

AUGUST 2022

## MORAN MONTHLY DIGEST

### Insights From Our Founder

Dear Clients,

I hope you enjoyed the summer season—whether that be relaxing, traveling, or spending quality time with family and friends. At MWM, we had our busiest summer to date working on our conversion to becoming a Registered Investment Advisor (RIA). I'm pleased to announce that as of last Friday, August 19th, the conversion is complete, with all team members, myself included, having transitioned to the BNY Mellon | Pershing Platform. I would like to express my sincere gratitude for your patience during this process. As we enter this new chapter as an independent firm, I'm humbled by your loyalty. I couldn't be more excited for what the future holds. This milestone reaffirms our commitment to offering industry-leading investment solutions and personalized customer service that always puts you, our clients, first and foremost.



Thomas M. Moran AIF®  
Chairman | CEO | CIO

This summer, the markets continue to be at the mercy of the Federal Reserve and inflation readings. After reaching a bottom in mid-June, stocks rallied upon softer-than-expected CPI data. Speculative investors are betting Jerome Powell will not raise interest rates in September as inflation shows signs of waning. Conversely, we believe this optimism is short-sighted. CPI data marginally decreased in July primarily due to declining oil prices, which dropped 7.7% compared with June. Because inflation remains abnormally high across most categories, we believe the Federal Reserve will stay the course and raise interest rates in September. We recommend our clients remain invested as we believe there could be a rally during the fourth quarter. Our economic commentary explains why we believe this is the case.

As always, please contact our office if you have any questions or if we may be of help in any way. It is our privilege to be of service to you and your family.

Cheers,  
Tom

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## ECONOMIC COMMENTARY

### Mid-year thoughts on the market

The Summer is often a time to relax and recharge the batteries. The global markets, however, completely missed this memo. The first six months of 2022 were the stock market's weakest start to the year since 1970. The S&P 500 had dropped 23% YTD as of June 16th, and the technology heavy NASDAQ dropped 32%. Since then, the market has rallied, recouping over 50% of its losses. Given the intense roller coaster ride in the markets so far in 2022, we thought it would be helpful and instructive to take stock of where we are today and where we may be headed.

### The Fed and Inflation

Inflation, a word not used in almost 40 years, is front and center as it dominates the news cycle. In June, the Consumer Price Index (CPI) hit a 41-year high at 9.1%. This acceleration is even more staggering when considering that inflation was just 3.9% in 2020 and 2.3% before the pandemic hit. Market sentiment turned extremely negative in Q2 as investors digested the stark possibility that the Fed had lost total control of inflation, precipitating the almost 24% drop in the S&P 500 from early April through mid-June. Since then, inflation has ticked down slightly in July to 8.5% as prices showed signs of cooling but remain near record highs. This led to a strong market rally since June 16th, particularly in technology stocks and speculative lower-quality companies. Investors are betting the Fed will make a dovish pivot and not raise rates in September. However, we believe this optimism is likely premature, and the Federal Reserve will continue its hawkish hike cycle as it tries to tighten financial conditions to tame inflation.

How this 40-year inflation problem arose is rather simple: too much demand chasing too little supply. Congress released \$5 trillion of fiscal spending to keep the economy open, businesses from failing, and provide aid to families during the pandemic. In addition, the Fed expanded its balance sheet from \$4 trillion to \$9 trillion over a 2-year period. We overstimulated demand at a time when supply chains were struggling to reopen after having been shut down on a dime due to the pandemic. Making the problem more acute was a chronically undersupplied housing market that led to increased house and rent prices, and the Russian invasion of Ukraine, which crippled the energy and agriculture markets and sent prices soaring. Many of the inflationary signs were obvious in the Fall of 2021, but up until November, Jerome Powell insisted inflation was "transitory." Clearly, in hindsight he was wrong.

The extraordinary \$10 trillion of fiscal and monetary stimulus, in addition to \$3 trillion of pent-up household savings created a post-pandemic consumer buying and travel party that has had far-reaching consequences. Since November, the Federal Reserve has battled to regain the confidence of the consumer and the investor. The seven Fed governors, including Jerome Powell, have spoken regularly on the talk show circuit and at various public economic conferences to reiterate that even though inflation is high, it is a monetary phenomenon that can be tamed with appropriate Fed actions.

