Disciplined Wealth Management

09/30/2022 Quarterly Newsletter

Discipline is the key to success

With every approach to the stock market, bear in mind that there will always be periods of over-performance and periods of under-performance. Here at Disciplined Wealth Management (DWM), our goal is to concentrate your portfolio in the leading asset classes while avoiding the performance-sapping lagging asset classes; over the long term, our approach strives to provide you with better performance compared to the overall stock market average (the S&P 500) and with less risk. In summary – stay disciplined during times of under-performance; don't become emotional and abandon a proven long-term strategy during a usually short period of under-performance, but stick with it and let the strategy work for you. If someone says they are never wrong, they have just proven themselves otherwise.

General Commentary—

Expense of the Economy

Fed Chairman Jerome Powell’s speech at the central bank’s annual symposium in Jackson Hole, and following the most recent Federal Reserve meeting didn’t reveal much in terms of new information, but it did reinforce the Fed’s commitment to lower inflation at the expense of the economy. Powell said that restoring price stability would “likely require maintaining a restrictive policy stance for some time” and “require a sustained period of below-trend growth”. The remarks essentially quashed the hope for a Fed pivot, at least in the near term.

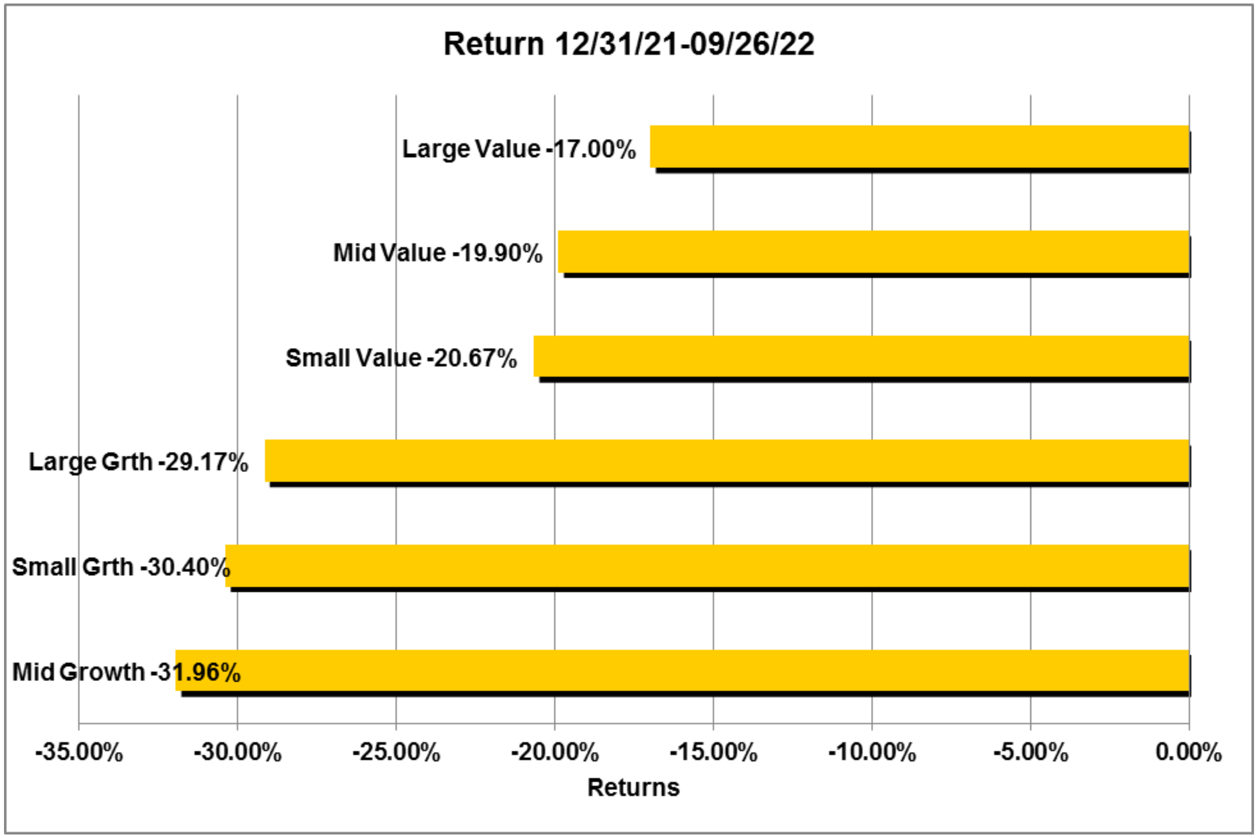
Growth has already substantially slowed, with the economy contracting in back-to-back quarters to begin the year. The Real GDP fell below potential in Q2 while inflation remained well above its five year trend. Stagflation has been a bearish scenario for stocks.

