Casey Mullooly: Hello, and welcome back to the Mullooly Asset Podcast. This is episode 408. I'm back in chair number one, I guess, this week. This is your regular host, Casey Mullooly. Shout out to Tim for filling in for me last week. We've got Brendan here in chair two.

Brendan: I'm more of a [inaudible 00:00:20] commentary guy. I missed you last week. Me and Tim held it down, but ...

Casey Mullooly: You guys did great.

Brendan: Good to have you back.

Casey Mullooly: Tom and I did a podcast about two months ago where we discussed the recent sluggish economic news and how the stock market typically moves ahead of the economy, both to the downside and the upside. We keep getting questions and we want to talk about this stuff and share how we're thinking about it and how we're viewing it. Apologies if you're getting tired of hearing the same old stuff from us, but that's our job is to communicate these things. The story is pretty much the same as it was two months ago.

Bren, you and Tim talked last week about the Fed's Jackson Hole comments and how we might be seeing inflation peaking, but the Fed is still talking tough and saying that they're far from done in terms of hiking interest rates. I also wanted to remind folks about how just because the Fed is hiking rates doesn't necessarily mean that it's having the... It's not like an immediate impact on the economy. I remember back when they first started hiking earlier this year, we talked about how that timeframe is usually nine months to a year for monetary policy to work its way through the economy. The first rate hike was in March and here we are in September, so it's really not going to be until 2023 where we're getting the impacts or the benefits.

Brendan: It could be the drawbacks too.

Casey Mullooly: Drawbacks of these rate hikes. I know we've seen the 10 year benchmark yield and mortgage rates have acted pretty [inaudible 00:02:18]. It seems like in some areas it is responding and in some areas it isn't.

Brendan: It's tough to tell. It could be kind of a placebo effect too, because it's like the Fed has been hiking rates and it's definitely feeding through to things like housing, I think, has shown signs of being impacted by mortgage rates going up, which is directly a result of the Fed raising their benchmark interest rate and bond performance reacting to moves in interest rates, same kind of a thing.

Also, some of the things that we're feeding into inflation earlier this year are just cooling off on their own. We've seen the price of oil really come down since the peak in spring, summertime and gas prices have begun to reflect that, and that's a component of inflation. How much of it is a result of what the Fed is doing and how much of it is just time healing the wounds, so to speak?

Casey Mullooly: Yeah, that's a good question. I know that we've seen some things like shipping times and used car sales and we're seeing some of those numbers roll over as well as, like you mentioned, things like oil and gas prices. That's all contributing to narrative that inflation is peaking, but it's going to be a while until we see these numbers come down. It's also going to be one thing to see it come down from where it is around eight, 9%. Five or 6% would feel pretty good relatively speaking, but the Fed's ultimate goal is to get it back down to 2%. I think it's still going to be a while until we see it back down in that range.

Brendan: I think that's what the market has been working through, to jump back to something you said at the beginning, it's, yeah, the story has been the same for a couple months now as the market has chopped up and down and tried to seemingly make up its mind whether or not it thinks inflation is peaking, or if the Fed is going to do too much to accomplish that goal of cooling off inflation and send us into a recession.

You said, I think it's correct, that the stock market moves in advance of the economic data in both directions. Basically it's trying to do that in real time now. That's the frustrating reality we have to live with is we get harsh comments from, some would say harsh comments, I would say it was the Fed saying the same thing they've been saying for the last couple of months. They said it last week, everybody got sad and stocks sold off because I think the interpretation was folks are worried that the Fed might take this too far and keep hiking at the magnitude they have been for the last couple of meetings through the fall and send us into a recession.

The market's trying to sniff that out ahead of time because the market does just that. It does it ahead of time. Then, on the flip side is we've gotten a couple of economic data points prior to last week's comments that showed, hey, inflation is coming down. Some people were like, "Wow, maybe the Fed is going to pull off this soft landing thing," and the market was up as a result of that. Again, the market trying to sniff out whether maybe we are through the worst of it after all, so we have to deal with that.

The result is up this week, down last week, vice versa. It's just this choppy market that we've been living through. If you look at a chart of what the S&P 500 has done over the summer months, it's a lot of back and forth in the same range. At times, it's felt like we've made a definitive move in one direction or the other. I think you're right, that if you look at it, we've been at the same point in terms of price levels a couple different times this year. It's felt different because earlier on in the year, we were on our way down. Then, through the back half of the summer, we were back on the way up.

