandemic
- Total non-mortgage debt is 12% higher than pre-pandemic
- Consumers have added to their balances for 20 straight months

Consumers say they are feeling terrible

University of Michigan Consumer Sentiment Index

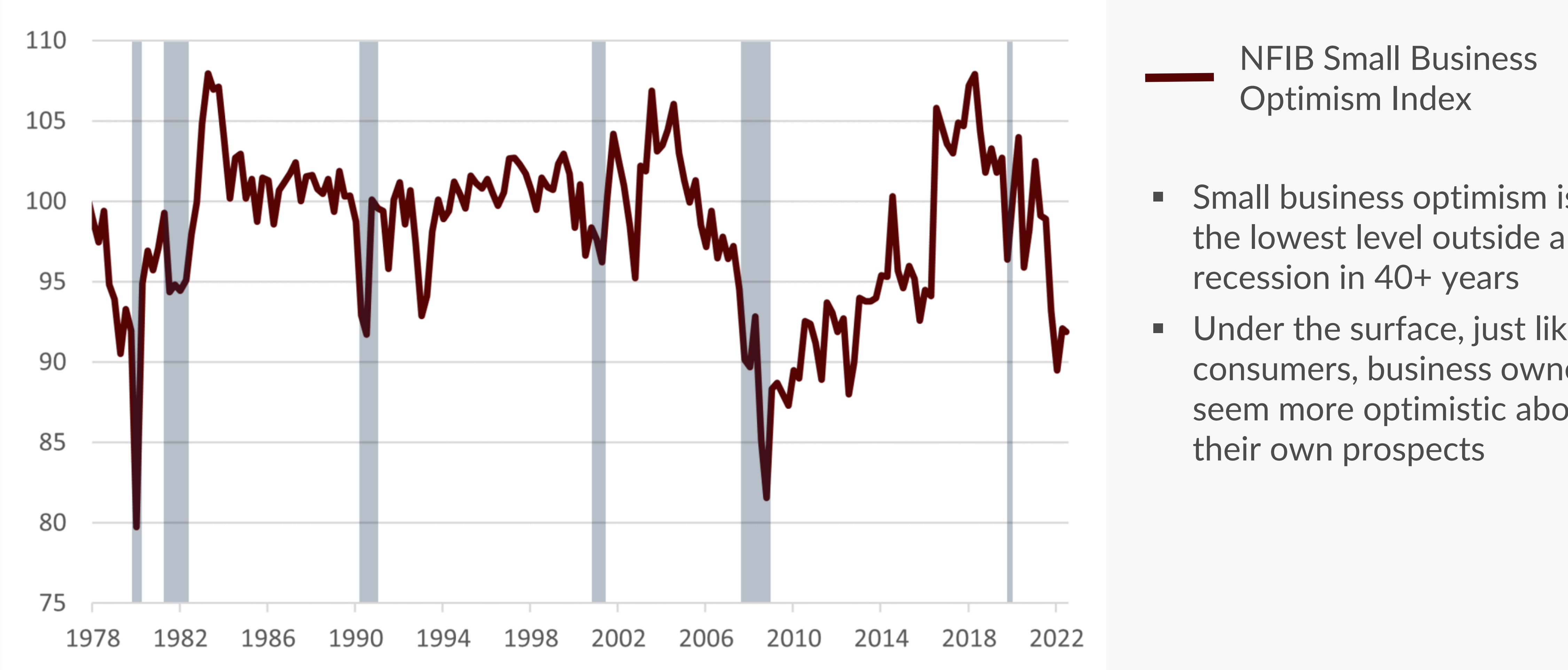
- Consumers are relating that they feel a lot worse than the data allows.
- Despite the top-line readings in this survey, consumers:
  - Think inflation is going to be lower a year from now
  - Their own financial situation will be better a year from now

Source: Bloomberg Finance L.P., University of Michigan

But consumers can hang on . . .

- Rents are still going up, but we seem to have passed peak housing unaffordability
- Consumers can handle the mortgage, the rent, and the credit cards
- As long as they don't lose their job

Business owners are not optimistic either



- Small business optimism is at the lowest level outside a recession in 40+ years
- Under the surface, just like consumers, business owners seem more optimistic about their own prospects