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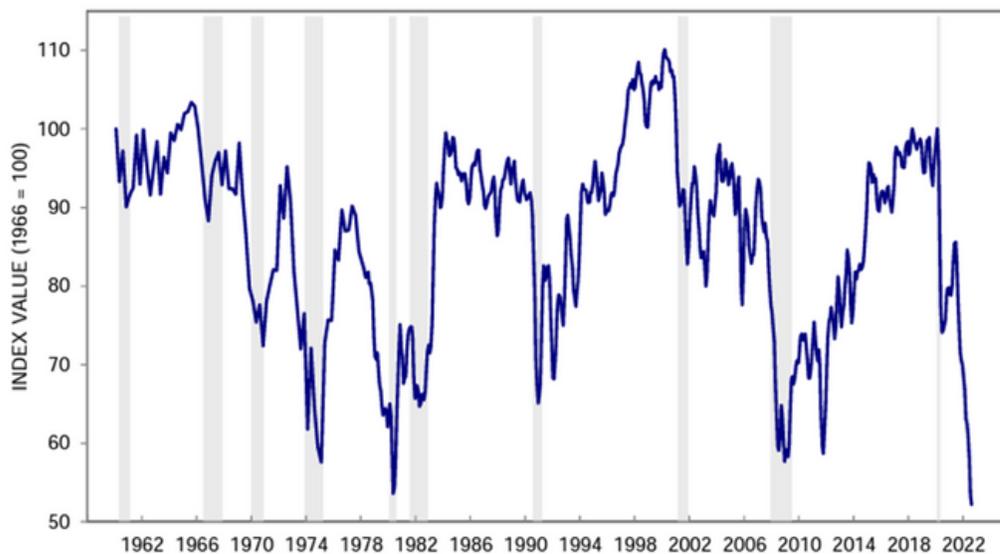
The Federal Reserve has two tools to tighten economic conditions and cool down demand. (1) the Fed can raise the Fed Funds rate, which guides many other benchmark rates; or (2) they can begin selling treasury bonds and mortgage-backed securities from their enormous balance sheet back into the open market, increasing longer-term market interest rates. The trick of course is not to have unemployment spike and catapult us into a nasty recession as they tighten.

### GDP and Recession

Economists almost unanimously agree a recession is inevitable but remain divided over whether we are in one currently. GDP declined 1.6% in the first quarter. In the second quarter, GDP contracted 0.9%. This would meet the common definition of a recession—two consecutive quarters of negative GDP growth. It is the National Bureau of Economic Research, however, that is ultimately responsible for making this call months down the road. Compared to the 12 prior recessions since WW2, there is one major component missing: high unemployment. At an unemployment rate of 3.6%, with only 5.9 million people looking for work and 10.7 million job openings, it certainly doesn't feel like a recession even if the data tell us otherwise. In fact, the US added 528,000 jobs last month.

Meanwhile, rising prices across all categories and higher interest rates have started to wear on consumer confidence, amplifying the possibility of a recession. Indicators like the University of Michigan Consumer Sentiment posted a July reading of 51.5, the lowest reading since the survey's inception.

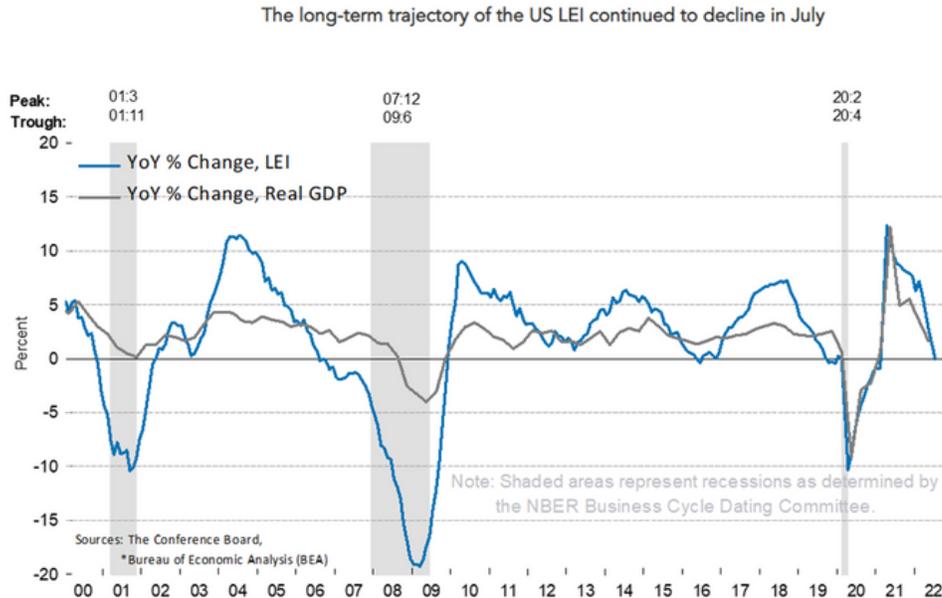
THE INDEX OF CONSUMER SENTIMENT



Additionally, we would be amiss if we did not mention one of the most reliable economic indicators—the inverted yield curve. Historically, when short-term interest rates trade above longer-term bond yields, a recession almost always follows. The 3-month and 10-year yield inversion has predicted the last eight recessions consecutively. So far, the spread remains positive but is narrowing.

