Episode 118 Economic Outlook for 2023 with Chief Investment Officer Brad Everett

Patti: Hi, everybody. Welcome back to the Patti Brennan Show. Whether you have $20 or $20 million, this show is for those of you who want to protect, grow, and use your assets to live your very best lives. As has become our tradition, we're going to be giving you our Key Financial Economic Outlook for 2023.

What this tradition entails is at the beginning of the year, our Chief Investment Officer, Brad Everett and I, talk about what happened last year and what we expect in the year to come.

What makes this a little bit different is that at the end of the year, we're going to circle back with all of you and we're going to keep ourselves honest and say, "OK, Brad, what were we thinking was going to happen? What actually did happen?" because I think that's important. It makes it real for all of you, as well as for all of us.

Brad, thank you for your willingness to join me on the show today.

Brad Everett: Thanks, Patti.

Patti: All righty. Let's just kind of recap what happened in 2022. It was a lousy year. Everybody lost value in their portfolios. Remember, not money - values. S&P 500 was down 18.1 percent. NASDAQ was down 32 percent. Gold was flat. Treasuries were down 13 percent. Who would have thought treasuries were going to be down 13 percent? The international equities also down 14 percent.

Let's just start by asking the question, or at least talking about the headlines that we see an awful lot. First of all, it is very unusual for stocks and bonds to be down in the same year. It's only happened three times. Bonds had never lost double-digit returns.

Let's peel that back a little bit. That's the headline. What's the actual reality, Brad?

Brad: If you look at calendar year returns, that's totally true. You can go back and confirm that. Looking at calendar-year returns is a little bit arbitrary. I don't know that most investors care the difference between January 1st versus March 1st as the beginning of a year.

If we went back and looked at rolling periods, it's actually more common for stocks and bonds to be down for rolling 12 months than you would think. We actually had a recent example. If you just look at a calendar year that starts on January 24th, it happened as recently as 2018.

It's actually not a totally rare occurrence. It's not common. It's certainly not the outcome you want. You usually buy bonds to offset some of the risks in stocks, thinking that they would often go in opposite directions, but it's not always the case.

Patti: That's what really matters to everybody who is investing their money. It's not so much the calendar year, but how am I doing? That's the most relevant factor here, right?

Brad: Sure. I mean, if you want to look at your portfolio on December 31st and ignore it the rest of the year, then calendar year returns do matter.

Patti: Wouldn't that be nice? Isn't that something that we tell people to do, "Go into a coma, a long term is what we're investing for."? Yet, we humans, and I don't want to use the word "insulting," but we human beings have a tough time thinking long term. We live in the short term.

Let's be real. We want to give it to people real and say, "Hey, when you're investing your money, it's unlikely, it's unusual that stocks and bonds are going to be down in the same 12-month period of time. The fact of the matter is it has happened. It's not quite as unusual as the headlines would lead us to believe. It's OK. It's happened, and eventually, people have recovered.

Brad: I think too. By looking at other rolling 12-month periods, it helps make the argument not to just dismiss 2022 as something that will never happen again. That's something that you want to be prepared to happen more regularly than maybe we might have thought.

Patti: Or maybe what we are often led to believe. Again, let's go beyond headlines here and do the work to establish realistic expectations going forward. Every experience is going to be different. Every individual and family are different. The most important thing is, how long is long-term for you? Right?

Brad: Right.

Patti: Another statistic that is out there is that we had a terrible year last year. I say terrible, it was a bad year. What is the probability that we're going to have another bad year? In other words, how often does it occur, where you have a loss, following a loss? When you look at the headlines, once again, the headlines would tell you, it's almost only happened nine percent of the time.

Brad: It's pretty rare. If you're going into a two-year period, what's the likelihood that that two-year period is going to be loss-loss? It's nine percent. We've already had the first loss.

If you look at the data of comparing a loss-gain versus a loss-loss, the odds of next year being a loss are probably...Again, that's not what you would predict, necessarily, but just based on historical precedent, you would probably have about a 66 percent chance of a positive year next year, about a one-third chance of another loss.

That doesn't say anything about the magnitude of a loss. You could lose one percent, or you could make 40. Who knows?

Patti: That's actually a really good point. It's the magnitude that is as important as whether or not it happens. It wouldn't surprise me, especially after a bad year, that you go into a new year, and people are feeling a little skittish. Although I will say that, as we record this today, that's not been the case for January of 2023.