Source: Bloomberg Finance L.P., NFIB Small Business Optimism Index

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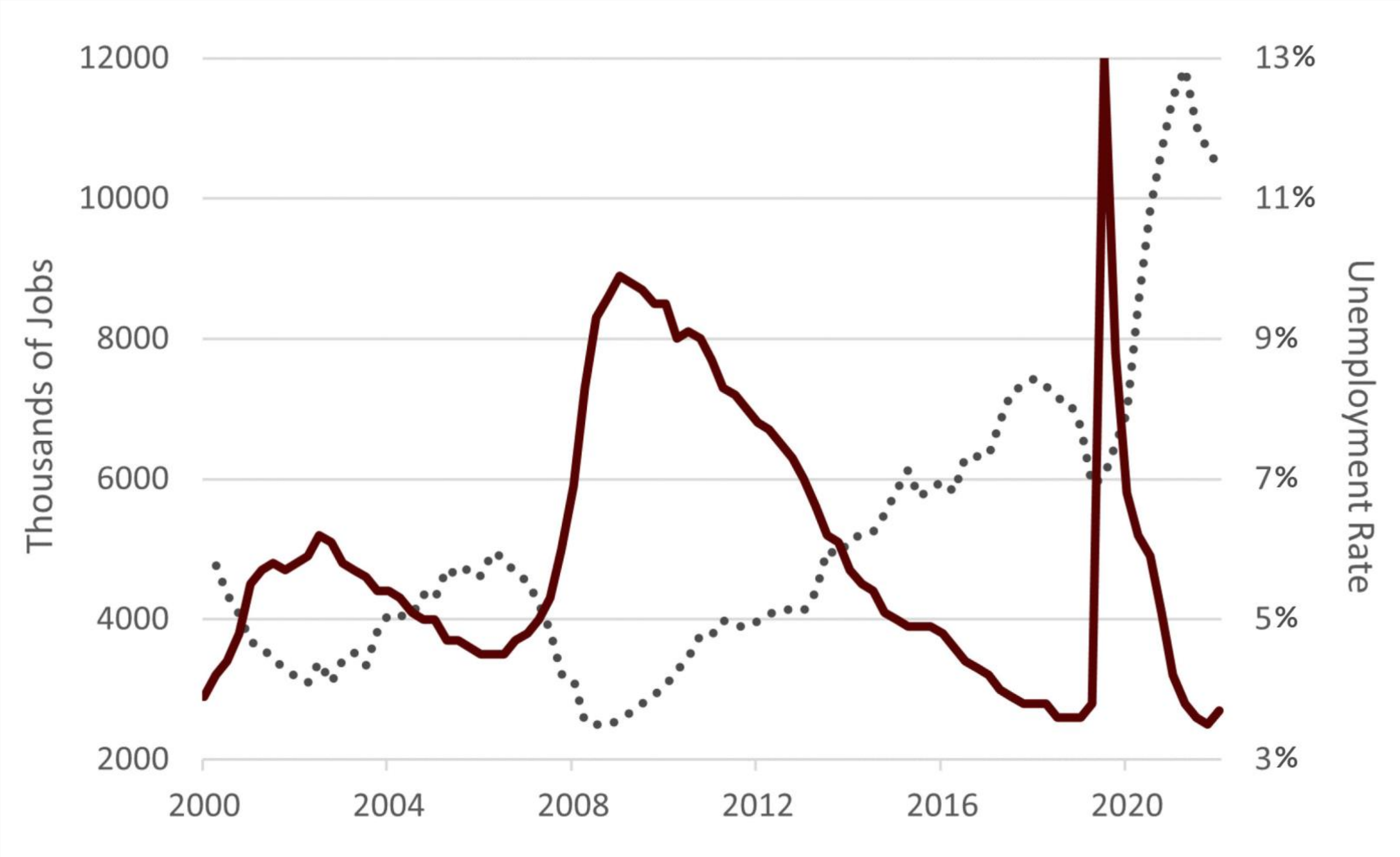
The job market is tight



U-3 US Unemployment Rate Total in Labor Force

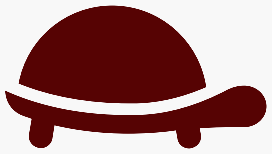
US Job Openings By Industry Total SA

- Employers are still looking to hire qualified employees
- Demographics contribute to labor market strains through aging and less immigration

Source: Bloomberg Finance L.P., Bureau of Labor Statistics

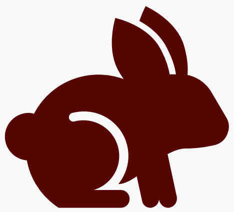
Fed policy

The Federal Reserve will continue to tighten monetary policy. Chairman Powell does not want a repeat of the 1970s when the Fed stopped fighting inflation too quickly and inflation got out of control.