The same price levels can feel different depending on which direction we're going in moving through them, but there hasn't been a lot to speak of in terms of direction. I think that's a change from the last couple of years, because we've gotten so used to those definitive market bottoms where we hit it and then we never look back. Exactly, the Vs. We haven't had a V this year, I don't even think. Remember we were talking about the shape of the economic recovery two years ago? It was like, "Are we going to be a U or a V or a W?"

Casey Mullooly: Or a K?

Brendan: Yeah, or a K. I don't even think we've had it. It's just been a very squiggly line in terms of at least what the market is doing as it digests what the economy is doing.

Casey Mullooly: Yeah. With all that being said, I wanted to share some interesting statistics from Charlie Bilello, who is a great financial writer that we all read and pay attention to. He shared this post last month about what it's like investing during recessions. I know we're not technically in a recession at this point, but I think the thought process is still helpful and the data points might help people think about how to do exactly that. Since 1871, there have been 30 recessions in the US, averaging one every five years. I think that alone is a good statistic for people to keep in their back pockets.

Brendan: That's good context. I mean, just as an aside, we talk to people who are entering retirement about how to invest now that they're going to be living off of their money. I think to appropriately set expectations, we're coaching them to anticipate things like bear markets and recessions. Sometimes go hand in hand. Sometimes they are separate things. Over a 20, 30 year retirement, we're going to go through several of those, right? We should expect it, and we build our plans expecting those things. We're not expecting to jump in and jump out and miss all of them as I think [inaudible 00:08:33].

Casey Mullooly: It's funny you should say that.

Brendan: Yeah. The stats bear that out a bit.

Casey Mullooly: Before we get to that, in spite of the fact that there's been 30 recessions in that 150 year time period, the average return of the S&P 500 is 6.9%, just under 7%. Like we said, it's all baked in there and that's after adjusting for inflation.

Brendan: Pretty good.

Casey Mullooly: Trying to sidestep the recessions, Charlie looked at, since the depression, if you were to time every single recession perfectly, if you were able to get out and then get back in, you would've underperformed just the buy and hold strategy. The timing strategy of getting out and then getting back in would've returned 10.6%, and the buy and hold strategy over that time period would've returned 11.7%. I know that back tests like these aren't reality, but it's a pretty counterintuitive statistic.

Brendan: You'd think it would be the opposite, and dramatically so. If we had perfect foresight and we could hop out, avoid recessionary periods in the stock market or in the economy, and as a result with our investments in the stock market, that we would do far better than just sitting tight and riding it out. It doesn't seem to be the case.

Casey Mullooly: This is because of that fact that the stock market moves ahead of the economy, and NBER is the one who declares when a recession starts and when a recession ends.

Brendan: They can only do that in hindsight, they're not telling us in real time that we're in one because economic data comes into us on a lag. Yeah. If you looked at the dates that recessions technically began by their definition, you were late getting out, and then you were probably late getting back in too because by the time they've declared it over, in a lot of cases, the market has bottomed in a dramatic fashion.

Casey Mullooly: During the last six recessions, this was 2020, 2008, 2009, 2001, 1990, 1981 to 1982 and 1980, during those last six recessions, the S&P 500 has gained an average of 61% from its low by the time the official end of the recession was declared by NBER. 61% move.

Brendan: It's pretty wild. I think that we hear a lot during difficult periods in the market, the idea of getting out until the coast is clear. Just to that point that you've made, it's tough to determine when the coast is clear. Often by the time we're all talking about the worst being behind us, it's really, really behind us. Usually the best time to buy is when we're still getting bad economic data, because it's only later on that we are able to see the incremental improvements that bring us out of those periods of time. It's so impossible to use that as an investing framework of getting out when things are scary and waiting for the dust to settle, it just doesn't work that way.

Casey Mullooly: Yeah. Just one more here from Charlie. Thanks again, Charlie, for putting all this information together. Let's say instead that you were early getting out and that you would get back in a year after the recession had ended, so you were out a year before it started and in a year after it ended.

