SIERRA MUTUAL FUNDS | OCEAN PARK ASSET MANAGEMENT

JULY 2023

Investment Insights

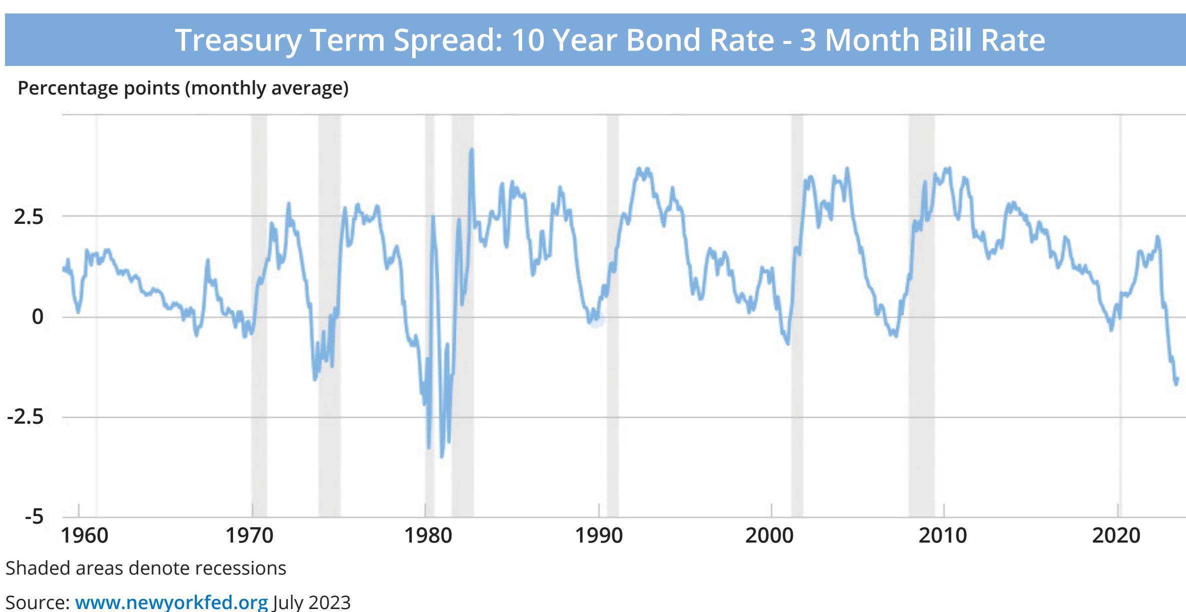
Disciplined Risk Management

Proceed with Caution

When the renowned investor Sir John Templeton famously said, "The four most dangerous words in investing are 'this time it's different,'" he offered a cautionary reminder to investors. This phrase warns against the belief that current market dynamics are entirely unique and will lead to outcomes significantly deviating from historical patterns. Despite this sage warning, market participants are often prone to embracing narratives that defy the patterns of history.

As the Federal Reserve and other central banks acknowledged that they had held onto accommodative monetary policy for too long in the name of combating the economic challenges of the pandemic, investors became increasingly anxious about the market implications of a necessary course correction to control inflation. Throughout the first half of 2022, as inflation pressure accelerated to levels not seen in over 40 years, it seemed unlikely that such inflation could be tamed without having a considerable negative impact on economic growth momentum.

To address the situation, the Fed launched an aggressive campaign to drain liquidity from the system by raising short-term interest rates and reducing its balance sheet or quantitative tightening. Calls for recession emerged under the assumption that such action would inevitably drag economic activity meaningfully into the red. Moreover, the increasingly inverted yield curve, a financial market signal that preceded every recession since the 1970s, was hard to ignore.