Staying Tight

Recession Risk



Getting Loose

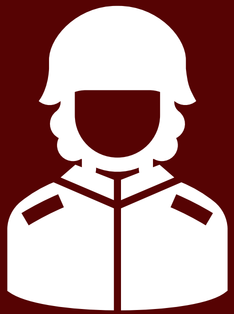
Inflation Resurgence

War in Ukraine

40 nations have committed to spending nearly 6.4% of their combined GDP

Refugee Cost: $21B

5 million refugees dispersed over Europe



Military Aid: $36B

Arms and ammunition from the US and other allies

Financial Aid: $116B

Total expended by Ukraine allies through November

Russian Cost: $82B

Approximate Russian cost through October

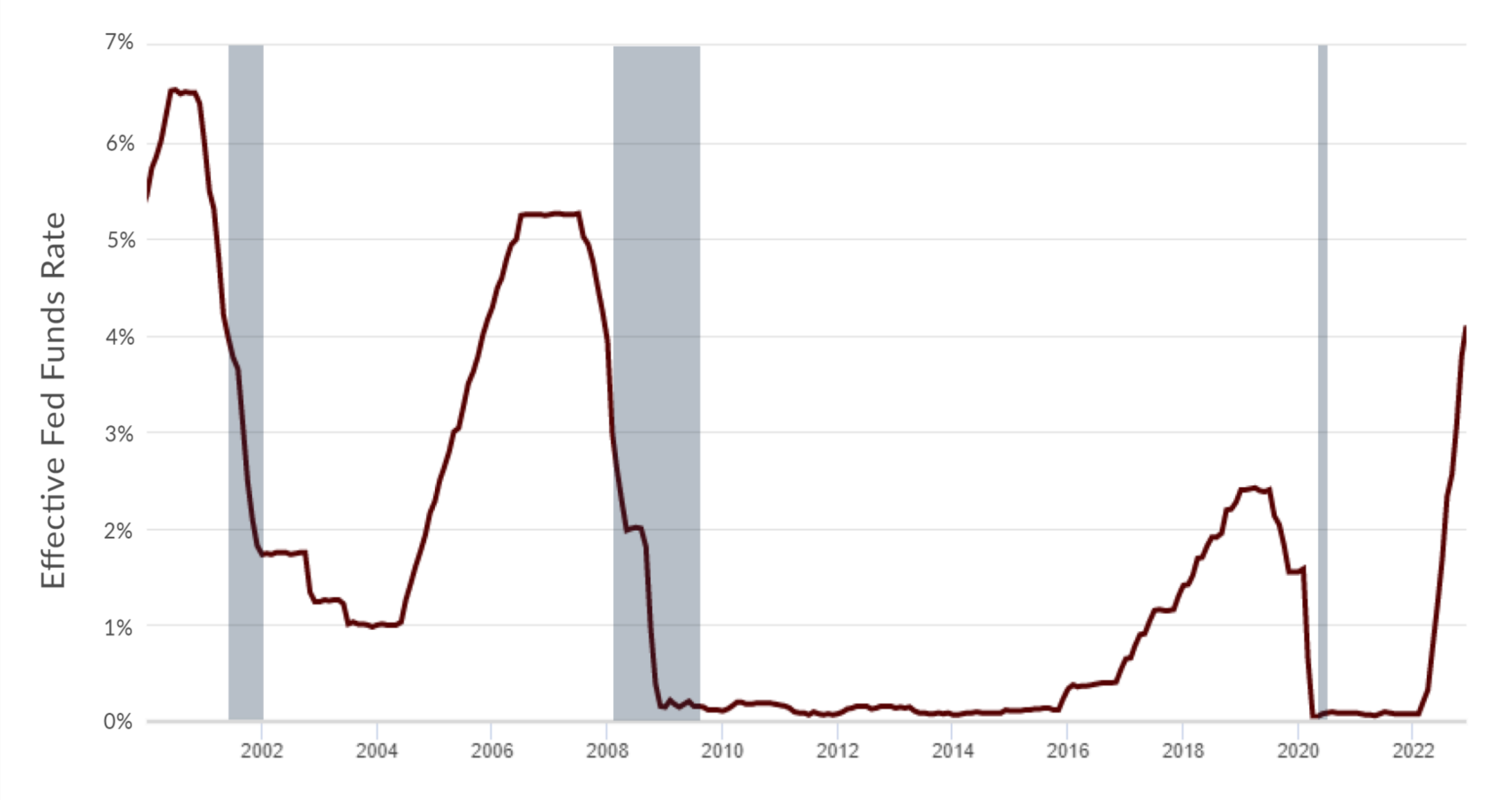
China is a black box

- Chinese PMI for manufacturing and services shows contraction
- Chinese inflation is reported to be 1.6% vs. much higher levels in the West
- A Chinese reopening might not be bullish

Where we may be going

Uncertainty is high. Recession is likely.

