Casey Mullooly: Hello, and welcome back to the Mullooly Asset Podcast. This is episode 398. I'm your host, Casey Mullooly. Joined here by Tom this week. Tom, how you doing?

Tom Mullooly: Good. Happy to be here.

Casey Mullooly: Happy to have you. So we're going to keep doing what we've been doing the last couple of podcasts here and talk about what everyone else is talking about. We're going to talk about the economy, inflation, the stock market, what we're seeing. I know we have some charts that we're going to share. So, lots to talk about and we're just going to get right into it.

Casey Mullooly: The big question out there in the economy is when is inflation going to slow down? And I just wanted to share three areas that kind of point to that happening at some point in the future. The first being copper or Doctor Copper as it is commonly referred to. So could you just explain to everyone out there, what copper is used to indicate and kind of why it's so important.

Tom Mullooly: Copper is one of the basic materials and it is a basic material that can be traded actively in the market. And so you can track the price of copper on a daily basis. A lot of folks in our industry like to call it Doctor Copper, because they will see copper moving up in price because there's demand in the midst of a recession. So we start to see prices rise for copper when there's more demand, builders are going to start putting pipes back in new homes. Copper's used in so many different places that when we see demand for copper pickup, and then we see prices for copper pickup, it's a clear indication, most times, that we're starting to see a pickup in economic activity. On the flip side, when we start to see the price of copper going down, it's an indication that things may be slowing down.

Casey Mullooly: Which is what we've seen happen this week. We saw the price of copper break down to a 52 week low so that it's trading at its lowest point in over a year. It's interesting though, because some would say in the usual context, yes, economic slow down is not a good thing that points to some larger issues. But in this instance, it could mean that demand is slowing, which means inflation could be slowing down, which means the Fed won't have to hike as aggressively, as they said to, which is kind of this black cloud that's just hanging over the market and the economy as a whole. So maybe good, maybe bad. We'll see how that shakes out.

Tom Mullooly: I think the concern that some folks have is that copper may be falling and they worry that could indicate that we're going into a recession.

Casey Mullooly: So, the next area to talk about here was the PMI Index, which is the Purchasing Managers' Index. So these are the people that are in charge of running factories and manufacturing across the country. So this is a survey of them about what their deliveries are looking like.

Tom Mullooly: It comes out every 30 days and it's an indication of orders that have been placed and they expect delivery in the next 30, 60, 90 days.

Casey Mullooly: Right. So that the PMI Index decreased from its May level. Which again, is assigned that demand is slowing, delivery times for these factories are going to decrease, which is going to smooth out some of the supply chain backlogs that we've seen, which have contributed so much to the inflationary landscape over the last year or so.

Tom Mullooly: And when we talk about the supply chain, it's easy to point to these maps of the Port of Los Angeles that show like an unlimited number of ships that are waiting to drop off cargo that was ordered six, eight, nine months ago. I'm sure my new refrigerator is waiting out there somewhere in the Pacific.

Casey Mullooly: Somewhere out there.

Tom Mullooly: Yeah. So people are not operating in a vacuum, they know that materials that were ordered three months ago, six months ago, eight months ago, they are on their way. It's not like these orders were canceled. People are still waiting for them. And so they know how to manage their inventory. And so we're going through this adjustment period, and this is part of what's making people lose their minds, is that the buyers at Walmart and Target have been getting destroyed, I think unnecessarily because of the high inventory levels that they reported last month. No, I think they're actually doing things right. They're saying, hey, we're going to take down our earnings estimates, we're going to take down our orders because we have so much inventory. PS, I got to believe for the next six months, Walmart and Target are going to have some pretty good sales.

Casey Mullooly: So the last area that I wanted to talk about was energy, which has been, I mean, you hear in a bear market that eventually the bears come for everyone. And I think the bears have been coming for energy and oil these last couple weeks. So just to kind of give a background of what we've seen in this market. This year we saw crude oil peak at $130 a barrel back in March and we've seen it move back down to around 105, that's what it's at today. And we've seen kind of the steam come out of that sector as well, over the last two or three weeks here.

Tom Mullooly: I'll also add that futures prices for delivery of crude in the next couple of months are now trading in the 90s. So it shows you the trend of where oil's going. I think the Fed is accomplishing a lot of what they have already set out to do. We did a podcast and I think it was in January where we talked about jawboning as an asset of the Fed. Sometimes just talking their game is enough to get people to change their habits or for businesses to change their habits too.

Casey Mullooly: Or for the market to react how it has and price all this stuff in faster than anyone thought possible.

Tom Mullooly: So I'll say just from my own experience looking at things, the market has priced in a severe recession. What if we don't get a severe recession? What if we get a mild recession? What if we get a very short recession? What if we don't have a recession? What do you think is going to happen to the market? I'll give you an example. Two years ago, stock market went down 35% in 33 days when we thought we were going to do 15 days to flatten the curve. We're just going to shut down the economy for an unknown period of time. And when that didn't really happen, look at how fast the market came back and then took off.