This is an example. These are two examples and important examples for all of you watching and listening to understand that statistics can be deceiving. It's important, far more important for all of you to understand what they mean in your lives, from a cash flow perspective.

From a long-term retirement perspective, or when you need the money for that tuition, or that car or the wedding, we all have a certain amount of resources. The most important thing is, how are those resources going to be used? When are they going to be needed?

How can they be optimized, given the fact that there's a reason why Brad, and I always say past history is no guarantee of what you can expect in the future, because guess what, it's the truth. That's all you're going to get from us. We don't know what's going to happen. We can give you an educated guess, as we will continue to do in this podcast today.

Always remember, the experience is going to be unique to your situation. What else are we talking about, Brad?

Brad: Just to recap, last year, you had Fed funds rate rise a lot, your treasury yields rise a lot. We had two quarters of negative GDP and then two positive quarters. Then, probably the biggest difference would be in market performance, the value versus the growth.

Patti: All I can say to you and everybody else, hallelujah.

Brad: It's been a while.

Patti: It has been forever. We've been talking about the value of diversification and the importance of having dividend-paying companies in a portfolio. They had significantly underperformed growth. Sure enough, when we least expected we saw a pivot, and boy, was the difference really remarkable.

It is the difference according to the indices. Both lost monies, but value indices lost four and a half percent. Growth lost 33.5 percent. That's a big difference, a big swing. I'm not saying losing money is easy in any environment, but it's nice when you can lose a little bit less.

Brad: [laughs] Right.

Patti: Now, what do you think that is? I think that your observation about why. Why did growth get hammered so much? Your point about a growth company and what they're doing with acquisitions, and the interest rate environment, is such an important part of that.

Brad: Interest rates drive almost all of it. From an analyst perspective, with discounted cash flow valuations, you're discounting those future growth companies by a bigger number. A dollar 10 years from now, discounted at one percent, is a lot different than a dollar 10 years from now discounted at five percent. That's a big difference right off the bat.

Patti: I'm sorry to interrupt you, but I just have to do a sidebar. You are beginning to sound like Professor Fuhrman, oh, my goodness.

Brad: I taught him everything he knows.

Patti: Yes. You did.

Brad: From the company's perspective, projects that looked like a good idea, two percent might not be a good idea at six percent anymore. The borrowing costs for the company itself makes a huge difference there too, in terms of whether there are projects that are worth even trying to undertake.

Patti: To wrap this in a nice little bow, then on top of everything else, we had Russia invade Ukraine. I don't know whether we're going to spend a lot of time talking about that. It is rather interesting to me.

I will make this observation that it's one of those things where, when it happened, we were all freaking out a little bit. One of the things we saw was in terms of the probabilities of Russia actually invading, a lot of people thought that they were bluffing.

Brad: Yeah. That was a common opinion until it continued to build and build and build.

Patti: It's also interesting that the Russian index, if you are a trader, you were going to invest in that ETF that was strictly Russian companies.

Brad: Yes. There's an iShare, a Blackrock ETF that tracks the Russian stock index. It was down. A year ago, we were probably standing here talking about whether this is a bluff or not. If you thought it was a bluff, when the military exercises started, that fund probably went down in the neighborhood of 40 or 45 percent.

If you thought they were bluffing, that's a great investment. It returns to its value. Those companies continue doing business. You can extract money out of Russia through profits. That ETF has now closed and the warrants, they're worth pennies. That obviously would have been a high-risk, terrible reward.

Patti: The old saying, "Don't try to catch a falling knife," applies to that. Last but not least, Crypto.

Brad: The great hedge.

Patti: The great hedge against inflation.

Brad: The great dollar hedge.

Patti: Here, it's going to be this replacement for gold as a hedge against inflation. Inflation peaks at 9.1 percent. Bitcoin falls by 60 percent. If we were going to put this on the show notes, gold hasn't been a good inflation hedge either, by the way.

It jiggled all year long, just when we needed it the most, by the way. Bitcoin, Crypto, also not a good hedge against inflation.

Brad: That's the way it worked out last year, for sure.

Patti: Well said. Also, you never know what is going to be in the future. Let's talk a little bit about inflation. It was swift. It was fast. It was not unexpected, because it was drifting up in 2021. As we all know, the Federal Reserve thought that was due primarily because of the supply chain issues.