The Fed was very active



- The Fed has raised rates 7 times this year:

March	0.25%
May	0.50%
June	0.75%
July	0.75%
September	0.75%
November	0.75%
December	0.50%

- The current Fed rate now sits within a target range of 4.25%-4.50%

Source: Federal Reserve Bank of St. Louis, Board of Governors of the Federal Reserve System (US)

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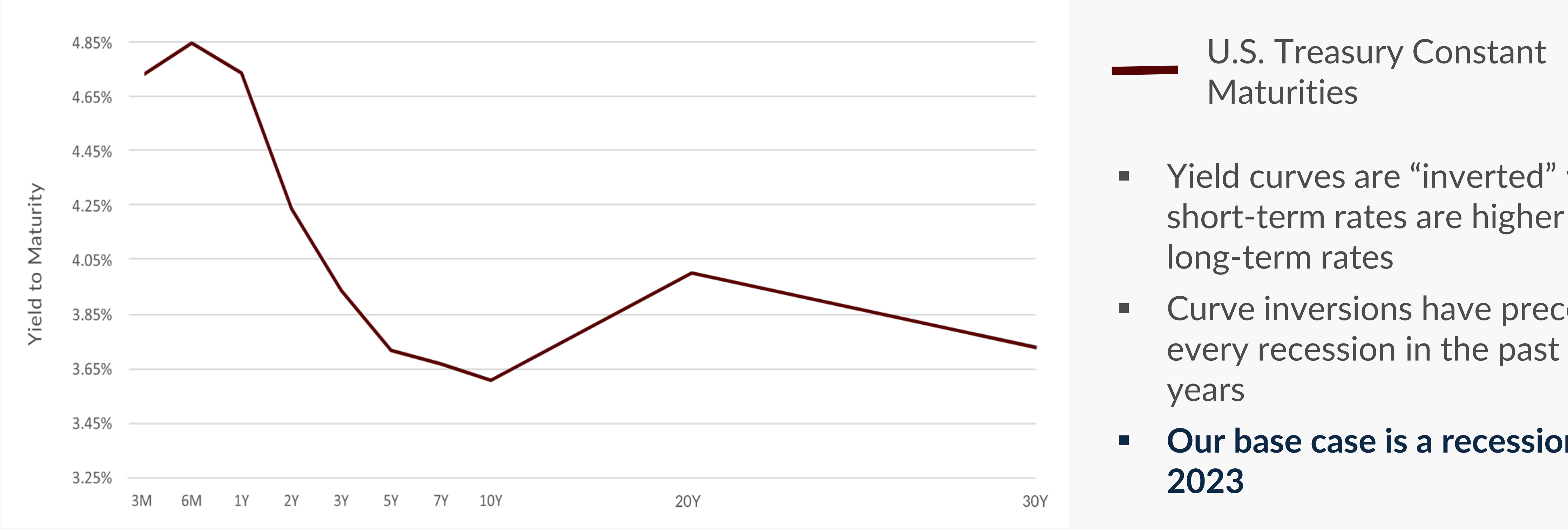
Inverted yield curve