Tom Mullooly: So, for the listeners out there, just think. The market has priced in a severe recession, if we don't have a severe recession, how fast will the economy and the market come back? If we have a mild recession, what impact would that have? If we don't enter into a recession, what will that do?

Casey Mullooly: Yeah, the market peaked on January 3rd and we've kind of been treading water down in bear market territory, not that entire time, but it certainly felt like that the entire time. So we're six months into it already, almost seven months.

Tom Mullooly: I will add that, what Casey just said is really for the S&P 500. If you look at the NASDAQ, which is a lot of technology, those names stopped going up in April of last year. So they have been trending down now for 16 months, something like that. We're a long ways into this already, but also these things are the engines of growth.

Tom Mullooly: It's interesting, one of the things that both you and I looked at was charts and tweets people we follow, we see XBI, this is not a recommendation, but that's the Biotech Index ETF, that seems to have put in a pretty significant bottom and seems to be rebounding. That is probably one of the most aggressive things that you could see out there. We've also seen some of these other areas like internet stocks, Chinese stocks, IPOs, even that ARK fund that Kathy Wood manages, these things have stopped going down because they got destroyed for 9, 10, 12 months.

Casey Mullooly: These were the things that led on the way down, these were the things that were going down in March, April, May of last year, 2021. So the point being that those things have stopped going down, not necessarily going back up, but kind of putting in that bottom, so to speak.

Casey Mullooly: I kind of wanted to jump back to a point, I think what happened in March of 2020 with the COVID crash and subsequent explosion in the stock market, I think maybe kind of just like broke people's brains in terms of like what to expect from bear markets and then rallies and how fast the market moves. I mean, I've said this on a couple videos that I've done over the last couple weeks where just because it happened that way in 2020 doesn't mean it's going to happen this time.

Casey Mullooly: We saw, it was Brendan's birthday, February 19th, that was the high. And then four weeks later, March 23rd or thereabouts, was the bottom. And then we were at all time highs again in the summer, probably like July or August. But point being that just because it happened that way doesn't mean it has to happen again that way. But I think a lot of people were expecting that we've had a couple dead cat bounces, bear market rallies, whatever you want to call them here. We had one in March, we had one in May where we're up 7, 8, 9, 10% in like two or three days. And everyone's like, okay, like it's backed. Then each subsequent time, it doesn't happen people lose faith even more and then they stop looking for bottoms and then the bottoms happen.

Tom Mullooly: That is pretty typical. If you listen to Bloomberg in the morning, Tom Keene, I love that guy. He's on all the time. He is asking all of the people that come on the show, when are we getting this cathartic puke where the market just spits everything out. I'm going to go out on a limb and say, we, I think we've seen it because people are looking for that one day event where the DOW is down 2,000 points. So the S&P is down 5% in one day that rarely happens

Casey Mullooly: Except in 2020.

Tom Mullooly: Yeah. Right. But we may see a period where we have five days in a row where the S&P loses 1 or 1.5%. And so you get to a point where we've had, I think, two weeks where the S&P 500 went down about 11%. I don't know, that seems to be a cathartic puke for me. It doesn't all have to happen on one or two days. So it can happen over a period of time where people just say that's it. I'm finished. I'm done.

Casey Mullooly: What do we see after that happens? So I know you have some stats here. I'm teeing you up here.

Tom Mullooly: Yeah this is [inaudible 00:12:40] Ryan Detrick. Thanks. He's the market strategist over at LPL Financial. So S&P 500 was down 5.8 last week, second consecutive week of a 5% plus drop in the S&P 500, and he wrote that's the bad news. The good news is a year after these kind of events. The returns have been solid up on average 28 plus percent, six out of the seven times. The only time that did not come true was after the 1987 stock market crash.

Casey Mullooly: It's like, we talk about pretty often the good usually follows the bad and vice versa. Yeah.

Tom Mullooly: So the other part of this, and I was on a conference call this morning, talking about investment returns. I sit on a finance council for a group here in New Jersey. We manage pensions and our target return is 6% per year. We have never hit 6% per year. And the discussion came up well, should we be making allocation changes today, or at least talking about making allocation changes today? And the answer is no, because going through a year like this, and I don't know where the year is going to finish, but going through years like this is the price that we pay for years where we made 20%, 18%, 12%, realize our target is to make 6. So we have these years where we're banking extra returns, and every once in a while, we're going to have a year where we have negative returns, that brings the average return down. So, it's okay.

Tom Mullooly: We do the same thing with our clients here in the office. When we talk about an average return during your retirement of 6%, we're baking into the cake years where we're going to make 12, 15, 18% and years where we're going to lose 20, 6, 5, 11, we're going to have years like that. So it all works out to be average.