The supply chain was an issue. Shipping times from Asia, for example, pre-COVID, were running in about 60 days. They peaked this time last year at 110 days. They're down to 80. They're better, but it hasn't gone away. The ships off of Long Beach, California are now in port. That issue seems to be resolved, but there are some lags still with supplies.

That's an important factor because let's again go back to fundamentals, Brad. What is inflation? Milton Friedman said, "Too much money chasing too few goods." We now understand the too few goods part. Too much money was the Federal Reserve loosening policy, lowering interest rates as well, as fiscal policy putting money into the bank accounts of every American.

We had a ton of money and nowhere to go. What happens? People bid things up, like housing, like all this stuff. That's what happened with inflation. Getting back to fundamentals for everybody listening and watching the show, what really is inflation?

Inflation is strictly measuring the change in prices from one period to another. Inflation, at one point in the 12 months prior, peaked at 9.1. In the second half of the year, it started to come down. It is now running at around six and a half percent on the CPI. What does that mean?

It doesn't mean that prices are going down. That's called deflation. That's the worst thing that a consumer-based economy like ours can go through. Deflation is really bad. By the way, that's what Japan has been going through since 1989. We don't have deflation. We have disinflation.

Disinflation is that prices are still going up. They're not going up as fast. That's a problem because there isn't a guaranteed investment. There isn't a safe investment. We all think that "I'll put the money into the bank, just get CDs, things of that nature." Here's the problem with that.

Let's say that inflation is running six percent and if you've got money in the bank at one percent, you're losing five percent on that deal. That's not a volatile asset class. That is not coming back. That's gone. That's not necessarily a good way to deal with the issue.

I always want to break it down because let's face it, I'm an old nurse. I don't have any education in this stuff. When I want to learn about something, I break it down in a way that I can truly understand. Hopefully, that makes it a little bit easier for you to understand as well.

I’ve got all these brainiacs here a Key Financial. They've got all that other stuff under wraps. Moving forward, we’ve got inflation. We understand that. We've talked about the supply chain. Can you tell me a little bit about the data, Brad? The lag in the data, especially with CPI, 41 percent of what CPI entails is housing related.

Brad: Sure. Housing's an interesting one. It's hard to get current prices on what housing costs. Even in the best sense, even if you knew exactly what all the houses sold for, oftentimes you come to an agreement on a sales price months before the transaction actually occurs.

This is something you negotiated, potentially, a month, or three months ago. Even that lag, if the transactions are so slow to occur, houses don't turn over every three months so you can get good data, there can be a lag of nine months, 12 months, even 18 sometimes.

I think that's the argument for the Fed pausing. We don't really know what the state of things are even at this moment. We won't know the state of things today for several months down the road. Do you kind of hold off and let things work through a little bit?

Patti: It's a really interesting point that you've brought up because, when I think about 2022, I think about CPI. Then I think about the year before and when housing was going nuts, and there were 40 bids on one house at six figures over asking price.

That's when inflation was going nuts. We didn't see that in housing, especially last year, and yet inflation is going crazy. That's because CPI was measuring what was actually happening, or at least a portion of that index was what was happening in 2021. That's very important.

The other important thing that I always want to bring home to everybody is that the experience of inflation is very personal. People feel inflation very differently, whether you are retired, whether you are a young family,

I think the best example I can give, and a true example, is I live about two miles from here. My kids are grown. I'm not schlepping four kids all over kingdom come to their different activities etc., so gas prices didn't affect Ed and I that much last year.

Michael, on the other hand, has three children and a gas guzzler. When he went to the pump, it would stop at $125. His gas tank wasn't even full, but the pump stopped him at $125 because of the price.

Brad: Because that's what they're asking the credit card to preapprove?

Patti: Exactly. He wasn't affected by inflation and gas prices a lot more than we were. Inflation is very personal. We see it down to the penny with each client because we know what's coming in and what's going out. It's very cool when we can see the trends holistically across however many clients we have, as well as on a personal level. It's amazing how different it is.

Moving forward, Federal Reserve. What do we think about the Fed? We look at the charts, and we listen to the broadcasts, and boy, they are scary, sometimes. They're going to continue to increase interest rates. They're going to stay higher for longer. Yet the market doesn't seem to agree.

Now, let's first define the difference between the FOMC and the market. I'm going to tee it up a little bit for you, Brad. When I say the market, we're talking about the bond market. There is a general sense, historically, that it's the bond market, who, you want to listen to. Why is that?