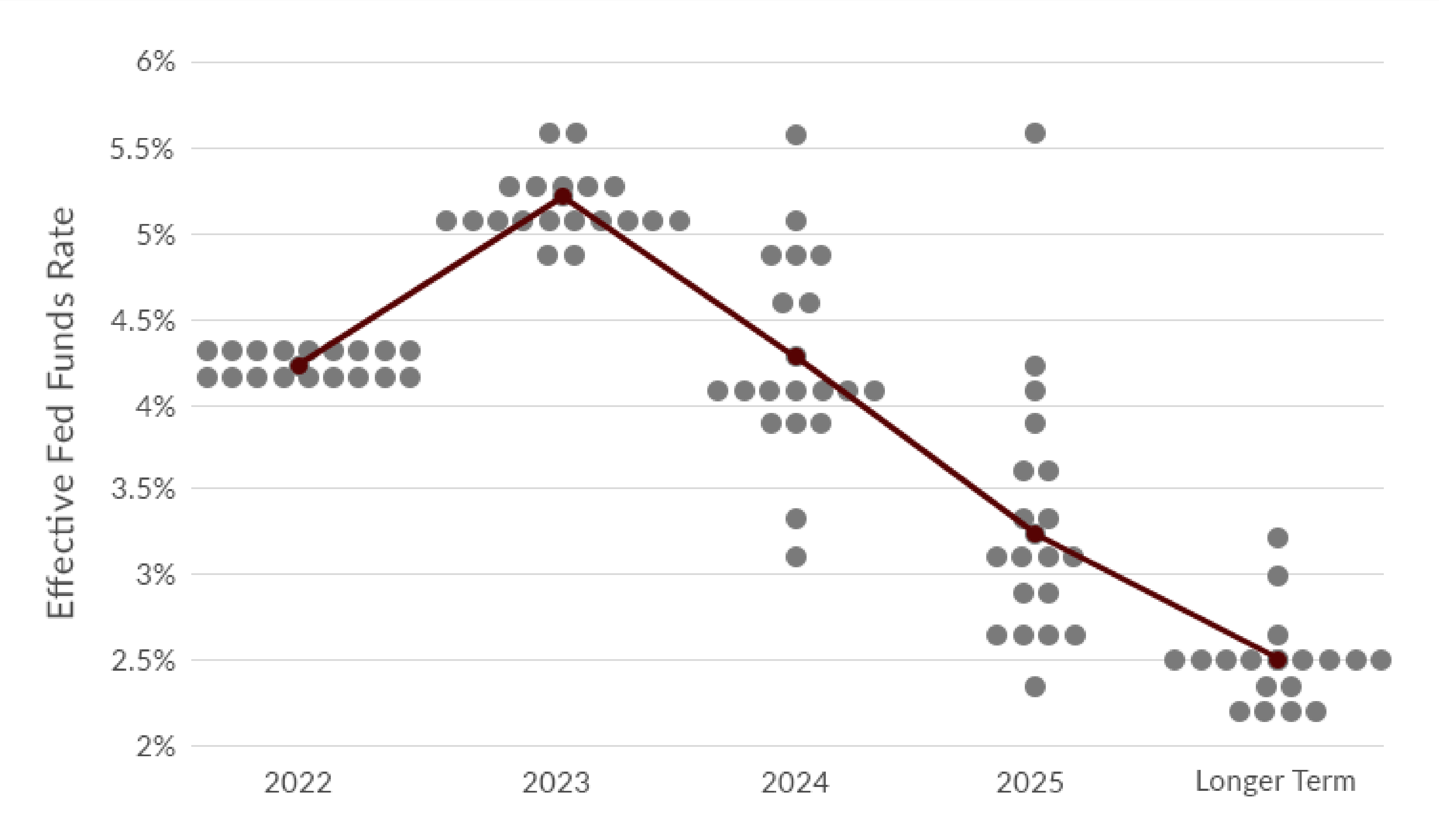
- Yield curves are “inverted” when short-term rates are higher than long-term rates
- Curve inversions have preceded every recession in the past 50 years
- **Our base case is a recession in 2023**

Source: Board of Governors of the Federal Reserve System (US), Treasury constant maturities, 2023 Jan 10

What happens to corporate profits?

- **Our base case: Recession is likely in 2023**
- Corporate profits decline or at least stop growing during a recession.
- Corporate profits may continue to rise or decline less because inflation is high.

What the U.S. Fed thinks



Source: Federal Open Market Committee (FOMC), Board of Governors of the Federal Reserve System (US)

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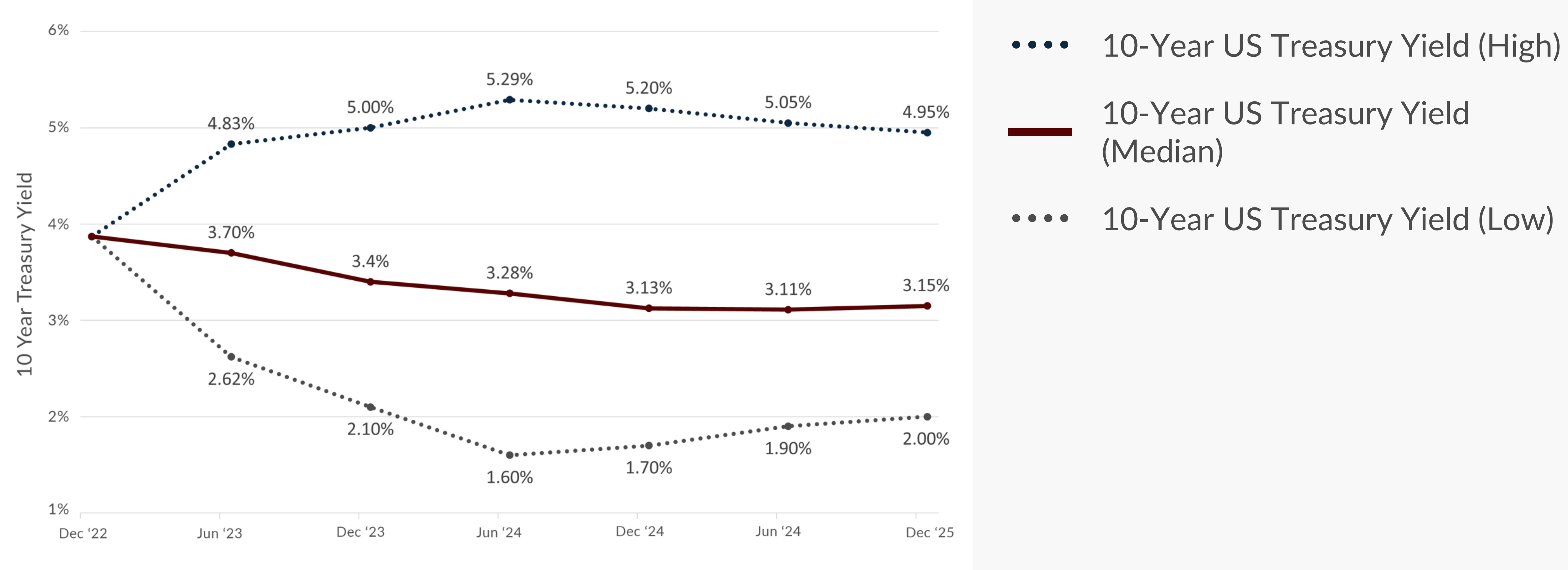
Economists seem uncertain about the future