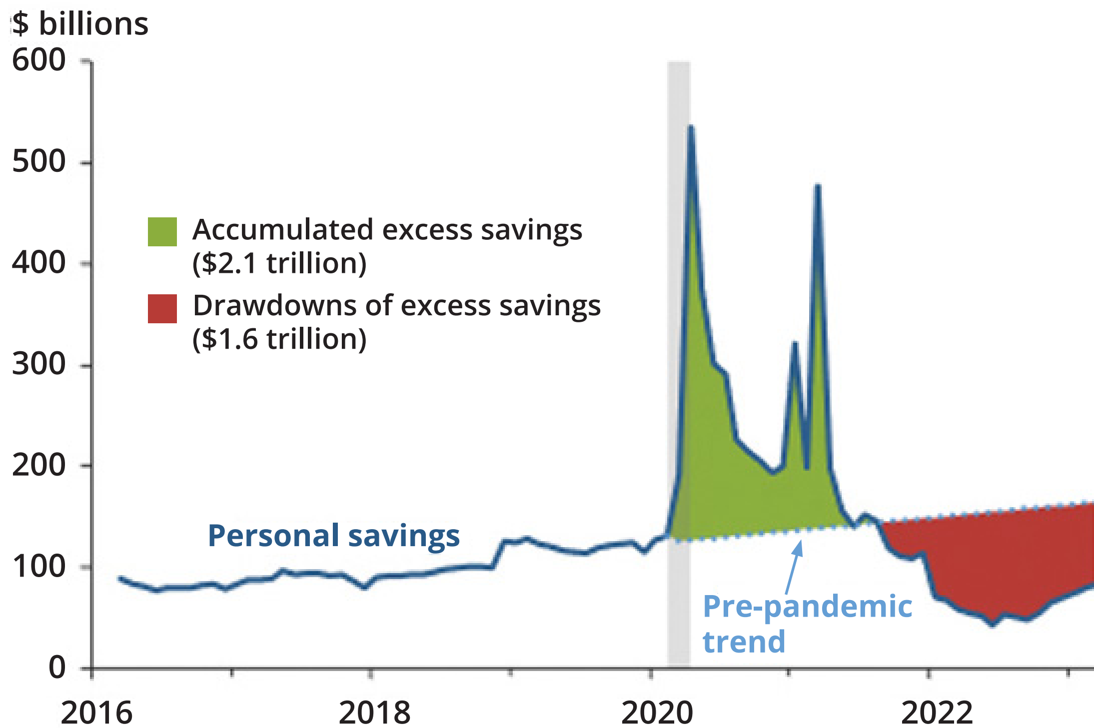
Shaded areas denote recessions

Source: www.newyorkfed.org July 2023

Many reacted to the possibility of an economic downturn by abandoning equity market risk. However, over time, economic growth appeared to be defying the typical reflexive response to falling liquidity. Despite higher borrowing costs and stricter lending standards, consumer spending remained relatively robust as jobs remained abundant. Even sectors of the economy highly sensitive to interest rates, like housing, showed surprising resilience.

Could this time truly be different? One explanation for the enduring momentum in the US economy is the strong financial position of consumers, thanks to unprecedented fiscal stimulus during the pandemic. Estimates indicate that US consumers saved $2.1 trillion from government support provided during the pandemic. These excess savings have been gradually spent since peaking in 2021, helping to mitigate the crowding-out effect of higher prices and borrowing costs.

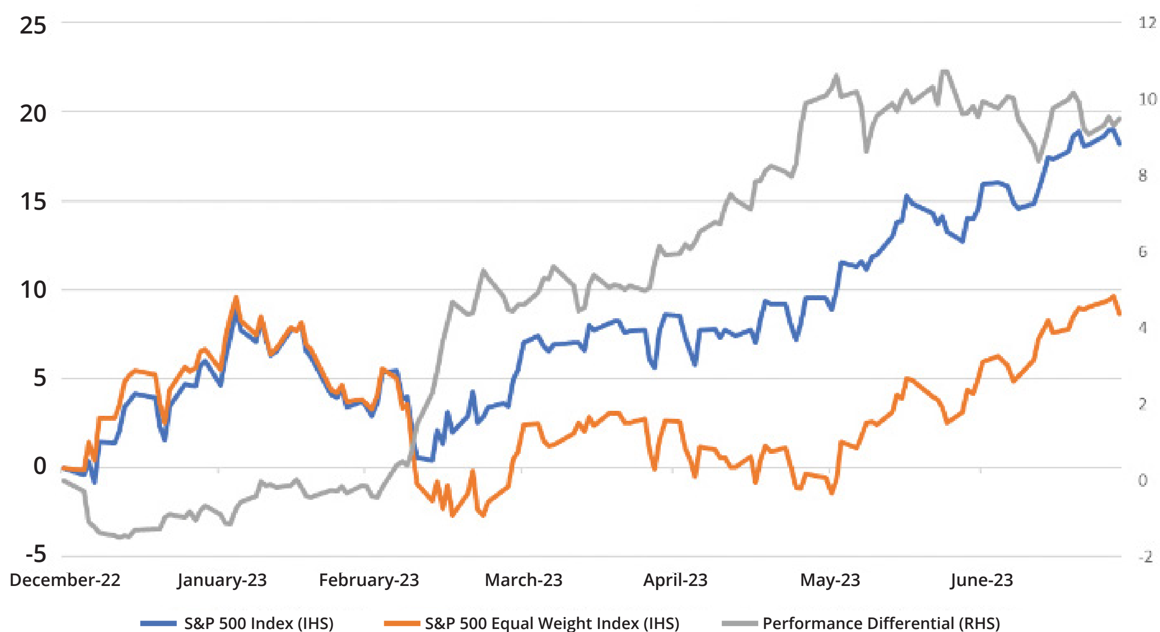
Aggregate Personal Savings Versus the Pre-pandemic Tread