Brad: I guess these are very specific products. These are actually Fed Funds futures rates, which are a contract that you would either receive money or pay money based on whether it is above or below a specific rate at the end of 2023, 2024, or '25.

Patti: This is the futures market, not the bond market?

Brad: Correct. They are very closely tied together. One obviously influences the other. There is definitely a disconnect between what the market thinks rates are versus what the Federal Open Market Committee will every September lease out there. It's not even really a forecast. It's what they think the best policy should be.

They're not necessarily giving an expectation, but what they think the policy should be. There's a real disconnect there. In cases like that, you tend to want to believe the market. You can go back to political poll.

There's great studies on what's more accurate, political polling, or gambling markets about political races. The gambling markets have always been phenomenally more successful at getting the odds correct than polling has. There's all kinds of human bias and things in polling that just is not quite as accurate.

So, do you believe that people that are voting on what they think should be the thing or the large institutions that have a lot of money riding on getting the decision right? It tends to be the people that have a lot of money riding on getting the decision right that tend to be a little closer at...

Brad: ...these things.

Patti: Fascinating. I think it's fascinating, and I think it's also important to recognize that when we talk about the FOMC, we're talking about 11 people.

Brad: Right.

Patti: Right. That's also kind of interesting. They can talk, and they can have their outlooks, and that sort, but we're all painfully human, and they are too. That's why they want to rely on the data. They're doing the best that they can.

You take two different outlooks, or what have you, in what they think policy should be. I will say, for all of you who are listening and watching, that it doesn't matter which one you're looking at. They both think the policy is going to be lower than it is today.

Brad: Yeah, they disagree on the magnitude, but the direction's the same in both cases. Right.

Patti: That, I think, is the most important takeaway. Just to give you a feel, the FOMC year-end estimates for 2026 would be a rate of 3.1 percent, whereas the market thinks it's going to be closer to 2.87. So, they're pretty close.

Brad: That one's a close one.

Patti: Yeah. Just to keep it all in perspective, it's really next year where there's a wider gap. The Feds basically say we're going to be over five percent. The market's thinking that there probably won't be.

Again, the longer you go out, the less accurate it's going to be. Really good takeaways, important for all of us to keep in mind and keep real.

Brad: You'll get a chance to refinance it in two or three years.

Patti: Oh, yes. Exactly.

Brad: If you just bought a house this year.

Patti: Absolutely. All right. Let's talk about recession risks. Let's first define what is a recession, Brad? It used to be that two negative quarters in GDP, you were in a recession.

Brad: Yeah, that's always been kind of the rule of thumb, right?

Patti: Yeah. We had that last year, and yet, it wasn't called. How come?

Brad: Yeah, so I think that's always been a rule of thumb. There's an organization called the National Economic Bureau of Research, or whatever NEBR stands for. They track six indicators.

Historically, if all those indicators are going down at the same time, or they're all in a bad place at the same time, you're more than likely going to have declining GDP as well.

I think if you want this quasi-official body to say there's a recession, they follow the indicators more than the actual GDP figures. They have figures on the consumption side, on the production side, and if both are trending south, you're usually in a recession or headed toward one quickly.

Patti: I'm going to read off the six indicators because again, I'm a nerd. For those fellow nerds out there, here's what they are. Real personal income, non-farm payroll, household employment, real personal consumption, wholesale retail sales, and industrial production.

To Brad's point, if you're going to have six of these, and they're all down, chances are you're going to have a recession. The only question is are we going to have a hard landing, a bad recession, a soft landing, not so bad, or no landing at all. That really is the question.

I think that we've talked about this a lot here. The more we talk about a recession, I feel like it's almost going to be one of those self-fulfilling prophecies.

What people feel like, "Oh, there's a recession coming in." It would be human nature for business leaders to say, "Everybody's predicting a recession in the summer, so we got to start thinking about who we're going to lay off."

They go ahead and lay those people off. Then, even the people who aren't being laid off, they stop buying stuff, because they feel like they want to shore up their emergency fund. By the way, all of you listening and watching, you should shore up your emergency funds. That's just good personal finance.

It's a very interesting feedback loop that tends to occur. Nobody really knows. Who knows? I'm going to say it first, I think the real Black Swan event for 2023 is if we have no recession at all.

Brad: Yeah, that everybody expects a recession, and it doesn't happen.