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Meanwhile, the 2-year and 10-year yield curve—a less reliable but still widely followed leading indicator—has been inverted since early July. This inversion has predicted the last 5 out of 6 recessions with an average lead time of 19 months. Therefore, we believe a recession at the end of 2023 or early 2024 has become a distinct possibility.



We are closely monitoring for signs of a recession because its magnitude can determine the severity and length of the current bear market. Fortunately, we believe the potential recession may be relatively mild as the debt levels (leverage) on corporate and consumer balance sheets remain moderate, the consumer is in better shape than in prior downturns, and unemployment is starting at much lower levels. Therefore, we would expect the potential recession to be akin to the 1990 recession where GDP dropped only 1.4%. It is important to remember that markets are forward-looking. They price in the risk and the magnitude of the recession 9-12 months before it even begins. Of the last 12 recessions, the stock market experienced an average decline peak to trough of 25-30% ahead of those recessions. This year, we have already experienced a 23% downturn in the S&P 500, so have already flirted with the historic averages of a bottom.

### Earnings and Valuation

When investing, it is easy to forget that the stock market is just a basket of companies. Companies generate revenues and earnings. If you own companies whose earnings are dependable, grow, and generate cash to pay dividends, the stock price will move higher over the long-term, keeping the valuation constant. Stock prices over the long term always follow earnings. Always. That is why so many analysts are employed to follow company earnings. Generally, if you get the earnings right, you will get the direction of the stock. The long-term chart on the next page illustrates this.

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By now, most S&P 500 companies have reported their second-quarter earnings and shared their projections for the future. By in large, reports came in mixed but better than feared, with over 77.8% coming in above analyst estimates. End demand is still rather strong, but there is rising corporate caution. Jamie Dimon of JP Morgan summarized the current mood best: “Geopolitical tension, high inflation, waning consumer confidence, the uncertainty about how high rates have to go and the never-before-seen quantitative tightening and their effects on global liquidity... are very likely to have negative consequences on the global economy sometime down the road.”

In terms of valuation, the S&P 500 currently trades at a price-to-earnings ratio (P/E) of 17x, down from the market highs last year of 22x. To keep it all in perspective, the market has historically traded at 16x forward earnings.

## WHAT DOES THE FUTURE HOLD?

We are now 8 months into a bear market. The million-dollar question is how long this downturn will last and what the prognosis is. We can harp on the past, but all that matters is the future. The market has already priced in a lot of negative. Bearish sentiment is at an extreme. The prices of copper, base metals, gasoline, lumber, grains, coffee, OJ, and many other commodities have rolled over and are declining. Consumer expectations of future inflation has pulled back significantly. Earnings are already being reset lower. Much of the speculative excess in unproven assets such as Special Purpose Acquisition Companies (SPACS), meme stocks, and unprofitable technology companies has been pummeled. Retailer surveys of pricing power are plunging. Layoffs at companies are beginning. Even the white-hot housing market is showing cracks. Existing home sales have fallen recently for 6 straight months to 4.8 million Seasonally Adjusted Annual Rate (SAAR), down from the 6.6 million peak during COVID-19. With this much extreme pessimism, it certainly would not take much to mark “the bottom.”

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### **Scenario 1: What could go right to end the bear market?**

1) Inflation caused the market downturn and will ultimately drive the rebound. The Bureau of Labor and Statistics releases Consumer Price Index (CPI), Producer Price Index (PPI), and Personal Consumption Expenditure (PCE) data every month. It will likely take several years to get anywhere near the Federal Reserve's desired 2% rate of inflation. The market, however, will start acting favorably as CPI reports continue to be less negative. With everything but rent prices falling at the moment, this outcome seems likely at some point this Fall.