However, the market does not seem to be anticipating a long bout with stagflation. While CPI remains near its highest reading in 40 years, inflation expectations have remained anchored.

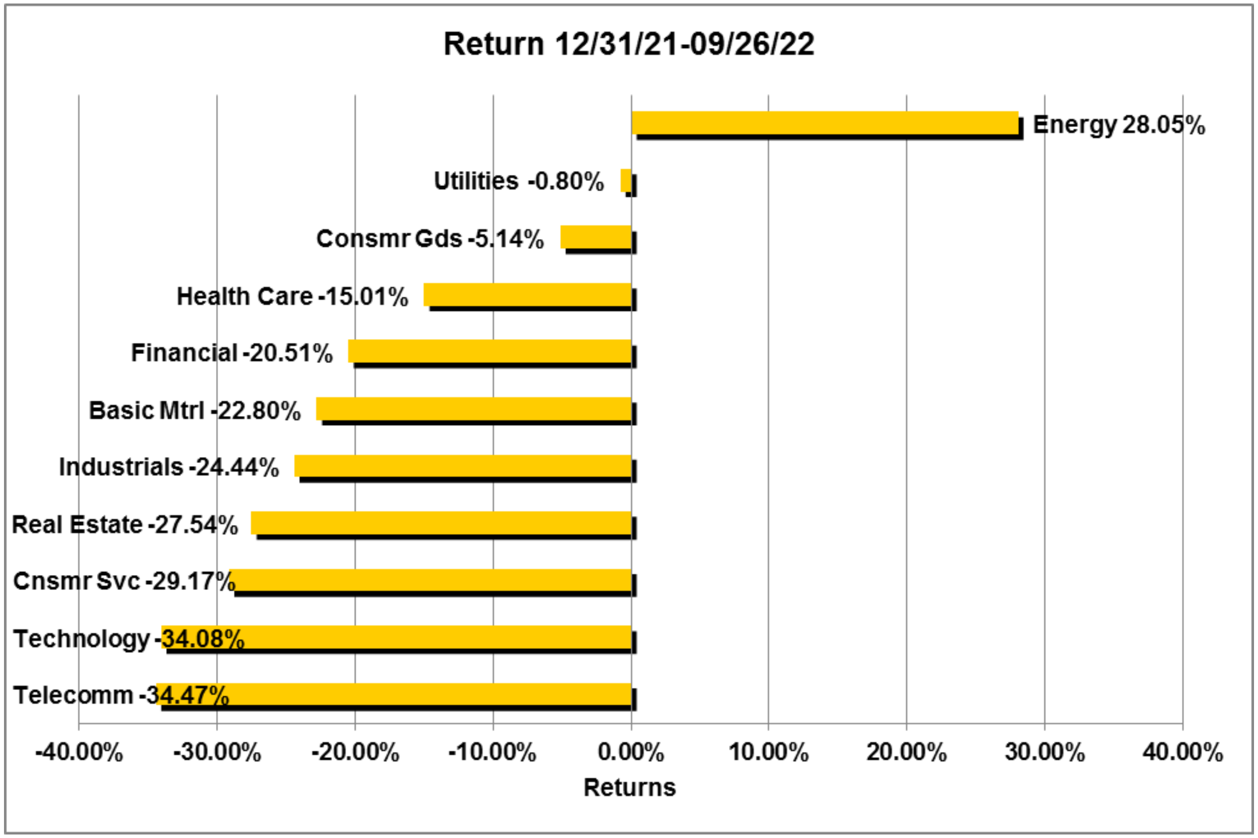
Demand destruction from the Fed should help bring down inflation in the near term. The supply side issues with respect to commodities, food, and labor, could mean that inflation remains a risk over the intermediate term.