Source: Wall Street Journal Survey of Economists, October 2022

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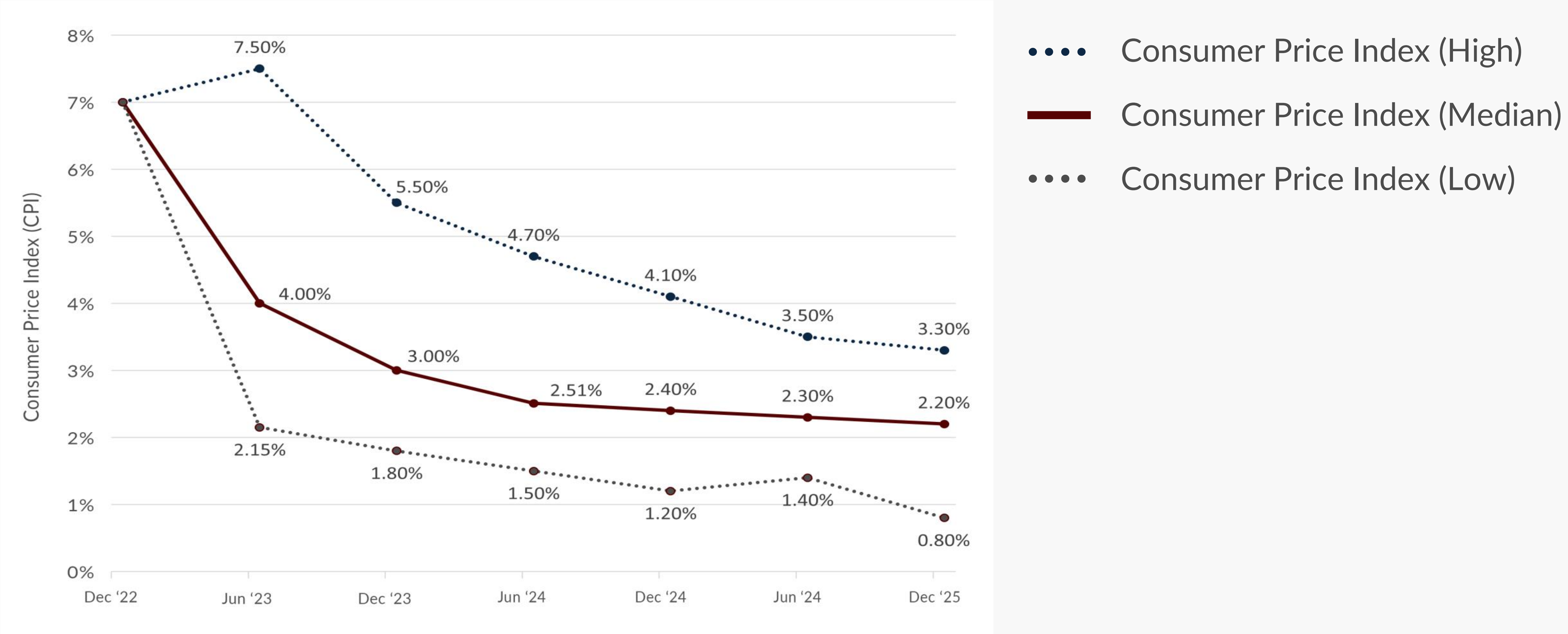
Economists think inflation is going lower . . .