2) Raising interest rates is the Federal Reserve's main tool to tamp down demand and rein in inflation. As we progress down the Federal Reserve's rate hiking cycle into the Fall, we will get a sense of their stopping point. Currently, the market futures are pricing in a terminal rate of about 3.6%, which it could achieve by early 2023. If the Fed Fund rate rises closer to 3.0% by the next Federal Open Market Committee (FOMC) Meeting in late September and Jerome Powell instills confidence that rate hikes are coming to an end, the market would react very positively. The "post rate hike" playbook could then be dusted off. This seems very plausible in the late Fall.

3) Second quarter earnings generally came in above estimates. Guidance for future quarters came down only marginally. The market had expected greater deterioration. The real question will be how well earnings hold up in the future. Third quarter reporting season will be very important. The deeper the recession, the deeper the earnings cuts. Again, stocks always follow earnings over the long haul.

4) The seasonals are in your favor. According to S&P Global, Q4 of any year is the strongest. In fact, since 1945 the average gain in Q4 is 3.8%, rising 77% of the time. The worst month of the year is September. After September we believe we will be better poised for a rally into the back part of the year.

5) Elections matter and have consequences. The country is headed into midterm elections in November. As it stands now, the chance for a split Congress looks rather certain with Democrats now having a 61.19% chance of maintaining their majority in the Senate and the House looking to flip Republican. This is good for the market as it historically prefers gridlock. The less intervention, the better.

### **Scenario 2: What could go wrong to cause the bear market to live on?**

1) If inflation remains high and we fail to see material drops in CPI, PPI and PCE, this bear market will continue. A 1970s-like inflationary environment and psyche would be awful. As a reminder, the stock market in the 70s went through a terrible 10-year bear market where we saw inflation and unemployment soar while growth stagnated. Many are making comparisons to this decade. That is not our perspective. In the 1970s, the Federal Reserve was met with fierce resistance to any notion of raising unemployment. We believe that today the Federal Reserve and Jerome Powell are prepared to take the necessary steps to bring down inflation even if that means raising unemployment.

## ECONOMIC COMMENTARY

2) If the Federal Reserve raises interest rates too aggressively, the consumer and the economy will suffer, and corporate earnings will come down as we head into a recession. The bear market will live on.

### CONCLUSION - WHAT TO DO?

In no shape or form do we expect a repeat of the inflation we saw in the 1970s. It will take time to cure the economy shattered by a global pandemic and the hangover from the \$10 trillion of US stimulus and \$25 trillion of global stimulus. The good news is that our Federal Reserve recognizes inflation is a problem and is working to course correct their delayed response to bring price growth down. Unfortunately, this is going to take time to achieve. We believe it will take at least 2-3 years for the Federal Reserve to lower inflation to anywhere near its objective of 2%.

We think the next couple months will continue to be choppy surrounding speculation over the Fed's interest rate hike trajectory. We are cautiously optimistic that we will start to see Scenario 1 play out during the 4th quarter—meaning we will start to see movement out of this bear market. We think Scenario 2 is possible, but a long shot. As painful as this bear market has been, we believe it is prudent to ride out the storm. If companies in the United States use their human capital and technology to innovate, expand, and increase their productivity, their sales and earnings will grow. It is what we have experienced since the creation of the first stock market in 1792. If earnings grow, stocks will follow.

We recognize the future faces many headwinds (inflation, recession, divisive politics, large federal debt burdens, etc.) and believe the next decade will be more challenging for the markets than the last. Frankly, the 14% Compound Annual Growth Rate (CAGR) over the last 10 years was exceptional, but not the norm when the annual average is closer to 8-9%. We think it would be wise to recalibrate a little and accept annual returns in the range of 7-8%. That still allows for acceptable withdrawal rates and is why we recommend staying invested. We favor more defensive and conservative styles at this part of the cycle like value and dividend-oriented equities. We believe investing is a long-term and disciplined process. Even though this is a confusing and nerve-wracking time, it is prudent to stay invested and not try to time the market.

Charles E. Chesebrough, Jr. CFA®  
Senior Vice President



## WHAT'S NEW AT MORAN WEALTH MANAGEMENT®

### **BROADRIDGE - CLASS ACTION SERVICES**

We are excited to introduce a new client benefit offered through Broadridge Financial Solutions - Class Action Services.

As you may be aware, security holders are occasionally entitled to cash settlements through class-action lawsuits. Oftentimes, the distribution check per person comes out to only a few cents, making the inconvenience of manually submitting the paperwork hardly worth the trouble. Fortunately, we have partnered with Broadridge to streamline this process end-to-end.