As we go to press, the overall Market Environment Indicator (MEI) remains bearish, along with the Individual Fund Signals (IFS). We will continue to monitor these indicators and make the necessary adjustments. For an individual performance review, please call 303-471-5189. Please note that, in the following pages, the performance charts for certain asset classes showing year-to-date returns, are for illustration purposes only and do not reflect our Relative Strength Analysis (RSA) system.

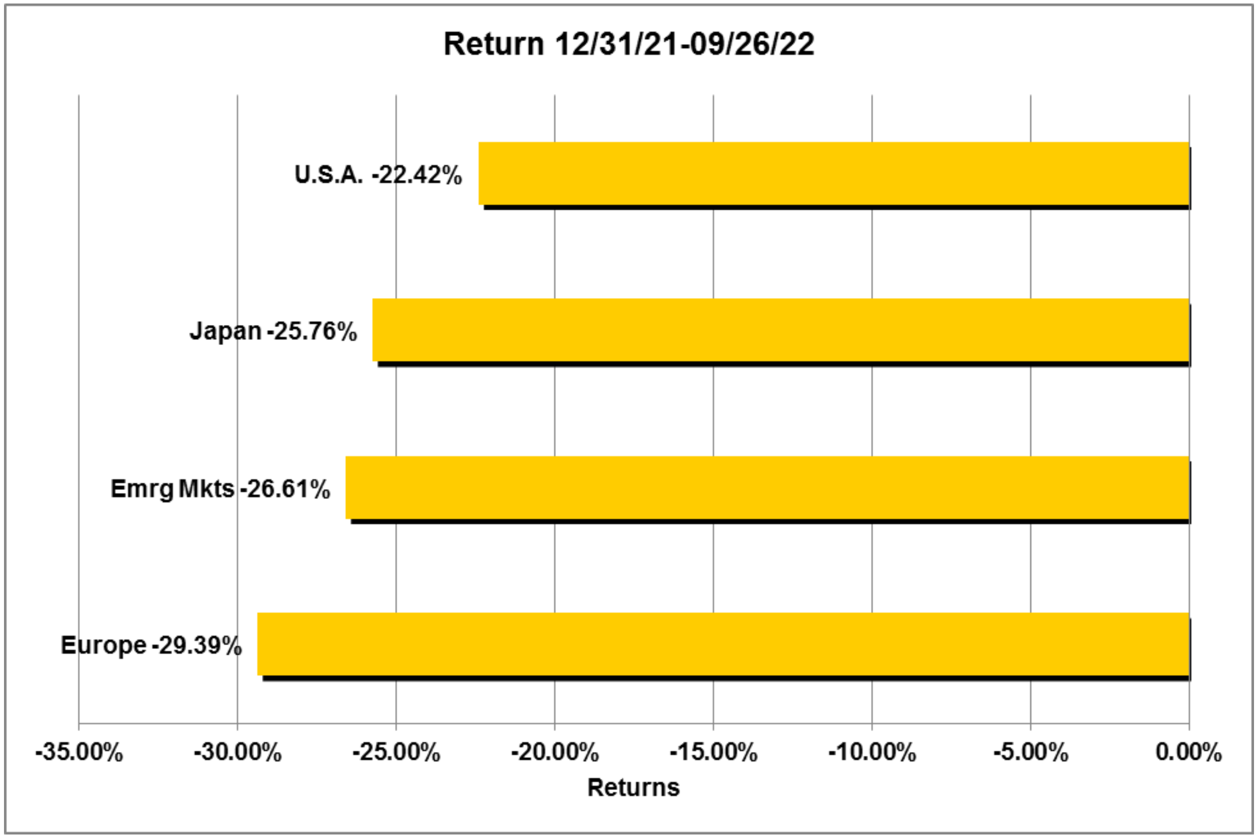
Style Boxes — As of September 26, 2022, Value continues its stronghold on the top three positions in my Relative Strength Analysis (RSA). Large Value maintained its spot at the number one position. Mid Value came in at number two, and Small Value in third place. Small Growth moved up one position to round out the top four. Large Growth experienced the biggest drop in my RSA, falling two spots to finish in last place at number six. As usual, we will continue to rely upon our time-tested RSA to guide our investments in Style Boxes.