Source: Bureau of Economic Analysis and author's calculations
Source: www.frbsf.org July 2023

Encouraged by surprisingly robust economic data, investors adopted a more optimistic outlook and embraced a risk-taking mood during the fourth quarter of the previous year. The risk-on rally continued with fervor over the first half of 2023, while barely pausing to fret over a series of large regional bank failures with potentially systemic implications.

However, beneath the surface, some signs of skepticism began to emerge when a strong January labor market report and a disappointing inflation reading raised questions about how hawkish the Fed would have to become to rein in inflation. Increasing uncertainty drove a performance divergence between tech-related companies with the largest weights in the S&P 500 Index and the rest of its constituents as investors perceived these stocks as least vulnerable to an economic downturn. Nevertheless, this cautious sentiment has waned since the beginning of June, as additional economic data supported the narrative of a 'soft landing.'



Source: Sierra Investment Management
Source: YCharts 7/27/23

Takeaway

For those market prognosticators who hold a pessimistic outlook, they argue that the good times won't last once excess savings are depleted and student loan forbearance ends later this year. In other words, from their perspective, it may not be so different this time; the recession might just be delayed, not avoided.

It is reasonable to acknowledge that the unusual economic distortions related to the pandemic may not have a perfect historical parallel, but one should keep in mind Mark Twain's reported quip, "History never repeats itself, but it does rhyme." While danger itself does not guarantee ill-fate, it should be respected.

James St. Aubin
Chief Investment Officer (CIO)

James St. Aubin, CFA®, CAIA®, is Chief Investment Officer for Sierra Mutual Funds and Ocean Park Asset Management. He will have oversight as to all activities of the Investment Management department, in collaboration with Sierra co-founders David Wright and Kenneth Sleeper. An accomplished investment management executive, his career of more than 20 years includes leadership roles in asset allocation, manager research and portfolio construction. James earned a Bachelor of Science in Finance from DePaul University and is a CFA® and CAIA® Charterholder.

RISKS AND DISCLOSURES:

Past performance is not an indication of future results and there is no guarantee that any investment strategy will achieve its objectives, generate profits, or avoid losses.

Investors should carefully consider the investment objectives, risks, charges and expenses of the Sierra Mutual Funds. This and other information about the Funds is contained in their prospectuses and should be read carefully before investing. The prospectuses can be obtained by visiting sierramutualfunds.com or by calling toll free 1-866-738-4363 (1-866-RETI-FND).

The Sierra Mutual Funds are distributed by Northern Lights Distributors, LLC, member FINRA/SIPC. Sierra Mutual Funds and Ocean Park Asset Management are not affiliated entities with Northern Lights. Ocean Park Asset Management, Inc. ("Ocean Park") is an SEC registered investment adviser. Registration does not imply a certain level of skill or training. For information pertaining to the registration status of Ocean Park, please call 1-844-727-1813 or refer to the Investment Adviser Public Disclosure website (www.adviserinfo.sec.gov).

SIERRA MUTUAL FUNDS | OCEAN PARK ASSET MANAGEMENT

©2023 Sierra Mutual Funds & Ocean Park Asset Management. All rights reserved.

1863-NLD-07312023