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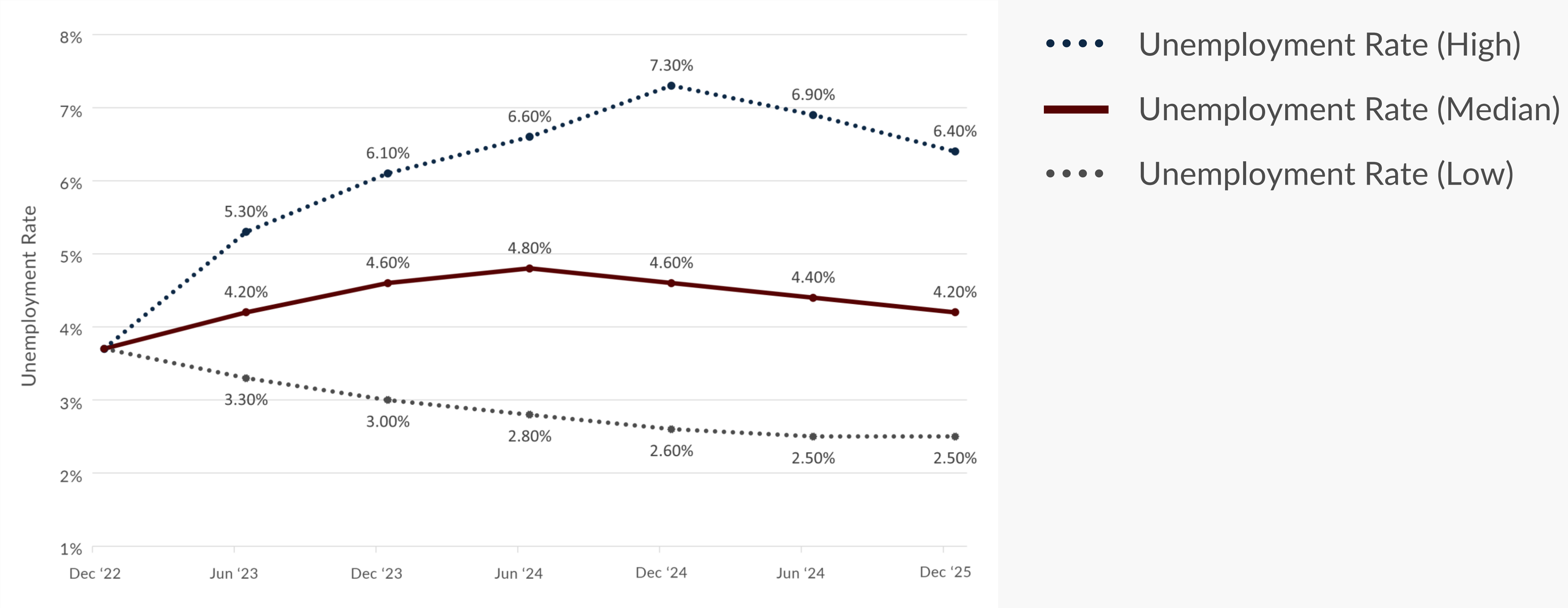
Without significant unemployment



Source: Wall Street Journal Survey of Economists, October 2022

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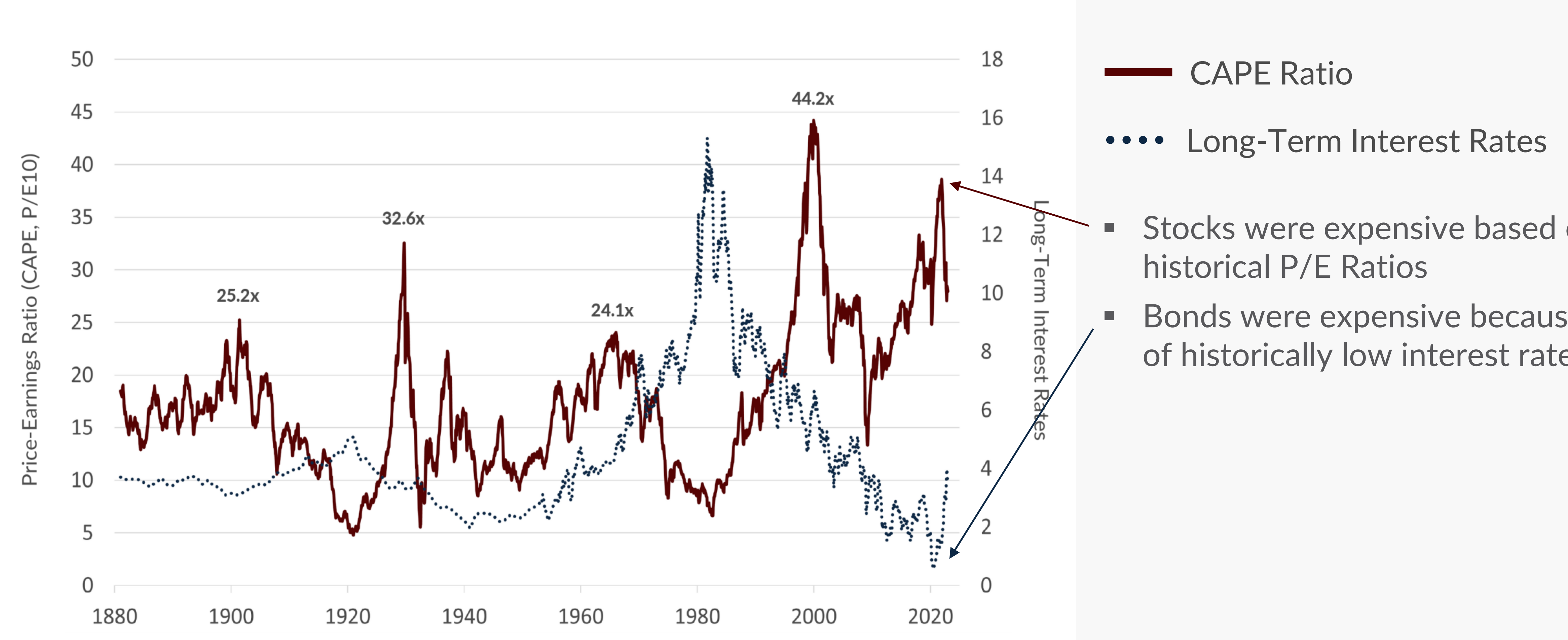
Valuations were historically rich



