Weekly Wire

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BRINKER CAPITAL INVESTMENTS
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The Fed's Crystal Ball is as Foggy as Mine

The title of this week's Weekly Wire is not meant to denigrate in any way the US Federal Reserve as an institution or the thousands of Americans who work at the world's most important central bank. As we have written about before, correctly managing monetary policy for the world's largest economy strikes us as a near impossible task, and that is before even considering that every decision the Fed makes on interest rates and balance sheet management is both relentlessly scrutinized on Wall Street and in Washington and has a meaningful impact on economies and central banks around the world. Instead, the title speaks to the fact that any macroeconomic forecast – even one from an institution that employs 400 Ph.D. economists – should be taken with a grain of salt.

By way of example, coming out of its December 2021 meeting, the Fed predicted that inflation, based on the Personal Consumption Expenditures Index (or PCE) would sit at 2.6% in 2022 and the Fed Funds Rate would hit 0.9% in 2022 (see the Fed's December 2021 Summary of Economic Projections, lower and mid-left). Well, as 2022 winds down, the PCE sits at 6.0% and the Fed Funds Rate sits between 3.75% and 4.0%. Clearly, the Fed badly missed the mark when it came to its projections for inflation and interest rates in 2022.

This turn of events is worth keeping in mind as the Fed gets set for its final meeting of the year on December 13th and 14th and gets set to release an updated Summary of Economic Projections (coming out of its September 2022 meeting the Fed predicted the Fed Funds Rate would hit 4.6% in 2023; it is most likely the December Summary will show that target moving higher still). We wonder – given growing evidence of waning inflation and a weakening US economy – if the Fed, after underestimating where the Fed Funds Rate would get to in 2022, might end up overestimating where the Fed Funds Rate might get to in 2023.

Percent

Variable	Median[1]					Central Tendency[2]					Range[3]				
	2021	2022	2023	2024	Longer run	2021	2022	2023	2024	Longer run	2021	2022	2023	2024	Longer run
Change in real GDP	5.5	4.0	2.2	2.0	1.8	5.5	3.6–4.5	2.0–2.5	1.8–2.0	1.8–2.0	5.3–5.8	3.2–4.6	1.8–2.8	1.7–2.3	1.6–2.2
September projection	5.9	3.8	2.5	2.0	1.8	5.8–6.0	3.4–4.5	2.2–2.5	2.0–2.2	1.8–2.0	5.5–6.3	3.1–4.9	1.8–3.0	1.8–2.5	1.6–2.2
Unemployment rate	4.3	3.5	3.5	3.5	4.0	4.2–4.3	3.4–3.7	3.2–3.6	3.2–3.7	3.8–4.2	4.0–4.4	3.0–4.0	2.8–4.0	3.1–4.0	3.5–4.3
September projection	4.8	3.8	3.5	3.5	4.0	4.6–4.8	3.6–4.0	3.3–3.7	3.3–3.6	3.8–4.3	4.5–5.1	3.0–4.0	2.8–4.0	3.0–4.0	3.5–4.5
PCE inflation	5.3	2.6	2.3	2.1	2.0	5.3–5.4	2.2–3.0	2.1–2.5	2.0–2.2	2.0	5.3–5.5	2.0–3.2	2.0–2.5	2.0–2.2	2.0
September projection	4.2	2.2	2.2	2.1	2.0	4.0–4.3	2.0–2.5	2.0–2.3	2.0–2.2	2.0	3.4–4.4	1.7–3.0	1.9–2.4	2.0–2.3	2.0
Core PCE inflation[4]	4.4	2.7	2.3	2.1		4.4	2.5–3.0	2.1–2.4	2.0–2.2		4.4–4.5	2.4–3.2	2.0–2.5	2.0–2.3	
September projection	3.7	2.3	2.2	2.1		3.6–3.8	2.0–2.5	2.0–2.3	2.0–2.2		3.5–4.2	1.9–2.8	2.0–2.3	2.0–2.4	
Memo: Projected appropriate policy path															
Federal funds rate	0.1	0.9	1.6	2.1	2.5	0.1	0.6–0.9	1.4–1.9	1.9–2.9	2.3–2.5	0.1	0.4–1.1	1.1–2.1	1.9–3.1	2.0–3.0
September projection	0.1	0.3	1.0	1.8	2.5	0.1	0.1–0.4	0.4–1.1	0.9–2.1	2.3–2.5	0.1	0.1–0.6	0.1–1.6	0.6–2.6	2.0–3.0