Casey Mullooly: Last week was pretty rough. And Ben Carlson tweeted out some stats about how year to date the S&P was down 23%, over the last year it's down 11%. But over the last 10 years-

Tom Mullooly: 241% return.

Casey Mullooly: Right. That's with everything, every 5, 10, 15, 35% draw downs in there. Those are all in there. So, we talk pretty often about how you can't expect average returns every single year, you're not going to make a smooth six every single year. But if you don't rip up the script time and time again, we are confident that you are going to get those returns over 10, 20, 30, 40 years and beyond. It's hard to find optimist these days.

Tom Mullooly: [inaudible 00:15:54] would be one of the last ones out there.

Casey Mullooly: Yeah. So we're going to jump back to kind of what the Fed does and what they don't do. Because yesterday we saw Jerome Powell, the Fed Chairman.

Tom Mullooly: He was testifying in front of the Senate Finance Committee. Today, as we're recording this, he is testifying in front of the House.

Casey Mullooly: Correct. So this is giving the opportunity to the politicians to ask any questions they want. And you never really know why they're asking their questions, whether they're just trying to score some points with the people they represent or whether they actually believe the things that they're asking, but it was pretty head scratching to see some of the questions coming in yesterday, basically accusing Powell and the Fed of manipulating the prices of oil and food. And just like we talked about in the beginning, the Fed doesn't have control over the price of oil or the price of food. I just wanted to kind of talk about what they actually do, which is control the supply of money in the economy, also known as M2 to the more...

Tom Mullooly: Folks that took economic class.

Casey Mullooly: Economics, and this was one of the first things that they taught us was M1, M2. So M2 actually involves M1, it's basically just all of the liquid money in the economy. Anything that is cash or anything that is easily convertible to cash.

Tom Mullooly: Right. And so M1 is basically, if you were to think on local terms, it's the checking account. And so M2 is all the money in circulation. So it's checking and savings right on a local level. And so M2 really is the money supply, right?

Casey Mullooly: I know when the Fed cut rates back in 2020 and did those bailouts, everyone was like, oh, they're printing money. And now we're seeing the opposite end of that. So this was from Charlie Bilello and after 144 consecutive monthly increases of the US money supply-

Tom Mullooly: M2.

Casey Mullooly: M2. It declined in April for the first time since March of 2010. And the year over year growth rate of 8% is the slowest we've seen since February of 2020 and is likely to decelerate in the coming months. So I just want to clarify, we're not saying that it's not growing, we're saying that it's growing slower, which is kind of a microcosm of what the Fed is trying to do to the economy overall.

Tom Mullooly: So the financial experts on CNBC will talk about shrinking money supply, how they're tightening, they call a QT, quantitative tightening. And then they want to frighten people by talking about deflation. When inflation a few months ago it was 8.6 and at some point in the future, it'll be somewhere in the sevens and then the sixes. People will start talking about deflation. They should be using in the right terminology is disinflation, where you still have inflation but it's not as much as it was before and it has stopped going up. I think that's the main thing that people need to focus on.

Tom Mullooly: Same thing with the money supply. I want to just zoom back in on something that Casey mentioned a minute ago. So this is the first time that we're seeing a smaller growth in the money supply going back to March of 2010, that's 12 years of increasing money supply. So this isn't something that was March of 2020 related. This is a real shift in what the Fed is doing. And I know if you scroll back two podcasts ago, we spent a lot of time talking about quantitative tightening and how this is really going to be a non-story when the dust settles on all of this stuff.

Casey Mullooly: Yeah. I think everyone likes to think that whatever's happening now is going to continue forever in the future. But I think as we saw with their decision to raise 75, instead of 50, they're going to pay attention to the data and act accordingly. Which I think goes back to your point before about jawboning and whether or not they're actually going to continue to hike through this year and into next year. Everyone kind of thinks that's just going to happen in perpetuity. I don't think we're big believers of that here.

Tom Mullooly: Point being, I had someone call in Friday, this is now two weeks ago, when the market was down almost 1,000 points. And I said to this gentleman on the phone, he was flipping out. He was losing his mind. He's goes, this is never going to stop. Like the market is just going down, down, down, and it's not going to stop. I'm like, look, if we continue to go down 1,000 points a day in 31 days, we'll have nothing to talk about because the Dow Jones will be at zero. It doesn't work that way.

Casey Mullooly: We'd have a lot bigger problems on our hands too.

Tom Mullooly: Oh boy.

Casey Mullooly: All right. So that's what we've been seeing this week. Kind of some green shoots as we like to call it and some other people on FinTwit like to call it, we're kind of mining for green shoots these days. We'll be the last standing optimist in the room, that's kind of our job here as advisors and financial planners is to kind of keep everybody focused on what actually matters. So that's going to wrap it up for episode 398 of the Mullooly Asset Podcast. Thanks as always for listening, we'll be back with you next time.