



CLA Outlook 2023 Economic, Market, Policy and Industry Insights

Staying the Course

December 7, 2022

We'll get you there.



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CLA Outlook 2023 – Staying the Course



Macroeconomic “top-down” analysis

- Despite higher interest rates and slowing economic growth that will impact areas such as housing, consumer spending and labor markets are resilient.
- **Manage your business: (tax, audit, global)**

Economic outlook

Equity, fixed income and alternatives views

- Stay invested as equities, fixed income markets and alternatives are now attractively valued along with attractive cash management yields
- **Maintain high-quality stance with an integrated approach to financial planning (private client services)**

Market outlook

Legislative and regulatory update

- With no single party in control, Congress and the Biden administration will likely focus on bipartisan priorities.
- **Carefully monitor regulatory guidance and actions that may affect your business**

Policy outlook

Industry outlook

2023 Outlook

Industry insights “bottom-up”

- Continued profitability seen due to top-line price increases, though expenses should be carefully managed to drive bottom-line growth.
- **Focus on efficiency (outsourcing, talent solutions, digital)**



CLA's Approach to Economic and Market Analysis

Our outlook uses the mosaic theory to formulate opinions and insights about general economic activity and the relative value of various investment options.

The **big macroeconomic drivers** of our mosaic are defined as:

- **Consumer finances** - Analysis of spending, borrowing and saving decisions made by households over time.
- **Business conditions** — Analysis of profitability, business optimism, inventory management, etc.
- **Labor market** - Analysis of unemployment, wage gains, nonfarm payrolls and job openings, etc.
- **Federal Reserve policy** — Analysis of the Federal funds rate and the Federal Reserve balance sheet.
- **Fiscal policy** — Analysis of government taxes, spending and regulation.

When analyzing the **financial markets**, our mosaic will compare and contrast **historic relative value**, tempered by current and expected macroeconomic conditions, specific to:

- **Equity markets** — Publicly-traded equities, large-, mid- and small cap, as well as developed and emerging international markets.
- **Fixed income markets** — Publicly-traded government, corporate and mortgage debt.
- **Private markets** — Credit, real estate and equity funds, generally formed as partnerships or LLCs.

Mosaic theory

- *A financial analyst gathers and interprets large quantities of information from many sources.*
- *Analysts seek and use such information to compare and contrast investment alternatives.*
- *Analysts are in the business of formulating opinions and insights that are not obvious to the general investing public about the attractiveness of particular securities.*

Source: Excerpts from CFA Institute, Standards of Practice Guidance

Agenda



- Introduction
- Economic outlook
 - Macroeconomic data
 - Consumer finances
 - Business conditions
 - Labor market
 - Federal reserve policy
 - Fiscal policy
- Financial markets outlook
 - Equity markets
 - Fixed income markets
 - Private markets
- Portfolio outlook
- Policy outlook
- Industry outlook



2023 Outlook — Executive Summary



Half Full

Economy: Robust consumer spending to continue.

Industry: Strong business profitability trends forecasted while the use of data insights and outsourcing should increase given labor shortages.

Financial markets: Attractive valuations in both equity, fixed income and alternative markets.

Policy: Congress and the Biden administration will work together on bipartisan and “must pass” legislation.

Portfolios: Well-constructed portfolios can participate in market upside while mitigating volatility to help achieve your goals.



Half Empty

Economy: Slowing GDP growth expected in 2023.

Industry: Tight labor markets and rising cost of capital may challenge unprepared business owners.

Financial markets: Expect more restrictive credit conditions as the Federal Reserve continues to withdraws liquidity in a bid to fight inflation.

Policy: A divided government may result in gridlock.

Portfolios: Recoveries take time and reward patient long-term investors rather than market-timers.





Economic Outlook

We'll get you there.

