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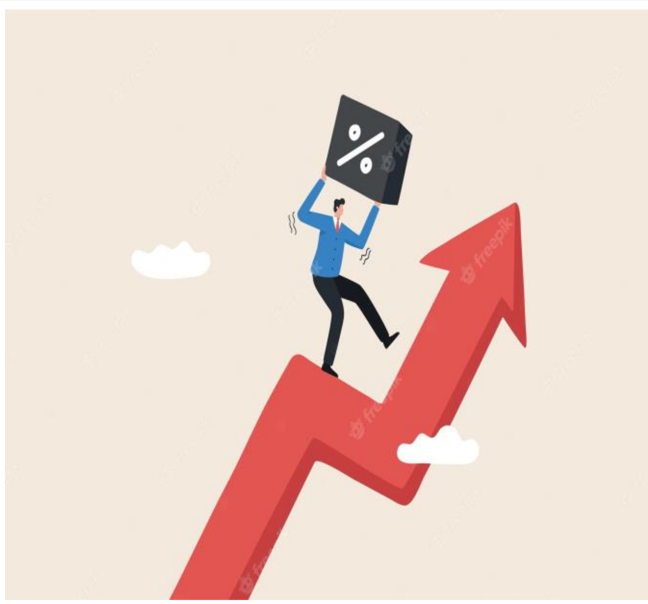
INSIGHTS & OBSERVATIONS

YOUR GUIDE TO FINANCIAL MARKETS AND INVESTMENTS **September/October 2023**

Welcome back. We are now 18 months into a rising interest rate environment and the repercussions continue and will do so long after rates peak. This shift by policymakers is a belated effort to combat inflation by returning rates to normal levels, although anyone under age 45 will likely be surprised by that description.

Over the past century rates have averaged about 6% in North America with plenty of fluctuations. The most notable of these wasn't 20% rates of 1980, but rather the decade of near zero rates preceding 2021. Hundreds of years from now economists will study the 2010–2020 period and marvel that we thought zero and negative interest rates were a wise policy.



The last year and a half has also been one of the quickest boosts in rates we've seen, as central bankers waited too long to move rates up and got left behind as inflation reawakened during the pandemic.

We are now expecting rate increases to slow and then pause before yearend, and should this transpire, it will help ease the adjustment period to the reality of higher rates which will take a few more years. Should the widely predicted but still elusive recession occur, we may even see rates decline somewhat early next year.

The two areas we're watching closely are government debt and the real estate market, since both are now quite exposed to rising rates given debt levels in each sector. They also share characteristics which allow them to be insulated from immediate effects of rising rates, but eventually mortgages must renew and government bonds come due, and they are then facing much higher interest rates costs.

The enormous distortions caused by the reaction to the pandemic are the cause of many unusual economic trends. Over time the excess government spending and all its side effects will gradually fade away, however our latest bout of inflation, sharply rising rates, and the massive increase in government debt will linger.

Investors should remain careful and recognize we are still in unique circumstances in some parts of the economy which means surprises are more common.

As a quick reminder, I am away from the 11th to the end of this month on a trip to Turkey. Yuki and Charlie will be here keeping an eye on everything for you.

Have a great month, take care.

Philip

September's Articles

Being 'good with money' is a rare trait. Few families can pass this along, very little on the subject occurs in school, and our basic human nature wiring will frequently sabotage our finances.

The keys to acquiring this skill are simple yet simultaneously hard to execute, which likely explains why so few people reach this state. Those who do get there often come from very humble beginnings. There is no 'secret', nor does one need to be exceptionally smart or talented.

In 1972 a professor at Stanford University conducted what would become a famous experiment called the Marshmallow Test. Young children were put in a room with a marshmallow on the table in front of them, and told they could eat it but if they could wait 15 minutes they would receive a second one. The researcher then left them alone in the room, returning in 15 minutes.

The children who were able to not eat the marshmallow and earn a second one were then tracked for years and were found to have greater life satisfaction and success by various measures. The children best able to distract themselves and resist the marshmallow had the skill of being able to defer gratification, also which turns out to be vital on the path toward becoming good with money.

As you'll read in the article linked below, author and financial planner **Jonathan Clements** delves further into the various attributes needed to enhance financial success. Much of what it takes simply involves discipline, patience, and setting appropriate priorities for ourselves. Sticking to these habits over the years will result in many happy outcomes.

https://humbledollar.com/2023/08/financial-superpowers/

Last month we included an article which discussed economic predictions and the misplaced pessimism which seemed universal in January. These forecasts – at least so far – have been proven wrong as the anticipated recession has failed to arrive and the adjustment to higher interest rates has gone smoother than expected.

This outcome isn't that surprising if we look at long-term economic trends. In the article linked below, author **Sam Ro** correctly points out that positive market and economic news is actually the norm, while recessions only occur a small minority of the time. Further, people usually feel and remember bad things more than good, so we underestimate the relatively consistent progress we've enjoyed most of the time.

We're also today dealing with a much more negative media and political landscape, making it even harder to believe the many gains made in recent years. Summing up, things are better than they feel for most of us, and this has been true for a very long time.

https://www.tker.co/p/july-retail-sales-good-economic-news

WHAT THEY SAID

"Risk and time are opposite sides of the same coin, for if there were no tomorrow there would be no risk. Time transforms risk, and the nature of risk is shaped by the time horizon: the future is the playing field."

Peter Bernstein, Against the Gods.