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April 25, 2022 – Weekly Notes

Economic Commentary:

Fed Chairman Jerome Powell roiled markets last week with comments emphasizing –again—the Fed's determined dedication to fighting inflationary forces with monetary policy actions. Investors interpreted his remarks as moving up to late 2022 short-term interest rate levels once anticipated for mid-2023. At this point, the US Federal Reserve is viewed as the most aggressive of global central banks on the issue of inflation, although many other central banks are moving in the same direction. One notable result of this viewpoint is the strengthening of the US dollar against the Yen and the Euro. While bond markets appear to be "stabilizing", with fears about long-term inflation substantially moderated, volatility in equity and currency markets has been exacerbated. Equity markets are now grappling with a new uncertainty, after years of COVID uncertainty, directly resulting from the certainty of interest rate hikes: economic growth and the associated outlook for business earnings. World economic growth is being revised downwards to approximately 3% in 2022 and there are serious questions as to whether US Q2 GDP growth will remain mired at 1%, following an anticipated Q1 growth number of 1.1-1.2%. The commentaries in this month's earnings calls have been almost uniformly cautious about the outlook for the remainder of the year, a notable sign of the significant differences in 2022 business environment from 2021.

Data to Watch:

1. US Durable Goods Orders for March, released Tuesday, April 26
2. US Pending Home Sales for March, released Wednesday, April 27
3. US GDP Growth Rate, Q1, first estimate, released Thursday, April 28
4. Michigan Consumer Sentiment Survey, Final for April, released Friday, April 29

Suggested Reading:

1. https://www.wsj.com/articles/some-job-switchers-are-having-second-thoughts-great-resignation-11650663370?mod=hp_lead_pos11
2. https://www.nytimes.com/2022/04/25/business/china-covid-zero-economy.html
3. https://www.axios.com/food-buying-habits-are-evolving-in-the-face-of-inflation-93aea003-c72f-4c3f-b008-1fb6dc95c949.html

Investment Commentary:

Sentiment

Investors are facing another challenging week as markets continue to evaluate corporate earnings and economic data relative to a U.S. central bank that has become hawkish. The toll of continued geopolitical uncertainty, stubborn inflation, and the effects of aggressive monetary policy shifts are clearly showing in the poorest investor sentiment in 30 years and record mutual-fund outflows. This backdrop is aggravated by the Chinese zero-COVID policy and the government's willingness to slow down economic growth at the expense of widespread infection.

Markets

The change in the short-duration environment now affords a positive nominal return on cash — again, an environment we have not had in over two years. The market's readjustment process has been very difficult for bond investors as the speed and magnitude of the re-pricing of monetary policy resulted in negative returns year-to-date. The equity markets are increasingly concerned that profits will be challenged as margins pressures increase and the Fed increases its focus to fight inflation. The historic benefits of both price earnings expansion and earnings growth are being challenged. As we look back in history, it is worth noting that the retail investor does not have a particularly good track record at timing the market, and behavioral biases tend to result in "selling low and buying high." The best antidote to address these tendencies is to know the details of your financial plan and its near-term and long-term objectives and liquidity requirements.

Wealth Planning Commentary:

The 4% Rule

A recent article in the WSJ discussed the 4% percent safe retirement withdrawal rate rule and how it may no longer apply with today's unprecedented conditions. Simply put, the rule states that a person in retirement may safely withdraw 4% of a 60/40 portfolio each year for 30 years without depleting the assets.

The rule is attributed to Bill Bengen, who researched and published his findings: 'Using historical data to determine withdrawal rates' in the early 90s. The media later popularized the '4% rule,' and it became a heuristic many relied upon to help determine how much savings were needed to maintain financial security in retirement.

It's a simple rule, but a 4% safe withdrawal rate should not be relied upon to determine adequate savings for retirement. It's likely Ben would agree. Each circumstance is unique, and if you are trying to arrive at a safe withdrawal rate, there is likely some risk of depleting assets; the stakes are high.

We recommend developing a wealth plan with your unique financial circumstances, including income sources, expected spending and portfolio assets. The plan should be tested against persistent higher than average inflation, lower than historical returns, portfolio return sequence risk, and longevity risk. What if your portfolio was down 30% in the first year of retirement, how does that change your safe portfolio withdrawal rate?

There's less leeway in retirement for unprecedented circumstances that negatively impact your plan. Developing a plan accounting for and addressing adverse conditions before retirement will help strengthen its resilience.

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Disclosures