THE DANA VIEWPOINT

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Good News is Good News

In the markets, sometimes good news is bad news and bad news is good news. Stick with us here. Market movements always factor in expectations, or more specifically, changes in expectations. When a company announces good news, sometimes its stock will go down if the news was not good enough relative to expectations. Or a stock may go up even if the company announces bad news, if the news is still better than expectations. For a number of months, the stock and bond markets have shown many instances where they have sold off on stronger economic news and rallied on weaker economic news. Why? It has to do with expectations, specifically expectations of future moves in the Fed Funds target rate.

Market participants fear a Fed-induced recession. The Fed has stated that they want slower economic growth and higher unemployment, so recent stronger than expected economic news has led to higher expected Fed Funds rates and lower stock and bond prices. Conversely, weaker economic news has led to expectations for a lower terminal Fed Funds rate.

It’s time to reframe this tradeoff; good news is good news. As the Fed nears the end of its tightening cycle, economic growth has stayed strong. Recall where we were at June 30, 2022: the Fed had just raised rates from 0.875% to 1.625%, GDP had declined in the first quarter of 2022 and would fall again in the second, trailing year CPI was 9.1% as of 6/30/22, and the S&P 500 Index fell 20% in the first six months of the year.

In the second half of 2022, the S&P 500 Index rose slightly. GDP rose slightly more than an annualized 3% – not too hot, not too cold. CPI averaged less than an annualized 3% in the second half of the year, even with a revision that increased that rate. This economic rebound happened while the Fed raised rates from under 2% to over 4% by year end. In the bond markets, rates increased far more on the short end than the long end, as recession fears were pervasive.

So the question of whether the economy and the markets can outlast the Fed rate increase cycle is not settled, even as we undoubtedly move closer to reconciliation, with higher rates and decelerating inflation. The end game is near, but still not completely clear. Many of our equity strategies have shown solid performance versus their indexes through the second half of the year and into 2023. Fixed income

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and preferred strategies have shown strong rebounds at the beginning of 2023. The Fed has chosen to move more cautiously of late, with the last increase being 25 basis points. A resilient economy will keep the Fed active, so inflation needs to continue to decline in order to satisfy the Fed.

Generating positive income and providing relative outperformance is possible even in choppy, unclear environments, and that remains our primary goal.

Random thought: "What do most people say on their deathbed? They don't say, 'I wish I'd made more money.' What they say is, 'I wish I'd spent more time with my family and done more for society or my community."   - David Rubenstein

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