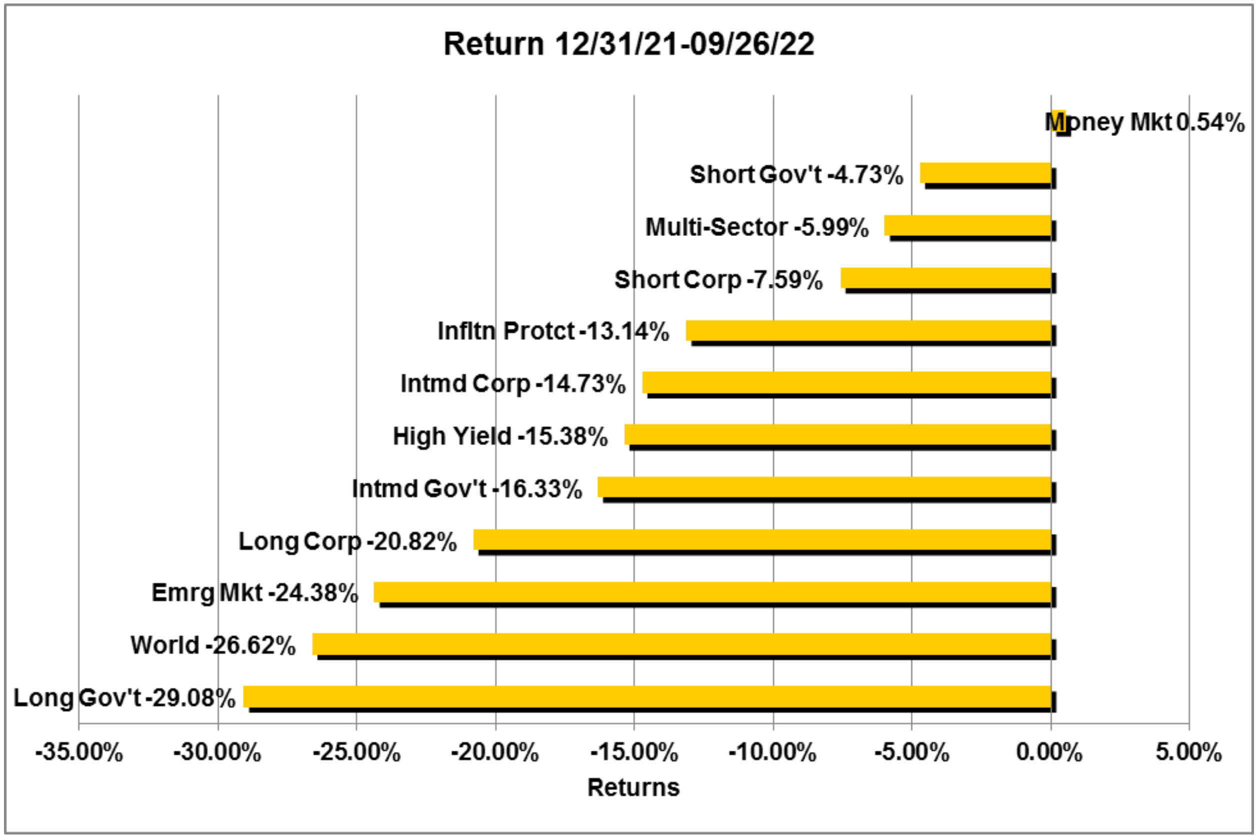
Sectors — As of September 26, 2022, Utilities and Energy swapped positions from last quarter's RSA. Utilities jumped two positions to claim the number one spot; Energy fell two positions to land in third place. Consumer Goods and Health Care experienced no movement in my RSA, finishing in second and fourth place. Consumer Services experienced the largest move up, jumping four positions to finish in seventh place in my RSA. Basic Materials fell the most, dropping five positions to finish tenth. As usual, we will continue to rely upon our time-tested RSA to guide our investments in Sectors.



