

August 2, 2023

Dear Valued Investor,

Making economic forecasts and stock market predictions can be humbling. It's especially tough when you expect stocks to go higher and get a big drop instead. The environment today is the opposite, but still tricky, as recession hasn't followed the chorus of predictions. In some ways, figuring out what to do now that stocks have gone up is as difficult as considering what to do when stocks are down.

Today's more fully valued stock market is pricing in an increasingly optimistic outlook for economic growth and corporate profits, but the economy still faces challenges that will likely lead to slower growth in the second half — and perhaps even a mild economic contraction. So why stay invested?

First, it's difficult to time the market. We've seen this play out several times in just the past few years. For example, few foresaw the strong market rebound that occurred as we came out of lockdown in 2020, or that inflation would become the ongoing problem that we're still dealing with today. We saw it again this past spring — professional portfolio managers and investors alike were broadly pessimistic about the stock market, particularly in the wake of several bank failures. Yet, stocks have gone virtually straight up since.

Another reason to stay invested is recent and encouraging economic data, which supports higher stock prices as the odds that the U.S. economy achieves a soft landing have increased. The U.S. economy grew 2.4% in the second quarter, a solid pace for a typical economic expansion these days. The job market remains healthy with near record-low unemployment. A resilient economy has fueled better profits for corporate America than most expected, setting up a likely end to the ongoing earnings recession in the current quarter.

Third, lower inflation may continue to support stocks in the months ahead as the Federal Reserve (Fed) winds down its interest rate hiking campaign. The Fed's preferred inflation measure (the core PCE deflator) dropped a half point in June to 4.1% and could potentially reach the mid-3s by year-end — not far from the central bank's 2% target. Lower inflation may also be good news for bonds by enabling the Fed to cut interest rates in 2024 as most expect.

Fourth is historical comparisons. Since 1950, stocks have gained an average of 40% one year following bear market lows. Nearly 10 months since our bear market low, our current bull market is up about 28% so far. Keep in mind, once the S&P 500 has gained 20% off a bear market low (which it did June 8, 2023), the one-year average historical gain is 18.9%. We're also in the best year for stocks within the four-year presidential cycle. In other words, more gains, and record highs, in the coming year are reasonable to expect.

Finally, for those worried that gains in the broad market have been driven by only a handful of stocks, stock market leadership has started to broaden out. We believe that's a necessary condition for the next leg of this bull market. Small cap stocks fared better than large caps in July and the average stock in the S&P 500 rose more than the index over the past two months.

For those who may have missed the rally, we would advocate for dollar cost averaging which is simply investing at regular intervals over a period of time. This can be a great approach as it takes emotion off the table. Consider maintaining a cash reserve so you can take advantage of dips that will inevitably come and use volatility as an opportunity to get back to long-term target allocations.

As always, please reach out to your financial advisor with questions.

Sincerely,



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LPL Research

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Dollar cost averaging involves continuous investment in securities regardless of fluctuation in price levels of such securities. An investor should consider their ability to continue purchasing through fluctuating price levels. Such a plan does not assure a profit and does not protect against loss in declining markets.

All index data from FactSet.

The Standard & Poor's 500 Index (S&P500) is a capitalization-weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

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