- Stocks were expensive based on historical P/E Ratios
- Bonds were expensive because of historically low interest rates

Source: Stock Market Data Used in "Irrational Exuberance" Princeton University Press, 2000, 2005, 2015, Updated

Asset classes were unusually highly correlated

	1973-Present	1973-74	1977-81	1993-94	1998-99	2012-13	2022
Large Stocks	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Small Stocks	0.78	0.76	0.82	0.83	0.76	0.87	0.95
International Stocks	0.69	0.62	0.41	0.67	0.80	0.79	0.91
Real Estate	0.62	0.90	0.67	0.38	0.56	0.49	0.90
High Yield Bonds	0.61	0.48	0.44	0.70	0.63	0.64	0.90
Investment Grade Bonds	0.36	(0.05)	0.30	0.74	0.21	0.06	0.74
Long Term Government Bonds	0.09	0.15	0.31	0.65	(0.19)	(0.49)	0.51
Intermediate Term Government Bonds	0.07	(0.05)	0.25	0.80	(0.10)	(0.08)	0.57
Precious Metals	0.05	0.25	0.19	(0.21)	0.11	0.25	0.26
Cash	(0.01)	0.03	(0.08)	0.05	(0.17)	(0.35)	0.08

Source: Bloomberg Finance L.P.

Violations of basic investing rules

If you can’t explain it, don’t buy it.

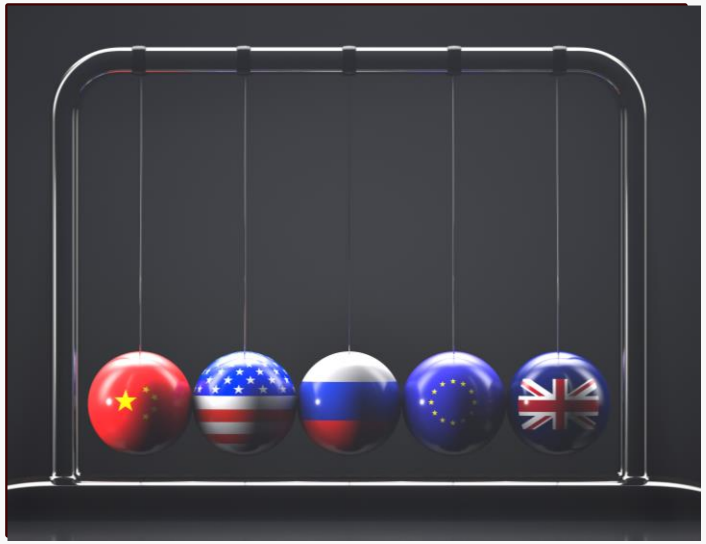
If someone is willing to pay you more than something is worth, sell it.

Unsustainable practices eventually end, sometimes abruptly and with substantial consequences.

What about foreign markets?

Structural changes in the U.S. and abroad that favor non-U.S.

Dollar weakness



Political stability, capitalism, and rule of law must reign supreme

Final thoughts

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"If you cannot control your emotions, you cannot control your money."

Warren Buffett

What should we do now?

1. US vs. International
2. Value vs. Growth
3. Short duration & high-quality vs. Long duration & low-quality
4. Have a plan

What’s new with you?

There may never be a more important time to work with a financial professional.

- New family member
- Wedding coming up
- Job transition

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Contact us

www.concordwealthpartners.com

276-628-5910

info@concordwealthpartners.com

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