Patti: Exactly. One of the things that's really contributing to this prediction is the yield curve. The yield curve is defined as the difference between a three-month treasury and a 10-year. Three-month, 10-year.

Typically, again, keep it real, if you're going to the bank, and you want to buy a CD, you would normally expect to get a higher interest rate, if you're willing to lock your money up for 10 years, than if you were only willing to lock your money up for three months. The bank would give you a higher interest rate on that 10-year CD.

Same thing with treasuries. 10-year treasury would pay a higher interest rate than a three-month. Guess what, folks? That is not the case right now. Not only is it not the case, it's inverted. Meaning, you can get a higher interest rate on a three-month treasury bill than you could even if you're willing to lock it up for 10 years.

The spread, the difference, is as we speak 1.27 percent.

Brad: It's pretty wide.

Patti: That's really wide. First of all, it's unusual for it to be negative. By the way, the reason we're bringing this up is because it tends to be a predictor of a recession.

Historically speaking, which, of course, is no guarantee when that has happened, we've always ended up in recession. Although, again, the data set is very limited. It's eight or nine times.

Having said that, 1.27 percent is a very widespread...I have been asking you, the professor, and everybody here, guys, we’ve got to do some research on this. When it's been this wide, how bad was the recession? Is it an indicator? Is the width of the spread, indicative of the magnitude of the pain that we might experience in a recession? What did you find, Brad?

Brad: Nothing? I have no idea.

Patti: Just so you know, we're trying, but there's absolutely nothing about it.

Brad: It's a good project. Maybe, we'll be the ones that get it out first.

Patti: If nothing else, it goes to show you that as long a history as our nation has had, our economic history is not that long. There aren't that many times that we've been in really awful, recessionary periods. We want to keep it real. We want to understand that these things can happen. They might happen.

The question is always going to circle back to your situation, what do we do about it? We talked about people worried about losing their jobs. There's another very important thing that we want to talk about in terms of data, statistics. Keep it real. Let's talk about the job openings versus unemployment.

One of the things that we talk about is, "Take the unemployment data with a grain of salt."

Brad: Yeah. It's such an easy number to track, and it either seems low or high. There's so much more to it. Whether you're actively looking for a job or not, it doesn't do a great job of describing your financial situation. It doesn't tell you if your overtime was cut. It doesn't do a good job of keeping track of temp jobs and part-time jobs and things like that.

Maybe your hourly wages have stalled or dropped, but you are technically still employed. There's more to it than that single inflation. Unemployment is great because it's only three and a half percent. There's more to it than that.

Patti: A lot more to it. That's important to look under the hood. It's very personal. Just like you said, wages, overtime pay, temp jobs, all of that is declining. That's what the Fed is now paying attention to. They're paying attention to wage growth because that is very sticky. That has that domino effect.

That's something that we're going to pay attention to, again just for fun, I suppose. I don't know that we're going to do much with that information. What do you think, Brad?

Brad: I agree. I don't know how actionable it is in terms of how you would change a portfolio. In terms of trying to anticipate what a recession may be, or how deep or shallow, that's probably an important part.

Patti: One thing that you've said, I've heard you say this over and over again, is that, how did you explain it? "The labor market is tight, but it's not strong."

Brad: To say that it comes down to that single number, three and a half percent. That's a tight labor market. Of all those 96.5 percent that are employed, maybe your wages aren't keeping up with inflation. If your monthly expenses go up, and your pay does not, essentially you can buy less and less stuff every month.

Technically, you have a job, but you probably wouldn't feel you're on very stable footing in that position.

Patti: Let's pivot away from the United States. Let's talk about other markets. The international markets, hallelujah, is all I can say again. All these years, we've been talking about the value of diversification and the importance of investing worldwide. It's never really worked out.

The US market has dominated in terms of returns. International markets have done well, just not quite as well. In your research, it's fascinating to learn that the impact the currency has, and what our clients actually experience in terms of returns.

Brad: We say US investments have dominated because we live in the US, and we measure investments in terms of dollars. If we lived in Poland, we might think exactly the opposite. There are very long stretches, especially in the last 15 years, where on a currency-neutral comparison, the markets have performed exactly the same.

If you compare the S&P 500 to the EFA, a US market and international market. The only difference in performance to a US investor is the change in the value of the dollar because what you have to do to invest in a company in Europe is to sell your dollars, buy the euro, purchase the European stock.