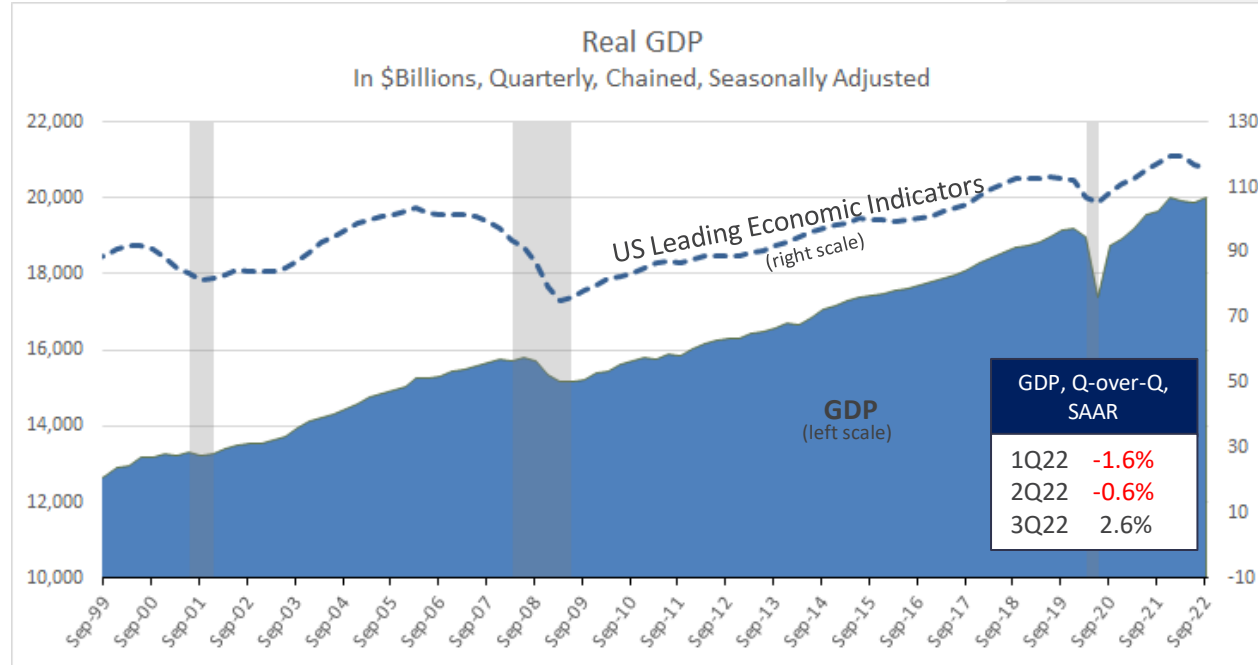
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Macroeconomy: GDP



GDP growth is slowing — but still resilient



Grey areas denote recessions.

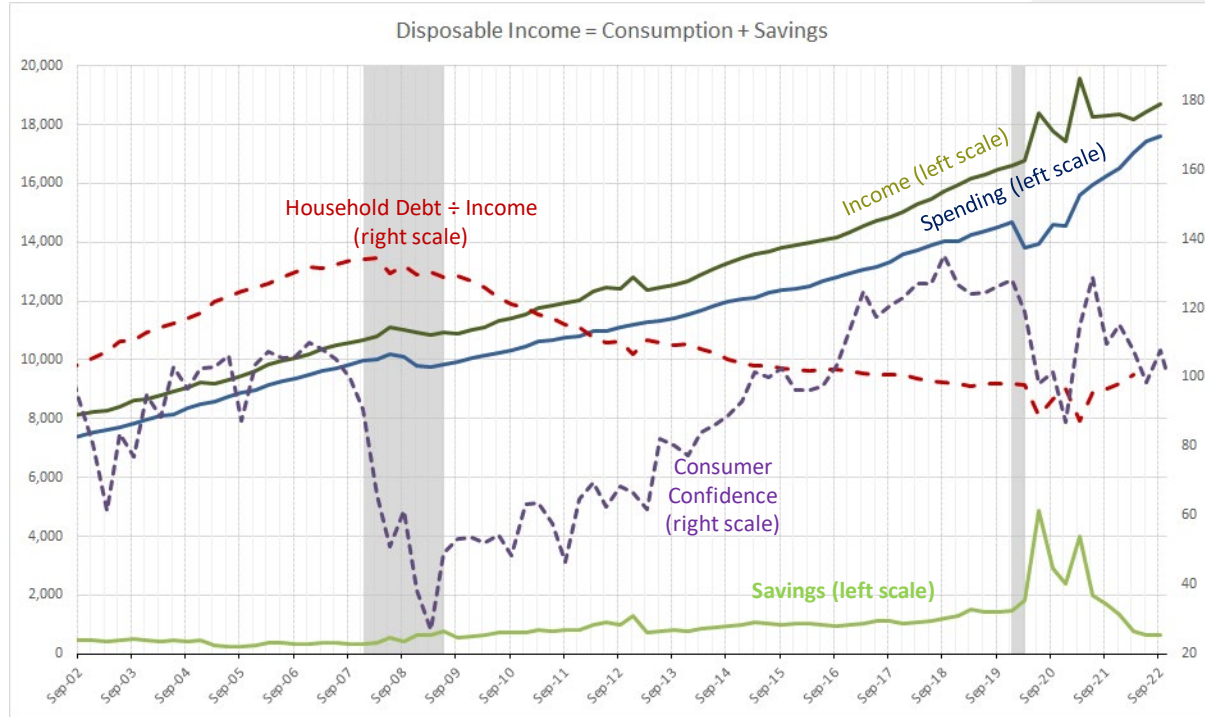
Source: US Bureau of Economic Analysis, Conference Board, National Bureau of Economic Research, Bloomberg, CLA Wealth Advisors