Stocks, bonds, and commodities (12/2/2022)

Security name	Last	QTD chg	YTD chg	12mo chg
S&P 500	4071.70	13.56%	-14.57%	-10.28%
MSCI AC World ex USA	287.73	16.47%	-16.44%	-13.66%
MSCI EAFE	1983.24	19.37%	-15.10%	-11.27%
MSCI EM	973.85	11.20%	-20.95%	-20.48%
Bloomberg Barclays US Agg	90.60	3.29%	-13.50%	-14.22%
Crude Oil WTI	80.34	1.07%	6.82%	21.25%
Natural Gas	6.22	-8.04%	74.92%	50.58%

Treasury rates (12/2/2022)

	Price	Yield
2Y	100.1 / 0.00	4.292
3Y	101.1 / 0.00	4.005
5Y	100.2 / 0.00	3.671
7Y	101.1 / 0.00	3.611
10Y	105.0 / 0.00	3.511
30Y	108.0 / 0.00	3.560

Weekly reports

This week (12/5/2022)

- Nov PPI NSA Y/Y
- Dec UofM Sentiment NSA

Week of 11/28/2022

- Nov ISM Manufacturing SA 49.0
- Nov Nonfarm Payrolls SA 263.0K

Source: US Federal Reserve

Brinker Capital Market Barometer

NOVEMBER 2022

Markets staged a much-needed comeback in October. Although the Consumer Price Index (CPI) remains elevated, year-over-year changes have slowed for several months, aiding sentiment. There was no Federal Open Market Committee meeting (FOMC) in October, fueling hopes of any sign of a policy change or reduction in the pace of interest rate hikes. Despite this, yields continued to rise, as the yield curve shifted upward in near parallel fashion. Economic activity showed resilience in the labor market and consumer sector and slowing in other areas such as housing. Both the US dollar and commodities eased off of their highs during the month. Third quarter earnings began in October, and early results were mixed as fewer companies than average beat estimates, but growth overall remained positive. Markets are entering the strongest seasonal period of the year in November, which has historically been amplified in midterm election years. Going forward, even the slightest monetary policy reprieve may have the power to support and build on October's rally.

SHORT-TERM FACTORS (< 6 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Momentum		●			Solid October gains across markets, but intermediate-term returns remain depressed
Trend		●			Markets have rebounded off of lows, but major indices remain below major moving averages
Investor sentiment				●	Surveys continue to show significantly more bears than bulls; tends to be a contrarian signal
Seasonality	→			●	Markets are in the strongest seasonal period of the year, particularly following midterm elections

INTERMEDIATE-TERM FACTORS (6-36 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Fiscal policy			●		Upcoming midterm election results will shed light on likelihood of major policy initiatives
Monetary policy		●			Rate hikes continue at a rapid pace; still unclear that the pace of hikes has peaked
Inflation		●			Headline inflation has moderated, but y/y numbers are still at very elevated levels
Interest rate environment		●			Absolute level of rates is moderate, but rate volatility and curve inversion are at historical levels
Macroeconomic			●		Labor market healthy and consumer resilient but wide array of economic data is decelerating
Business sentiment		●			Business confidence measures remain subdued with elevated inflation as a primary driver
Consumer sentiment		●			Consumer sentiment has rebounded over the past few months but near the lowest recorded levels
Corporate earnings	←		●		Earnings growth and the number of companies beating estimates continues to slow during Q3 season
Credit environment				●	Level of credit spreads at long-term averages, defaults remain low, credit conditions modest

LONG-TERM FACTORS (36+ months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Valuation			●		U.S. equity valuations near long-term averages; overseas markets below average valuations
Business cycle			●		Strong initial Q3 GDP release diminishes near-tearm recession risk
Demographics			●		Emerging markets possess more favorable trends overall than developed markets

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