

Kenneth A. Gilpin CFP

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# Sound Investments Inc.

4th Quarter 2022

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DJIA 33147.2 S&P 500 3824.3 Nasdaq 11080.6

## Summary

Blackrock, the world's largest investment manager, believes the world is in a new regime. It warned that they expect inflation "to cool but stay persistently higher than the central bank target interest rate of 2%. Blackrock presents two big arguments supporting this world view. The first is that a progressively aging population results in a reduced workforce, which increases labor bargaining power and hence inflation. Over the last 20 years China's workforce was integrated into the world economy which keeps prices down. But now, due to their one child policy, China, has an older population as well. The 2nd argument is that the world is pulling back from globalization. The war in the Ukraine has pitted the Western democracies against the Communist world again. The world is tending to revert back to the old economic and financial blocs. This will higher interest rates and inflation, making long term bonds a less attractive investment.

I attended a meeting sponsored by The Financial Planning Association. The speakers thought there was a 70% chance of a recession but they believed it would be mild.

*This investment letter is mailed quarterly to our clients and friends.*

## Enduring the Cool Down

Last January, I started rebalancing the portfolios and moving from stocks to cash and it was a good thing as the S&P 500 had it's worst first half of the year since 1970. For the entire year, it lost a fifth of it's value and was down 18.2%. The Dow Jones Industrials was among the best performer but was still down, losing 7%. The shine came off large cap growth, particularly technology as the technology-focused Nasdaq sank 32.6%. (see chart on back of this page)

Gains were hard to come by. Even Bonds failed to provide much protection with the Bloomberg's Aggregate Bond Index down over 13%. Overseas wasn't much better. The main European Index slumped -14.2% in 2022, a year marked by increasing interest rates and the war in Ukraine. Emerging Markets also sank just over 20%.

In our quarterly client letters in December and March we discussed moving to cash and switching to value funds which help reduce loses. Also, most clients bought government guarantee CD's paying over 4.5% for 6 months.

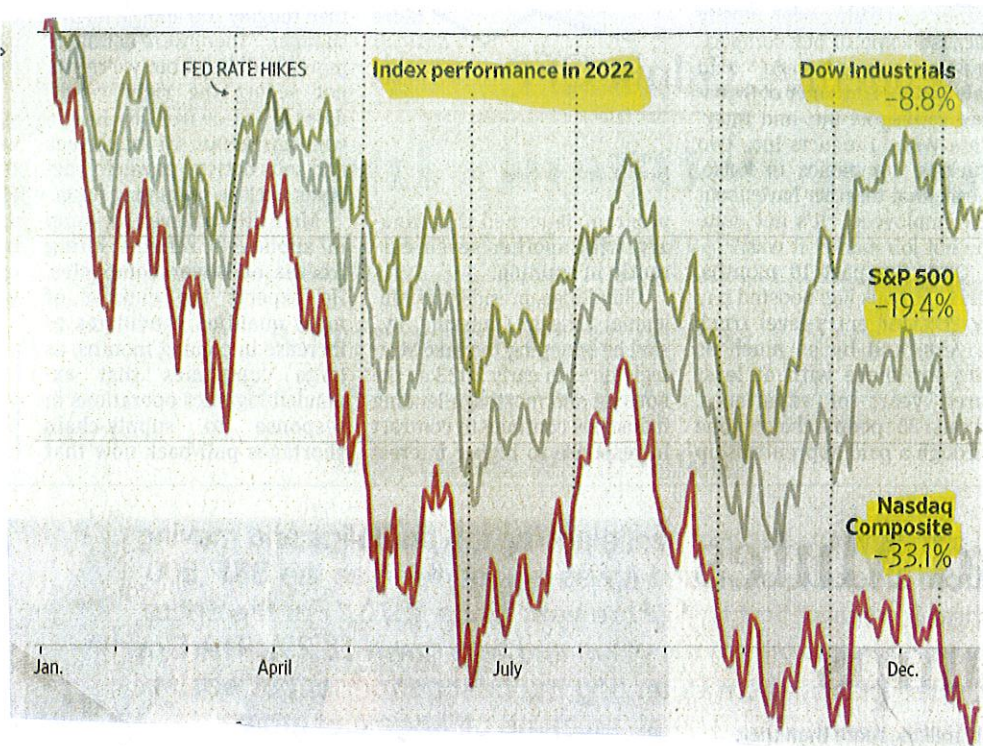
Next, we will discuss concerns over inflation, interest rates and a looming recession.

## The Elephant in the Room

U.S. inflation eased for the 6th straight month but the price of goods or inflation rose 6.5% from a year earlier. This is down from a peak of 9.1% in June. Not to confuse anyone with the numbers, but over the last 3 months, prices have increased only by 2.1%. The elephant in the room refers to the Federal Reserve Bank and its leader, Jerome Powell. He wants to bring inflation down to 2% and his weapon of choice is to raise interest rates to slow down the economy.