Then, when you are ready to sell it and get your money back, you sell it. Then you have to sell your euros and buy the dollar. You have this return in the company or itself. Then you have a return in the change and the exchange rate over the entire time of the investment.

For a long time, the dollar has done fantastically well. That has driven a lot of the return comparison in the US towards the international, but you can see there's stretches where, if you look back to September of this year, there's about a 12 percent outperformance by the MSCI EFA versus the S&P 500. That matches almost exactly the change in the value of the dollar versus the euro.

The performance to local investors is exactly the same. The only money you've made or lost is the currency you're holding at the time. It does matter in terms of diversification and trying to figure out and allocation to US versus international stocks.

Patti: That is so interesting to me. Maybe, would it be safe to say that the reason that we diversify, globally, the difference between the US and international, it's not so much that there are better companies overseas, per se, it's just that you diversify because you want that currency kicker?

Brad: Yeah. It should even out over time. I think it's really just for diversification. No theory would suggest that in the next 30 years that stocks in the US should outperform stocks in Europe. You would think they're probably going to be pretty similar.

You can smooth that ride out if sometimes you're invested in Euros, and part of your portfolio is invested in dollars, and some of it's invested in yen.

You can experience that same long-term rate of return that equity should provide, and the currency differentials can help smooth it out over time.

Patti: The pattern of the returns is going to be different.

By having different patterns, to your point, it smoothes out the experience and gives you an opportunity to rebalance and do all of that kind of stuff that we do, tax loss harvesting, all of the things behind the scenes that we do, and that people who are watching can do for themselves if they don't have an advisor. Or, that your advisor is probably, hopefully, doing.

It is important to have that. Again, it's not a stock call. It's nothing of that nature. It's just to have returns at different periods of time.

Brad, you've heard me use this metaphor all the time, but I need the simple stuff to understand it. It's like the garden. You plant a whole bunch of stuff, and it's all going to bloom at different times during the year, but at least you always have something to look at.

That's the point. That's where that beautiful thing called compounded returns can occur. Let's use the math to the benefit of your portfolio, of your experience, and your lives. That's the whole point, it's not that we're trying to guess, etc.

Let's go back to the recession. I've talked about this in a prior podcast, but I think it's really important for us to really drive this point home.

When we think about history, and we think about the fact that we are a consumer-based economy, 70 percent of our economy is what you and I are buying today, tomorrow. Going into a recession, historically, at least, the consumer has never been in a better spot.

Really looking at the data, household debt is at a 50-year low. 90 percent of mortgages are fixed at four percent or below. Unemployment is low, we talked about that. The opportunities still present themselves for people who do want to increase their revenue coming into the household, 1.7 jobs for every person looking.

This is a statistic that a lot of people are not aware of. Even after the pain of 2022, and it was painful, household net worth has increased 27 percent since 2019. That's a big deal. That's three years.

Now, if we break that down, that's $29 trillion, with a T, guys. $29 trillion that has been earned over the last three years, or about $85,000 per person in the US.

Yes, it's probably lopsided. That's the problem. The rich are getting richer. I got news for you, though. In 2021 and 2022, the greatest gains actually came from the bottom 50 percent. Again, it's all relative, but at least things are improving for everybody.

Excess personal savings, which is really, I think, an important thing for us to keep in mind...Because of the two fire hoses, we can all look back and say the Fed blew it.

They didn't see inflation. They let the economy go off way too long, and inflation was the result. Let's all keep it real and remember where we were in 2020. That is basically three years ago.

With the pandemic, unemployment got up to 11 percent. GDP was down 10 percent. It was really scary. There was no vaccine. We didn't know that a vaccine was going to be on the horizon as quickly as it was, so it was a scary time.

The Fed did what the Fed can do. They just threw a lot of money into this consumer-based economy. The federal government did the same. There was a ton of money. What that resulted in is excess personal savings in the amount of $2.2 trillion.

Now, let me say that again. It's excess personal savings, over and above what we all keep in our regular emergency funds. To keep it real, that has been burned down. We're burning through that a little bit. That now stands at $900 billion.

At the current rate, that could be gone by the summertime. Which, it seems to be contributing to this old narrative that we're going to have a recession in the summer. I don't know that it's going to happen. That's just a contributing factor.

Corporations are also very healthy with seven trillion dollars of cash in their coffers, so we're in pretty good shape if we do go into this recession. It's not great. It won't be fun. Who knows how long it's going to last?

