CLAYTON WEALTH PARTNERS

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MONTHLY MARKET PERSPECTIVE

Recession (or a Lack of One) Key to the Path Forward

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DASHBOARD

- Business Cycle (red)
- Valuation (yellow)
- Trend (green)

It's that time when Wall Street strategists publish their outlooks for the year ahead. Collectively, they offer a wide range of opinions and, naturally, a wide range of accuracy. We don't publish forecasts in this traditional sense, but we do participate in the thought process they require. We believe the key to the path forward for markets is whether the U.S. economy experiences a recession in the near term.

To illustrate, consider the S&P 500's 24% decline over nine months last year. It was short and shallow compared to the typical bear market since World War II, which fell more than 30% over 15 months or so. (See Exhibit.)

Exhibit: Bear Markets Since World War II

BEAR MARKETS SINCE WWII

	Date of S&P 500 High	Date of S&P 500 Low	Duration of S&P 500 Decline (Mos.)	S&P 500 Price at High	S&P 500 Price at Low	Total Decline	Bear Mkt Assoc. W/ Recession?
1	5/29/1946	6/13/1949	37	19.25	13.55	-29.6%	Y
2	8/3/1956	10/22/1957	15	49.64	38.98	-21.5%	Y
3	12/12/1961	6/26/1962	7	72.64	52.32	-28.0%	N
4	2/9/1966	10/7/1966	8	94.06	73.20	-22.2%	N
5	11/29/1968	5/26/1970	18	108.37	69.29	-36.1%	Y
6	1/11/1973	10/3/1974	21	120.24	62.28	-48.2%	Y
7	11/28/1980	8/12/1982	21	140.52	102.42	-27.1%	Y
8	8/25/1987	12/4/1987	3	336.77	223.92	-33.5%	N
9	7/16/1990	10/11/1990	3	368.95	295.46	-19.9%	Y
10	3/24/2000	10/9/2002	31	1,527.46	776.76	-49.1%	Y
11	10/9/2007	3/9/2009	17	1,565.15	676.53	-56.8%	Y
12	2/19/2020	3/23/2020	1	3,386.15	2,237.40	-33.9%	Y
13	1/3/2022	?	?	4,796.56	?	?	?
Mean			15			-33.8%	
Mean ex-Hi/Lo			14			-32.9%	
Median			16			-31.6%	
If October '22 Was The Low:			*9*			*-25.4%*	

Source: Standard & Poor's, Clayton Wealth Partners.

Parsing the data, we see that previous bear markets not associated with a recession (1961, 1966, and 1987) saw an average decline of 28% over about six months. The similarities to last year's bear market suggest that, so far, market participants think the Fed will succeed in sticking to the soft landing.

Have we avoided a recession? We're open to it. But we think it's too early to make that call. As we've written before, history suggests the bar to achieve a soft landing remains very high. There are numerous reasons, not least of which is the amount of time it takes—historically about 24 months—for changes in interest rates to impact the economy. The Fed started its most aggressive hiking campaign in 40 years in March 2022, which suggests we're still in the early innings.

If we don't avoid a recession, and we've been enjoying a significant bear-market rally (not unheard of), historical comparisons aren't as friendly and warn of another leg down. Those previous bear markets that are associated with a recession saw an average decline of 36% over 18 months. We think that fact warrants continued caution until we have conviction that a near-term recession is unlikely.

Bullish

- The Fed has made good progress in reducing inflation.
- The services sector of the U.S. has remained strong.
- The most attractive yields for fixed income and cash in years.
- Consumer and corporate balance generally remain healthy.

Bearish

- Global inflation remains too high.
- Slowing global economic growth with recession pressures mounting.
- Banks are tightening lending standards.
- Housing affordability remains at a decades-low.
- Leading indicators of unemployment are generally trending down.
- Delinquency rates on consumer loans are rising.
- Russia-Ukraine war, Israel-Hamas conflict, and other geopolitical concerns.
- China's post-Covid economic rebound has lost momentum, with deflation fears growing.
- Federal debt and deficits have ballooned.

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As Partner and Chief Investment Officer, James Walden strives to maximize our clients' long-term, risk-adjusted portfolio returns. This includes determining strategic and tactical asset allocations, as well as specific investment analysis and prudent rebalancing. Jim is also a partner and management team member. His expertise includes advanced investment research and valuation, and he is passionate about his role in helping clients reach and exceed their financial goals.

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