On behalf of each individual client, Broadridge will monitor and identify any eligible class action suite, then file the claim for you automatically, saving you the trouble of submitting the paperwork manually. Broadridge files, monitors, and expedites the payment distribution compliant with SEC guidelines. Broadridge retains 20% of any successful settlement as compensation for the services provided. The distributions, less the 20% contingency fee, will be directly deposited by Broadridge into your accounts at our custodian Pershing.

Clients are automatically included in this service but may opt-out at any time by calling us at [239.920.4440](tel:239.920.4440). If a client opts-out, MWM and Broadridge will not monitor class action filings for that client. We believe that our clients will have great benefit from using Broadridge to minimize the risk of any missed settlement opportunities.

# WHAT'S NEW AT MORAN WEALTH MANAGEMENT®

## **CLIENT UPDATES - INTERNAL OPERATIONS:**

We believe one of the benefits for you as a client at Moran Wealth Management® is the strength of our team. If your primary contact is unavailable, we welcome you to speak with any other qualified team member. Any associate can provide the exceptional service to which you are accustomed. We appreciate your patience during our conversion to becoming a Registered Investment Advisor.

Please confirm, if you have not done so already, to:

- Establish Online Access
- Enroll in Bill Suite
- Verify that your statement linking is to your preference

Each of these tasks can be completed by one of our Client Relations Associates in just a few minutes by calling our office at [239.920.4440](tel:239.920.4440).

In addition, as we are transitioning your assets and funding your accounts custodied at Pershing, you may receive any of the following paper or email notifications as part of your initial enrollment in these features:

- Enrollment of periodic consolidations & periodic distributions of funds; your monthly distributions
- Standing and Periodic Automated Clearing House (ACH) instructions
- Disclosures and Privacy Statements
- Prospectuses
- Proxy Voting Notices

If further action is needed on your part, a Moran Wealth Management® Associate will contact you by phone or email.

Please note that you will no longer have access to your Wells Fargo brokerage accounts once the accounts are no longer funded. Former Wells Fargo clients are required to call and request any historical documents from Wells Fargo Advisors at [1-866-281-7436](tel:1-866-281-7436). If you have any questions or inquiries regarding your checking account, you may also contact Wells Fargo's customer service at [1-800-869-3557](tel:1-800-869-3557) or visit a Wells Fargo branch to speak with an associate in person.

# PHILANTHROPY



## **FEATURED CHARITY**

Philanthropic giving is one of the many ways we can make a difference in our community. At Moran Wealth Management®, we are privileged to have served over 30 charities and counting through financial donations and volunteer efforts.

We seek to bring awareness, advocacy, and resources to those in need. Today we would like to highlight Child's Path.

Child's Path aims to support early childhood education in Southwest Florida through tuition assistance for children in low-income families. Serving nearly 400 children yearly, The Bright Path's Scholarship Fund has helped children receive high-quality education and care. Early childhood education aids in cognitive, physical, and emotional skills, ensuring a successful future.

To learn more about this organization, please visit <https://www.childspath.org/>.



[Click to play video](#)

# WELCOME TO THE TEAM

## **Gavin Schell - Investment Analyst**



Gavin Schell earned his B.S. in Finance from Florida Gulf Coast University where he was a member of the school's Student Managed Investment Fund. He also previously spent six years in the United States Naval Sea Cadet Corps.

A native of Irvine, California, Gavin holds dual citizenship in New Zealand. On his inspiration to achieve a career in finance, he abides by the quote from Benjamin Franklin that "An investment in knowledge pays the best interest." Gavin is proud to volunteer at FGCU's Wasmer, Schroeder, & Company Bloomberg Terminal Laboratory and serves as role coordinator of the Bloomberg Lab volunteers.

## **Christian Pineda - Client Associate**



Christian Pineda is a graduate of Florida Gulf Coast University, where he earned dual bachelor's degrees in Accounting and Finance, with a concentration in Analysis and Management. He previously spent eight years with the United States Marine Corps as a CH-53E Crew Chief Sergeant.

Christian is a native of Somerville, New Jersey. During his time at FGCU, he served as a police officer for four years with the on-campus department. Christian is also a trained dancer with a background in salsa, merengue, and bachata. In his off time, he volunteers as a youth wrestling coach, after having previously spent five years as an assistant high school coach.

# MORAN WEALTH MANAGEMENT®

## CENTER FOR FINANCIAL EDUCATION

### UPCOMING SEMINARS

We look forward to hosting many more educational events in the near future and welcoming you into our newly renovated space!

Visit our website for future dates [www.moranwm.com](http://www.moranwm.com).

Please feel free to call us to schedule a private meeting:

[239.920.4440](tel:239.920.4440).

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