What I do know, and what history has told us, is that the market is a leading indicator. What do we mean by that, Brad? What are we saying in English, for everybody listening and watching the show today?

Brad: It's such a wonderful idea to just say, let's just get out of the market. We'll get back in when things look better. The problem there is that the market will have anticipated things looking better longer, far ahead of time.

Historically, if you look at the last 9 or 10 recessions, the S&P has bottomed out before the recession was even acknowledged. Once even the recession is announced, you've already missed the jump off the bottom. That can sometimes be a rapid increase, or maybe it takes a little longer, but that's a time you want to be invested, not waiting for better news to come along.

Patti: It's interesting, we didn't talk about this. My research has shown that we always talk about if you miss the best days in the market in the last 10 years, the last 20 years, you pretty much lost all of the return. What I wanted to understand is, when did those best days actually occur?

What I found fascinating is that 21 of the last 25 best days in the market, the market goes nuts, 900 points in a day, for example. That has happened within one month of the worst day. 84 percent of the time, the worst day happens within a month, sometimes the next day.

Brad: And you can't pick one or the other.

Patti: You can't pick one or the other. We're not going to pick it, either. I do not want to take the chance that someone's going to miss out on that. The other thing that I think is fascinating is it's a statistic, don't know that it's going to happen. I'm going to say that it did happen. It is part of our responsibility, I think.

One thing that we look at is consumer sentiment. There's an index. Last year, consumer sentiment got down to 50. That was the low. It's at 59 right now. When consumer sentiment has been this low, even at 59, looking forward the next 12 months returns on markets were unusually positive. I'm talking unusually to the tune, on average 24.9 percent.

I'm not going to say it's going to happen. I'm just saying that's what did happen. We can feel awful, which is what sentiment does. It measures how we're feeling about things these days. We can feel awful, just don't do anything about it because you don't want to miss out on that potential.

Brad: Exactly.

Patti: That's the one takeaway I get. Our tagline is so important. I look at that, and I think about that all the time. Key Financial, "Wealth Management with Wisdom & Care." To me, the wisdom is understanding and recognizing that we don't know what's going to happen this year. We're not going to try to get too cute. We also don't want to fall prey to our fears.

One of those includes this thing called recency bias. What that means is that we think that what happened last year is just going to keep on happening. That's called recency bias. It's a human nature fact. It's big when it comes to investing.

My message to you, and everyone watching and listening today is things aren't necessarily going to be bad. They might be different. That's OK, recognize that. Let me give you a great example.

For the last 15 years, you and I have been taking care of our clients, many of whom are retired. For 15 years, we've had to overweigh inequities, because bonds weren't paying anything. That's been the fact since the financial crisis.

Literally, for the first time, we have options. We now have legitimate alternative options in fixed income that we haven't had in 15 years. I have got to tell you, that's pretty OK because they tend to have less volatility. That's an important thing for people who are retired. By the way, as we are all, let's go back two years ago when the Fed lowered their interest rates to zero.

When they were building up their balance sheet, and everybody's wringing their hands and saying, "Oh, my goodness, the Fed's running out of arrows in their quiver, if we have another crisis, they're not going to have anything that they're going to be able to do about it, because they got nothing left." Well, guess what?

Brad: They have arrows again.

Patti: They've got options. That's important too, not a bad thing. Unfortunately, and this is awful for me to say, there's this idea, the Russia-Ukraine war, and it's becoming old news. There are people who are losing their lives over there, their homes, their everything.

I don't want to ever lose sight of the human suffering that's happening over there. I also don't want to become complacent to it. Yet, I find that people aren't paying as much attention to it. We can also talk about mortgage rates. Personally, people are going to get used to five and six percent mortgage rates again.

It's OK. Things aren't necessarily bad. We've had six percent mortgage rates in the history of our country. By the way, the economy did just fine. Things aren't going to be bad, necessarily, just different.

Speaking of Russia-Ukraine, think about international security, we've got a renewal of the NATO alliances that we haven't had in years, and refocus on supply chains, and maybe bringing some of that manufacturing back to the US. I don't know, maybe it's me. I can't think that that's going to be all bad. It might be more expensive, but I don't think it's necessarily going to be all bad.

We talk about inflation. Governments have been using inflation to monetize their debt. After World War II, they monetized all the debt that came about from World War II.

