Good morning. I am having elbow surgery on 9/22/22 so Mike Carilli is sending this note on my behalf. Wish me luck and I hope to be back in the saddle next week!

On Wednesday, September 21st, as expected, The Fed moved up the short-term overnight borrowing rate, The Fed Funds, by .75%. This was widely expected which is why the market initially bounced higher off the news. Then Powell's Press conference came where the Fed announced the Terminal Rate (I've mentioned this before – this is where they want to go with rates) to 4.62% and a higher year-end rate which effectively boxes them in for a possible .75% increase in November & .50% in December. Could this change based on the economic date that comes in between now and then? Absolutely. The Fed has changed course several times over the last year so there's nothing to say they won't be data-dependent going forward.

So does this change anything going forward? As I mentioned in my note earlier this week, due to the higher than expected core inflation data, a major earnings pre-announcement and the market breaking a key trend-line, we did change our near-term outlook on equities and reduced our exposure to U.S. Growth. The Fed decision does not change anything from here but here are the main takeaways:

- Fed Funds/Short Term Rates will settle around 4.5% from the 3%-3.25% they are at today.
- Most of the heavy-lifting has been done for rates – we are over halfway through this rate-hike cycle.
- The effects of these rates have not been fully absorbed by the economy.
- Economic growth will slow down but so far this year both corporate earnings and economic growth has surprised to the upside.
- We will be laser-focused on economic data and earnings going forward.
- Employment remains strong but we do expect the labor market to soften up in 2023 and the unemployment rate to increase which will subdue inflation data,
- We will continue to watch various market trend lines going forward and make adjustments along the way per our investment discipline. We will not make emotional or gut-decisions.
- See some of my thoughts on the economy in an interview given earlier this week: https://www.investmentnews.com/as-fed-battles-inflation-financial-advisers-brace-for-recession-fallout-226715

The flip-side of the glass half-empty argument is that the market has now already contracted significantly and we are now on-track for the worst year for both stocks & bonds ever. That is correct, the worst year ever. Going forward, that means things will be different. Unlike in the past, bonds have competitive yields now which are actually looking like they could be a buy. We also anticipate longer duration bonds to peak before short-term rates so we may be seeing an opportunity to lock in some of these higher yields. The longer term picture still points to a structurally lower interest rate environment for quite some time due to debt and demographic trends. Stock & bond correlations have been very high this year (hence our attraction to asset classes like Managed Futures) but going forward they should decouple. Market multiples are coming down, especially in some of the formally high-flying sectors like tech and growth. That will turn into an opportunity for which we have dry powder.

We are monitoring our portfolios and allocation with a very watchful eye. The market has been challenging this year but we have tried to stay in front of things and be as proactive as possible. As always, please reach out to me directly with any comments or questions.

Regards,
Tim

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