Brendan: Right. Kind of in reference to what we just said. In this one, rather than being late getting out, like the first example that you walked through, in this one, you're early, but you're still late getting back in. You nailed the exit, but then you're a little too timid to jump back into the pool when things are looking better.

Casey Mullooly: Yeah. You would've averaged a 9% return per year, pretty good, but you would've underperformed buy and hold again, which would've returned 9.7% annualized per year.

Brendan: I don't think that the numbers fully bear out what that experience is like of trying to jump back in when you've made the decision to get out, because the decision to get out, you're taking in a lot of negativity when you're making that decision. You've kind of settled yourself in the bearish negative camp at that point.

To be able to do an about face and say that you're then bullish on the prospects of the economy and the stock market at a certain point, while the data still looks like garbage and stocks are probably still going down or just starting to go back up, we've even seen those narratives in the small bit of chop that we've had in the market here for just a handful of months in the sense that things start going back up again for a few weeks and people are like, "Oh, dead cat bounce, bear market rally." It's like, "How do we know? We don't know those things until after the fact."

Casey Mullooly: Or was that the bottom?

Brendan: Or it was... Yes, exactly. Trying to make those decisions, I think you're choosing to play a game that's difficult that you don't have to play to get good returns in the market.

Casey Mullooly: What's the old saying? Bulls make money, bears make money, pigs get slaughtered.

Brendan: That's it.

Casey Mullooly: Can't be both.

Brendan: That's true.

Casey Mullooly: One more statistic here, this one is from Ryan Detrick over at Carson Wealth Group. This one looks at how stocks do after midterm elections. Basically the idea is that another investing cliche is markets hate uncertainty, whether or not it's going to be a Democrat or Republican controlled Senate or House or what's going to happen. Basically it's the idea that markets, it doesn't really matter, and that markets just want to get through that uncertainty.

Brendan: Once we know, we can start planning. We all like to look ahead and think about how things might happen. Even though our predictions are probably not really worth much at all, it gives us some clarity about what the future might look like.

Casey Mullooly: Yeah. Ryan looked at how stocks do the year after midterm elections. This was going back to 1946 and every single year the year after midterm elections, the S&P 500 is up to varying degrees. It varies from barely up to up 33%, but it goes to show that there is some merit to the idea that stocks do actually hate uncertainty.

Brendan: Yeah. It's tough because there's always uncertainty if you're out there looking for it. I guess, in particular, it seems like the data bears out that this political uncertainty is... Maybe it is a factor. We get through the elections. We know who's going to have control, whether it's one party or the other, for the next couple of years and what the likelihood of any proposed legislation that's been on the table getting through, not getting through, that sort of a thing. If it's worked out that way since the '40s, then it's gone in every direction.

Casey Mullooly: It's gone both ways, yeah.

Brendan: Both parties. I think point well made that it's just one less thing that we have to worry about when we're through a period of time like that.

Casey Mullooly: Yeah. Everyone's got that to look forward to. We're recording this here in September, so we still have a couple weeks here or about two months until those midterm elections actually take place. As the information there from Ryan shows, we could be set up nicely for a good bounce back year in 2023. We know that we've been talking about this kind of stuff a lot here in 2022, but the one thing that all bear markets and all rough cycles have in common is that they all precede the next move up in the market and the next bull markets.

Brendan: They all end.

Casey Mullooly: They all end at some point in time. I think that's going to wrap it up here this week, Brendan. I know we don't have Tim on the mic so I'd be interested to get his take on this, but the NFL season starts tonight. What do you think the Jets are going to do here in the 2022/2023 season?

Brendan: I mean I would take 500 as some progress, but I guess they're going to be without Zach Wilson until week four, which was a surprise we heard about this week. I guess it's in Flacco we trust for a couple of games here. We'll see. They got some new, exciting rookies on offense. I think the team should be more fun this season. I'm not getting pinned down to a win total, this is the Jets.

Casey Mullooly: I'll circle back with Tim next week and report back. We do have to go back and revisit our Mets predictions because we're getting to the end here. I think I was the only one who predicted over a hundred wins.

Brendan: Wow, okay. Hey, you might be right.

Casey Mullooly: We'll see.

Brendan: I hope you are.

Casey Mullooly: Yeah. Thanks as always for listening. This was episode 408 of the Mullooly Asset Podcast. We'll be back with you for 409 next week.