What You Need to Know to Calm Your Recession Anxiety

Investors are wondering about the current health of financial markets, and for good reason: Every day, financial media and market commentators are discussing the possibility of a recession in the U.S. economy and the potential for further downside in financial markets.

Today we would like to do two things: Put the current economic conditions into historical perspective and, considering those conditions, highlight the importance of long-term investing.

In the first quarter of this year, the U.S. Gross Domestic Product (GDP) declined by 1.5%. That decline was a surprise, considering predictions of growth. Yet the decline resulted from unexpected inventory adjustments as well as a higher-than-expected trade deficit. With the Atlanta Federal Reserve's GDPNow forecast predicting a meager 0.9% growth in second-quarter GDP, there are concerns that the conventionally held definition of a recession – two successive quarters of negative GDP – is dangerously close.

This seems a good time to remember that the National Bureau of Economic Research (NBER) is the official arbiter of recessions. Their definition includes this important phrase:

> ***The NBER's traditional definition of a recession is that it is a significant decline in economic activity that is spread across the economy and that lasts more than a few months.***

With continuing jobless claims hovering at all-time lows, positive retail sales growth, and ISM Surveys meaningfully above 50, it seems far-fetched to conclude that we are currently in recession. However, investor and consumer confidence surveys are showing a large portion of the population is fearful that we are already in one. Their concern centers on high inflation and aggressive measures by global central banks to combat that inflation. U.S. GDP is important to the overall global economy, more so now with Europe's economy hobbled by the war in Ukraine and China recovering from its Covid induced shutdown.

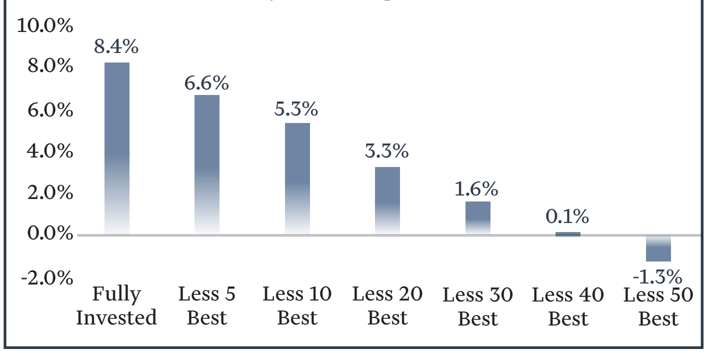
We don't think that NBER is likely to call the current situation a recession. Unemployment is 3.6%. Airplanes and hotels are packed. Corporate profits are still growing. We acknowledge that this could, and may, change. But it is important to reiterate that we don't believe the U.S. economy is currently in recession.

Even if we are wrong with our prediction, the implications for how to position investments do not change. Investors often think that a viable strategy is to see a recession on the horizon and then sell stocks ahead of the market's reaction to it. The problem with the strategy is that the market doesn't respond in the same way every time a recession nears.

A good example of that is this year. In past cases where the U.S. Federal Reserve has started raising interest rates, drawing forward fear of a recession, the stock market has rallied for at least two years afterwards. While we think that will be the case this time, the stock market is currently down 18% from its recent high in anticipation of it. Adding to the discomfort, bonds have produced losses in the same period, so their counterbalancing effect on stocks is not clear. This "nowhere to hide" environment may well be the result of the financial markets having already responded to a future economic downturn that may or may not even happen.

Attempting to time markets is not a good strategy. To illustrate that, we turn to one of our favorite charts.

S&P 500 COMPOUND ANNUAL GROWTH RATE
(January 1, 1995 - April 30, 2022)



Here the message should be clear: Trying to time markets/ recessions has the potential to drag down long-term returns significantly.

Compounding the point is that the best up-days are normally found within two weeks of the worst down-days. This suggests that the instinct as to when to trim equities will normally be counterintuitive to how the markets "feel." And while some may point out that missing the worst 5, 10, 20, etc. days would enhance returns, we point to the 8.4% buy-and-hold annualized return and suggest that every investor evaluate what their purpose is in the markets. The markets' long-term return is a proven way to enhance wealth and purchasing power. Trying to further enhance returns through market timing is really a form of speculation.

While speculation may occasionally be successful, very few people have proven it generates the same returns as staying in the markets through good and bad times.

Investing for the long run is a tried-and-true process to achieve meaningful returns. However, it is not easy. The length of the last economic expansion and bull market hid that truth for many investors.

We invite you to discuss your investment plan with your Cerity Partners advisor. It is our passion to help you through times like these.

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