Macroeconomy: Consumer



Healthy consumer spending and income levels despite lower savings



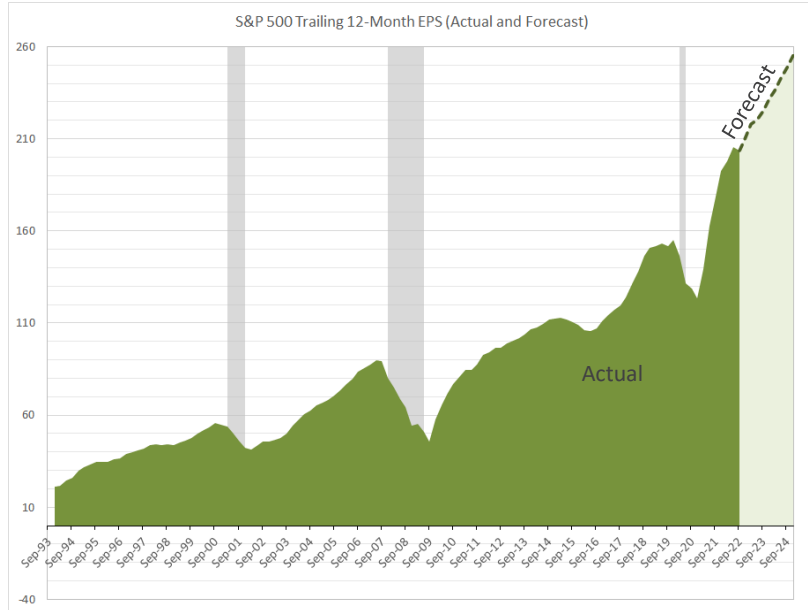
Grey areas denote recessions.



Macroeconomy: Business Conditions



Strong profits to continue though watch excess inventory building

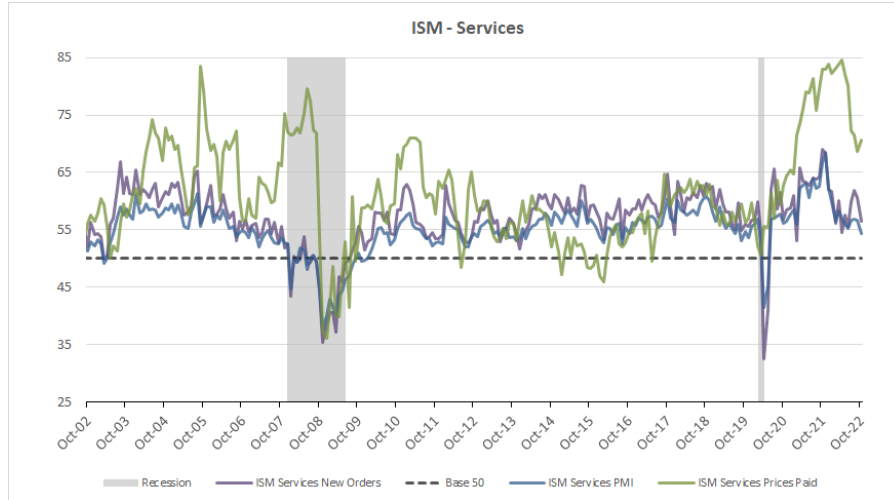


Macroeconomy

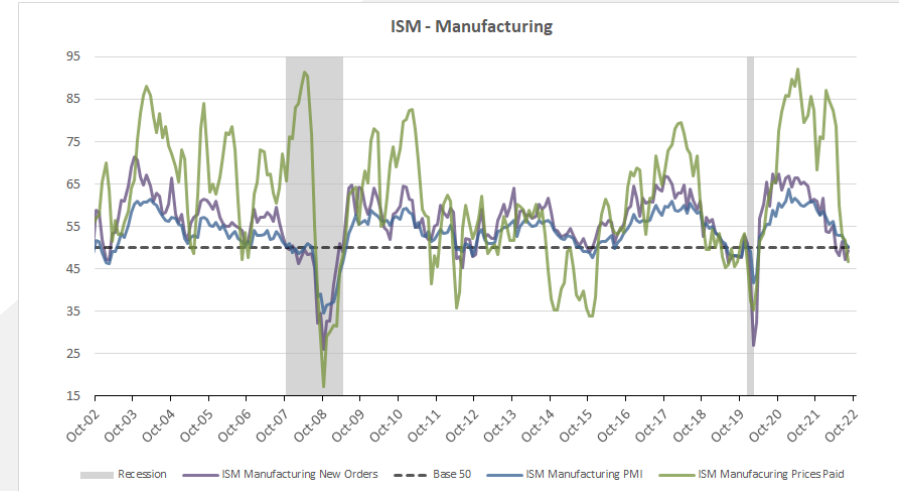


Business conditions — ISM services and manufacturing

With a diffusion Index, any reading above 50 (dotted line) indicates growth.