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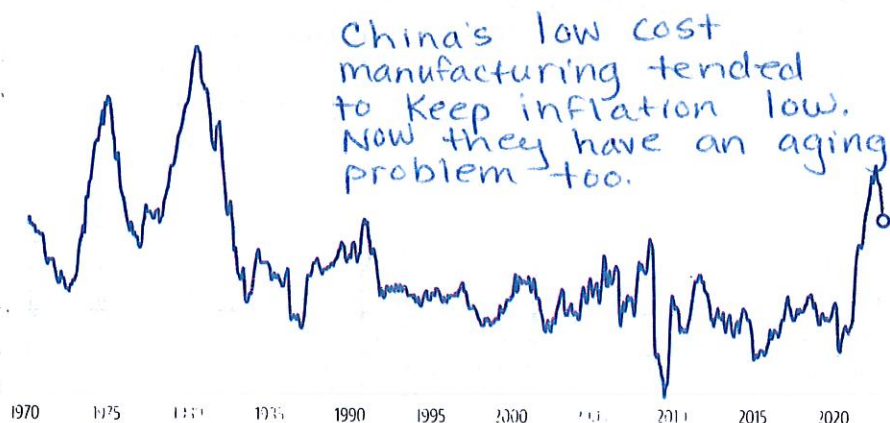




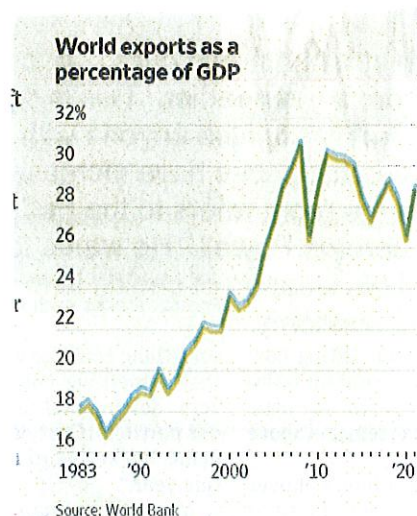
Stocks log their worst performance since 2008.

All 3 Indexes were down

### U.S. CONSUMER PRICE INDEX, YEAR-OVER-YEAR CHANGE SINCE 1970



Inflation hit over 9% in June, 2022 and is currently 6.5%



Globalization is slowing, indicating a bipolar world which makes raw materials more expensive and may increase inflation.



So far, short term interest rates currently stand at 4.25 to 4.5% and will likely need to go above 5%, and stay at that level for an extend period, to effectively fight inflation. The higher rates have resulted in a slowing economy. Imports and exports fell in October and November while retail sales, manufacturing output, and home sales all declined. Job and wage growth slowed in Dec although labor markets remain tight. **So, are we looking at a recession? Maybe .... it will be touch and go but we are not out of the woods yet.** We feel it will be difficult to get inflation down to 2 or 3 % and have it stay there. Inflation is a world wide phenomenon with high rates throughout Europe and Asia and it may take time to bring them down.

### **The World View**

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### **Conclusion and Chances of a Recession**

I attended a meeting sponsored by The Financial Planning Association. The speakers thought there was a 70% chance of a recession but they believed it would be mild. The economist brought up a number of items which point to a recession, such as, a slowing world economy, and higher interest rates. They all mention one thing that's holding up the economy and that's low unemployment rates and persistent wage gains. (see charts on the back of this page). It is hard to predict the future but we feel the economy will continue to bounce around. Barring a major expansion of the war in the Ukraine, we think Markets will be higher at year end.

Accumulating wealth takes time and we may face many challenges along the way. Most accounts have cash in them and **we are looking to slowly reinvest the funds over the next several months into Sound Companies with good business models and strong balance sheets.**

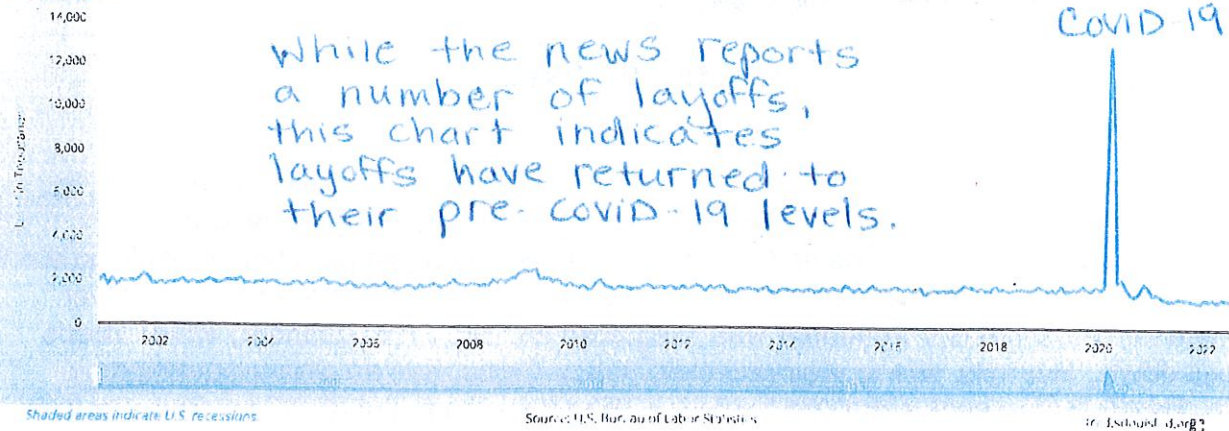
We welcome your calls.

# Layoffs and Discharges: Total Nonfarm

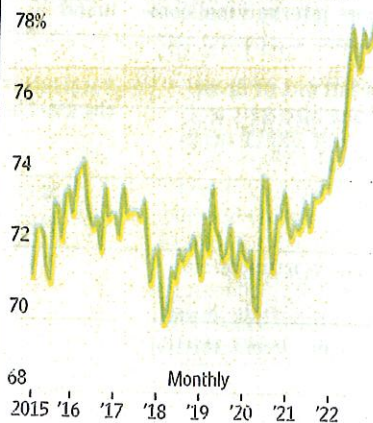
Observation Units Frequency

2000-12-01 2022-11-01

## FRED Layoffs and Discharges: Total Nonfarm



### Job openings at employers with fewer than 250 workers as a share of overall private-sector job openings



Companies keep hiring despite their fears that a downturn is coming.

### Bosses Pay Up To Keep Staff

Employees who stay put in their jobs are getting their heftiest pay raises in decades, helping fuel inflation. A2

Median hourly wages, change from a year earlier, 12-month moving average



Wage increases indicate a strong demand for labor.