Dynamic Wealth Advisors

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The Debt Ceiling Debate

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Do the Right Thing

We haven't had a shortage of headline risks this year with the turmoil in the banking sector, the potential for a recession, trying to predict the Federal Reserve's (Fed) next interest rate move and most recently, the debt-ceiling drama.

Debating the debt ceiling isn't something new. It seems to come up for discussion every couple of years, and there's always an impasse. There are heated debates, sensational headlines and increased investor fear. The point is, it always seems to come down to the last minute, but it always gets resolved. And the reason is simple: At the end of the day, no politician wants the U.S. to default. They recognize the importance of preserving the full faith and credit of the United States, which is key to maintaining its world leadership status, and ultimately the U.S. government will do the right thing.

Despite some of the short-term noise, as always, it's important to focus on the data. Both the stock and bond markets remain resilient. Much of the positive performance can be attributed to increased expectations of the end of the Federal Reserve (Fed) interest rate hiking cycle. In fact, the market expectations are that we have seen the last hike in May, AND we might see cuts before the end of the year.

We are starting to see signs of a "return to normal," highlighted by three key observations:

1. **Volatility Coming Down**: Volatility levels (daily swings in the markets as measured by the Market Volatility Index VIX) were elevated throughout 2022, but are starting to come back down to earth.
2. **Correlations Coming Down**: Correlations between stocks and bonds were at historically high levels in 2022, according to Morningstar data, but we are starting to see more traditionally expected behaviors: When stocks are down, bonds are up (and vice versa).
3. **Inflation Coming Down**: Inflation in 2022 was the highest we have seen in decades, but we have now seen 10 consecutive monthly drops in the Consumer Price Index (CPI), as measured by the U.S. Bureau of Labor Statistics.

Overall, we're seeing continued resilience from companies, consumers, and the overall economy and markets.

U.S. Market Resilience

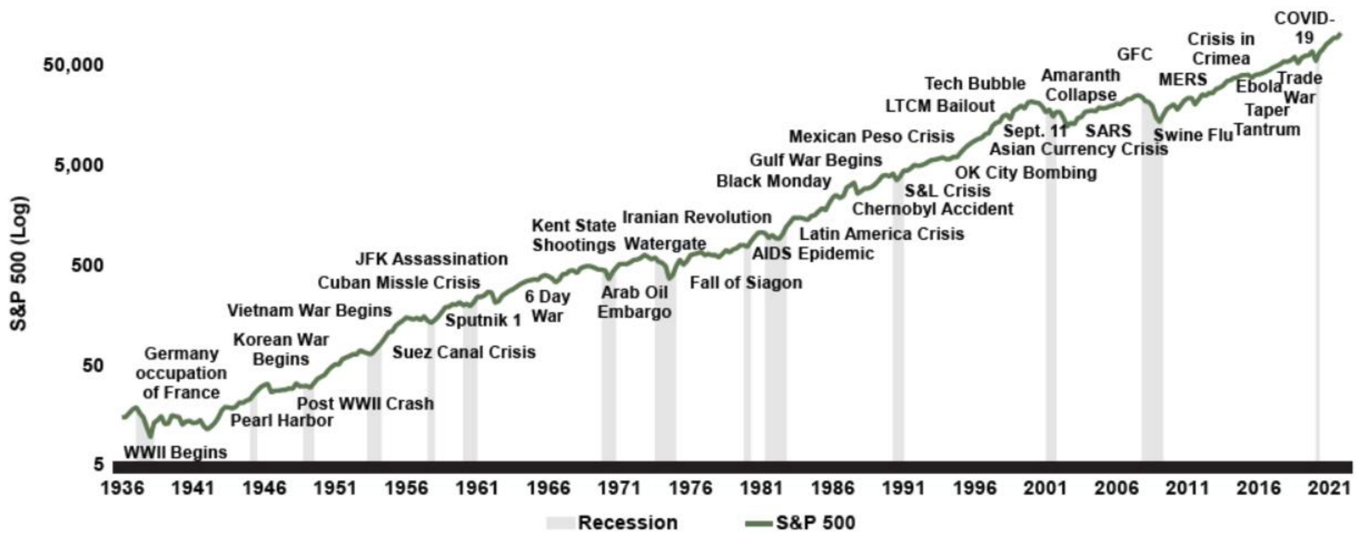
A famous quote from Benjamin Graham: "In the short run, the market is a voting machine, but in the long run it is a weighing machine." What Graham is trying to relay is that in the short-term, there is often market turmoil driven by news headlines and fear. But in the long-term, the market is driven by fundamentals (how profitable companies are).

The chart below, “Performance of U.S. Stock Market and Crisis Events,” shows significant crisis events back to 1936, compared to stock market growth. These events were certainly painful when they happened, but how impactful were they to long-term market performance? Taking a step back and looking at the long-term view paints a different picture:

1. **Investor Fear:** Fear can lead to emotional decisions and irrational behaviors for investors, which often translates to increased volatility and potential market drops.
2. **Fundamentals:** Companies grow their profits over time because consumers continue to spend more money as they earn more money. This relationship is unlikely to change any time soon.
3. **Long-Term Focus:** Consumer spending, corporate profits and the stock market are intertwined. They may be cyclical in nature, but the long-term trend shows consistent growth.

With this in mind, often the best thing you can do around crisis events is “nothing.”

Performance of U.S. Stock Market and Crisis Events
(S&P 500 Since 1936: A History of Moving through Difficult Times)



Source: St. Louis Fred & Morningstar Direct. S&P 500: Daily market return index as of 12/31/2021. Log: Lognormal Scale. Graph obtained from https://topforeignstocks.com/2022/07/21/performance-of-us-stock-market-and-crisis-events-since-1936/. Past performance is no guarantee of future results.

As always, Dynamic recommends staying balanced, diversified and invested. Despite short-term market pullbacks, it’s more important than ever to focus on the long-term, improving the chances for investors to reach their goals.

Should you need help navigating client concerns, don’t hesitate to reach out to Dynamic’s Investment Management team at (877) 257-3840, ext. 4 or investmentmanagement@dynamicadvisorsolutions.com.

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