Internationals — As of September 26, 2022, the top two positions switched places with the bottom two positions. The U.S.A. moved up two positions to claim the number one spot in my RSA. Japan also jumped two positions to finish in second place. Emerging Markets fell two positions to finish in third place, and Europe fell two positions to finish at the bottom. As usual, we will continue to rely upon our time-tested RSA to guide our investments in Internationals.



Bonds — As of September 26, 2022, Bonds have had a negative 2022 so far. With interest rates rising, bond prices move inversely to rates. With inflation hitting the highest level in forty years, it comes as no surprise the safest bond play (money markets) came in first place. This is a rare situation and doesn't happen very often. Still, when it does, that will be the only position to concentrate on as all the others are losing value. As usual, we will continue to rely upon our time-tested RSA to guide our investments in Bonds.



Forecast —

Depends on Recession

Where the market goes from here could depend on one thing: Is there going to be a recession? Deutsche Bank's Binky Chadha said there are two potential outcomes for the market resting on that question.

If the U.S. can avoid a recession, the S&P 500 should rebound from current levels and reach Chadha's year-end target of 4,750. That level is nearly 26% above where the index closed on 9/22/2022.

The outlook is far more dire if the U.S. economy does enter a recession. In this scenario, Chadha sees the S&P 500 falling all the way down to 3,000. That level is nearly 20% below where the index closed on 9/22/2022.

"While peak -to -trough the market had fallen by an average recession decline, historically the size of recession selloffs has been closely tied to both the severity of the recession (earnings decline) and the extent of initial overvaluation," Chadha said. This points to a decline of 35% to 40% for the S&P 500. The strategist warned that while the macro indicators Deutsche tracks aren't signaling a recession has already arrived, they are "consistent with a descent into recession." CNBC Pro

The volatility of the market has also been unique. The recent pullback in stocks that erased much of a summer rally also looks like an outlier relative to history, Emanuel said. "Not only did the 50% retracement rally occur in August, but a 50% decline from the August peak to halfway (3,981) to the June low then happened within days. Such a 50/50 whipsaw has happened only 4 other times since 1950 and confirms that the prevailing Bear Market has not ended," Emanuel wrote. . https://www.cnbc.com/2022/09/07/2022-is-unlike-any-year-investors-have-seen-before-how-to-play-it-from-here.html

A big difference in potential market moves, up 26% by the end of the year (4750 for the S&P 500 by year-end) or a drop of 20% (S&P 500 falling to 3000) from current levels. A big drop of another 20-25% would set the market up for even a bigger move higher. All the active tactical DWM portfolios are well positioned to either quickly participate in a new uptrend, with all DWM portfolios having large levels of cash, about 94%, to commit to new leaders. And if the trend continues down, those same high levels of cash will protect the portfolios from large losses until a new bull emerges.

Which one will be the case? No one knows for sure and only time will tell. DWM, for one, will continue to rely upon its tactical tools to stay in line with the market's fluctuations. Always remember: the key to investment success is to stay disciplined and flexible in an ever-changing market environment. The moment you start to second-guess your decisions is usually when you shouldn't.

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Sources: Style box data = i-Shares Russell Indexes. Source: Investors FastTrack.Sector data = DJ US Sector Indexes via I-Shares. Source: Investors FastTrack. International data = i-Shares for Emerging Markets, Europe, pan, S&P 500 Index for U.S.A. Source: Investors FastTrack.
Bond data = various bond exchange traded funds (ETF). Source: Investors FastTrack.