The Crescent Group

(214) 775-6401
us.rbcwm.com/thecrescentgroup

Wealth Management
The Crescent Group

RBC Wealth Management

The Crescent Group

Carsten Frederiksen, CFP®
Senior Vice President
Financial Advisor
Senior Portfolio Manager
Portfolio Focus
Direct: 214-775-6401
NMLS#: 1321563 City National Bank

Paul Hendershot, CFP®
Senior Vice President
Financial Advisor
Senior Portfolio Manager
Portfolio Focus
Direct: 214-775-6430
NMLS # 1370978 City National Bank

Lindsey Vickers, MBA
Senior Registered Client Associate
Direct: 214-775-6458

Randi Walker, CFP®
Senior Financial Associate
Direct: 214-775-6444

The Crescent Group website

Continued on page 2

August 2024 Crescent Commentary

Fork in the road: economic slowdown or recessionary warning?

During August, we continued to receive mixed signals from the economy, which came in the form of choppy economic data from July. Some of the positive data points were: retail sales doing better than expected; and inflation falling to a 2.9% annual rate, which was the first time since 2021 that the inflation rate fellow below 3%. Contrasting this good news was July jobs growth, which was much less than expected, as well as the fact that the unemployment rate increased to 4.3%. There are now 23% more unemployed Americans compared to a year ago. The all-important question is whether the increase in the unemployment rate represents a slowdown, or the early stages of a recession.(1)(2)

Over the past two years, we've seen headlines off and on about whether the increase in interest rates in the U.S. will lead to a "soft landing" where inflation falls and our economy keeps growing, or a "hard landing" where we experience a recession. Historically, it has taken several years for the full impact of higher interest rates to filter through the U.S. economy. For example, during the last time period when the Fed increased interest rates substantially, the Fed stopped raising interest rates in June 2006. But we didn't see the full impact on our economy until the Financial Crisis more than two years later. Thinking about a similar timeline today, the Fed stopped raising rates in November of last year, so we may have to wait until the end of 2025 or sometime in 2026 before we see the full economic impact of the interest rate increases.(3)(4)

Concerns about the possibility of a hard versus soft landing drove a volatile month for investment markets. As you may know, the U.S. stock market fell more than 3% on August 5th, which marked a decline of more than 8% from its high level set in July. This was a reaction to the mixed economic data we described above. It shows that popular investments are priced for perfection and are vulnerable to a steep correction if the future isn't perfect. This reinforces the need to diversify well beyond currently popular investments. If the economic data were actually to move beyond mixed and turn negative, then we would expect dramatic losses for the most popular and speculative investments, based on what we saw on August 5th. Naturally, now is the time to take action to proactively diversify and protect yourself from such a scenario.(5)

While public financial markets typically react to headlines, private markets can show what's going on under the surface. According to a recent Wall Street Journal article, the default rate on below investment-grade bonds and loans has roughly tripled since 2022. These bonds and loans are primarily used for private equity buyouts of companies, and reflect the impact that high inflation and interest rates have had on companies.(5)

As we mentioned, the big question going forward is whether the stress we've seen in public and private markets reflects a growth scare, or something more. Our view is that it remains an open question as to whether the U.S. economy is experiencing a slowdown that will resolve itself, versus heading into a recession. At RBC, we look at seven leading economic indicators that we use to evaluate the likelihood of a near-term recession.

In June, three of the seven indicators showed a recessionary level. In July, with the increase in the unemployment rate, the number of indicators showing a recessionary level has increased to four out of seven. As we mentioned above, the number of unemployed Americans is now 23% higher than it was one year ago. The impact of a higher unemployment rate goes beyond the decline in spending from those who have lost jobs. It also extends to increased precautionary savings and reduced spending by employed people who see others getting laid off. The combination of the steady rise in the unemployment rate over the past year, along with low consumer confidence, and the depletion of household savings built up during the pandemic, increases the uncertainty as to whether our economy will experience a soft versus hard landing.[6]

Balancing out the increase in recessionary indicators over the past several months, we've also seen several indicators of economic strength. Earlier, we mentioned July retail sales coming in better than expected, as well as the inflation rate falling to below 3% for the first time since 2021. Other positive data points include positive comments from corporate management, and data pointing to U.S. companies emerging from a mild earnings recession rather than heading into one.[1][6]

As we mentioned earlier, it's too soon to know whether the mixed economic data we've seen represents a temporary growth scare, or will lead to an actual recession. Given the uncertainty and delicacy of the situation, we continue to recommend balanced investment allocations that diversify well beyond currently popular investments. It's fine to own highly diversified amounts of investments currently perceived as "growth" investments, but at some point perceptions will change. And when that happens, adequate diversification will help protect you from adverse developments. Offsetting those perceived growth investments, we recommend a heavy allocation to high-quality, dividend-paying investments. Many of these investments are neglected in the current climate of exuberance, and that sets them up for attractive growth prospects going forward. Additionally, high-quality, dividend-paying investments can better withstand any further economic deterioration or a recession, should that occur.[6]

The Crescent Group: Paul Hendershot , CFP® | Carsten Frederiksen, CFP® | Lindsey Vickers, MBA | Randi Walker, CFP®
Forbes Best-In-State Wealth Management Team 2024

Sources:
(1) CNBC
(2) The Financial Times
(3) Board of Governors of the Federal Reserve System
(4) Reuters
(5) The Wall Street Journal
(6) RBC

The views presented herein are solely those of The Crescent Group, and do not necessarily represent the views of RBC Wealth Management. Current status of issues discussed in this letter is subject to change based upon market conditions and industry fundamentals. Clients should work with their Financial Advisor to develop investment strategies tailored to their own financial circumstances. Past performance is no guarantee of future results.

The 2024 Forbes Best-In-State Wealth Management Teams award was announced January 2024. Data as of 3/31/23. The award was developed by SHOOK Research and is based on in-person, virtual and telephone due diligence meetings and a ranking algorithm that includes: a measure of each team's best practices, client retention, industry experience, review of compliance records, firm nominations; and quantitative criteria, including: assets under management and revenue generated for their firms. Investment performance is not a criterion because client objectives and risk tolerances vary, and advisors rarely have audited performance reports. SHOOK's research and rankings provide opinions intended to help investors choose the right financial advisor and team, and are not indicative of future performance or representative of any one client's experience. Past performance is not an indication of future results. Neither Forbes nor SHOOK Research receive compensation in exchange for placement on the ranking. The financial advisor does not pay a fee to be considered for or to receive this award. This award does not evaluate the quality of services provided to clients. This is not indicative of this financial advisor's future performance.

Wealth Management