All that really means is $100,000 loan 30 years from now isn't going to feel like $100,000 30 years from now because it's discounted. It's going to feel like a $20,000 loan today. That's called monetizing debt. Governments have been using it for decades. Inflation isn't all that bad.

As we look at, and we are talking, you're going to hear about the debt ceiling debate, and all that stuff. In addition to that, and potential impact on people listening is, Social Security went up 8.7 percent. Whether you're taking it or not, that's a nice little perk.

If you're not taking it, that's on top of the eight percent interest that you also got by not taking it until a later age after your full retirement age. That's a little bit of a hedge on that as well.

There is a brand-new tax law. I'm just bringing this to your attention. We're going to do a separate podcast on this tax law that nobody seems to be talking about. It's chock-full of stuff that is going to affect everybody that's listening to this podcast and watching this show.

It's about their retirement accounts. It's about 529s. There's lots of little nuggets in there, that we've peeled out, that it's important for people to be aware of. One of them is increasing the limits that people can contribute to their 401(k)s.

For a couple who might be feeling a little behind after putting their kids through college. They might be feeling a little bit behind with their retirement savings. Each individual is going to be allowed with a catch-up contribution to put $30,000 per person or $60,000 per couple into their 401(k). You do that a few years, and you'll catch up pretty quick.

Those are the things that are important that people want to stay focused on. Let's wrap this up. What do we do with all this information, Brad? What are we going to tell the people who are watching and listening to the show?

Brad: I don't know. Probably nothing, Patti.

Patti: [laughs]

Brad: This has been a good example of why we diversify. Why you want different types of assets. Why you don't just buy two indices. To say that you have an aggregate bond index and the S&P, that's not the way most people are invested. That portfolio didn't do very well. That doesn't serve necessarily a purpose for anyone.

Historically, we've always started with a financial plan and backed into an asset allocation from there. If somebody needs money next week, they're not invested in those two asset classes exclusively.

Brad: You have cash. You have short-term bonds. You have real estate. You have other places that you can take money from that did well.

Patti: If I can go back to the garden, it's like having an evergreen and a tulip. That's it, in your garden. There's a lot of other things that we can choose from that are doing fine right now. That's important because ultimately, that math will help them. For me, the most important thing that we talk about is we have no illusion of certainty.

We will be back to all of you at the end of this year, to keep ourselves honest, and to say, "Hey, this is what we thought. This is what's actually happened. Here's what we're going to do about it," because you do want to be proactive. For me, at least, as we listen to the different TV shows, and honestly, as you probably know, I'm going to be on again next Wednesday.

It's important that as we all hear the shrieks and the cries and people on TV freaking out about this impending recession, and this random economic data point, that somebody's interpreting a particular way because of that, the market's going nuts and going down.

It's important to keep it real and recognize that markets -- the stock market, the bond market -- we have to remember that there are people in those companies.

Those same people who are the leaders of these companies, as we speak today, are making important decisions and implementing strategies to adjust to what's happening, to serve the wants and needs of about 8 billion people that live in this world.

Brad: ...and far beyond this year, too.

Patti: Exactly. Let's all keep perspective. These are human beings. You can look at the enduring businesses. Their earnings may not grow as much as they had hoped, they're still making money.

Let's keep some perspective and recognize that the most important decisions that you're going to make, is that we make them on behalf of our clients...because, ultimately, this is a stewardship.

The most important decisions, to your point, Brad, is what's happening in these people's lives this year. What do they want to happen, what do they aspire to, what are they worried about, and what are we going to do about it?

I'm going to end this today. Thank you, Brad. As always, you are an amazing Chief Investment Officer. You're so smart. I love the way you phrase things...

Brad: Thanks.

Patti: Quick and to the point. Thanks to all of you for listening in today. Thank you for the trust and the confidence that you have in us and for tuning in, spending what will probably be almost an hour of your time. I don't take that for granted. I am so grateful and honored that you spent that time with us today.

I hope you have a great day, a great week, and a great year. If you have any questions about anything that Brad and I talked about today, please feel free to go to our website at keyfinancialinc.com. Ask us questions. Send us an idea for a podcast.

We are here for you. We never lose sight of that. It's so much more than a job to us. It's truly a vocation, and I'm hoping that you get that from these podcasts, from the things that we work on behind the scenes to try and create value for you as you listen to these podcasts and engage with us.

I hope you have a great day. Take care.