Services include Real Estate, Utilities; Construction; Education; Information; Transportation & Warehousing; Health Care & Social Assistance; Public Administration; Finance & Insurance; Management of Companies & Support Services; Professional, Scientific & Technical Services, Agriculture, Forestry, Fishing & Hunting; and Arts, Entertainment & Recreation; and Other Services.



Manufacturing includes Mineral Products; Petroleum & Coal; Transportation Equipment; Computer & Electronic Products; Printing & Related Activities; Plastics & Rubber Products; Primary Metals; Machinery; Food, Beverage & Tobacco Products; Wood Products; Apparel, Leather & Allied Products; Furniture & Related Products; Paper Products; Chemical Products; Fabricated Metal Products; and Electrical Equipment, Appliances & Components.

Grey areas denote recessions.

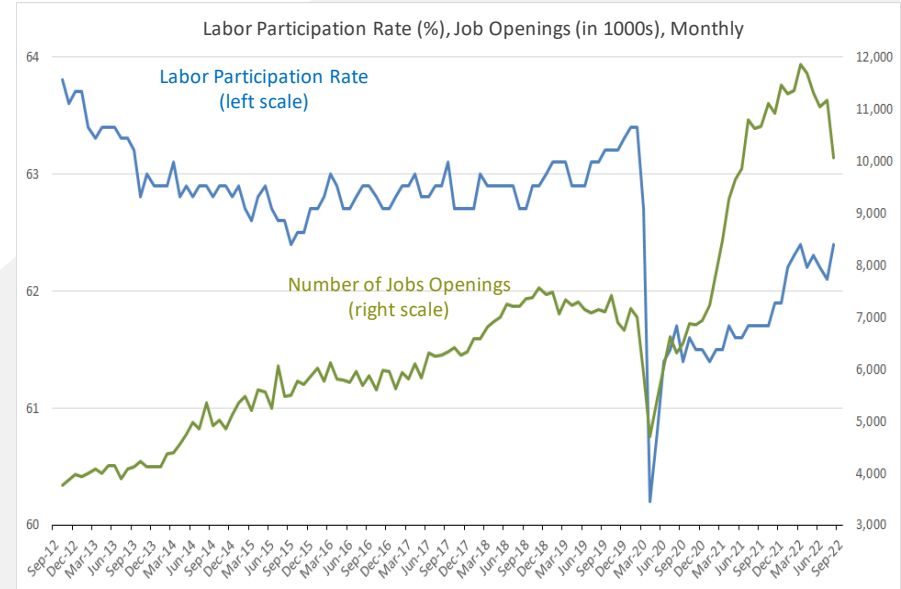
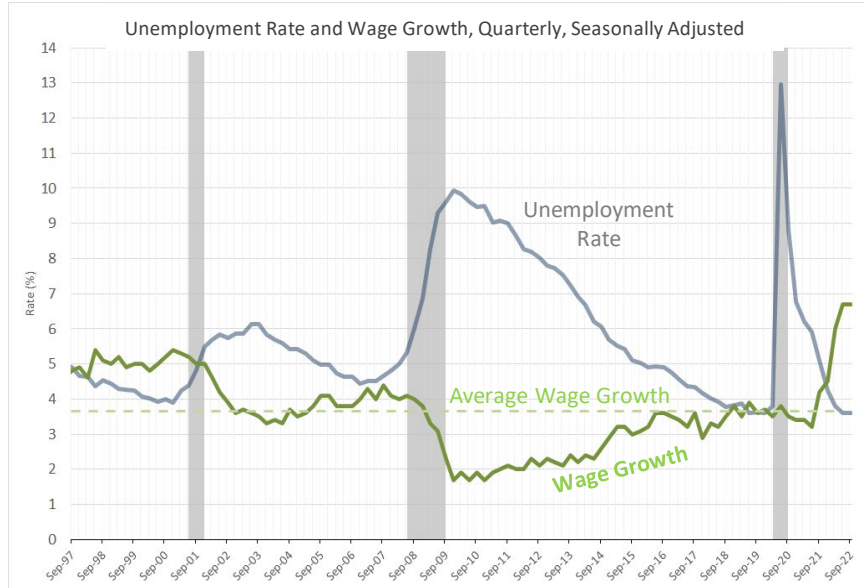
Source: Institute of Supply Management, CLA Wealth Advisors



Macroeconomy



Low unemployment remains, making it tough to find labor



Grey areas denote recessions.

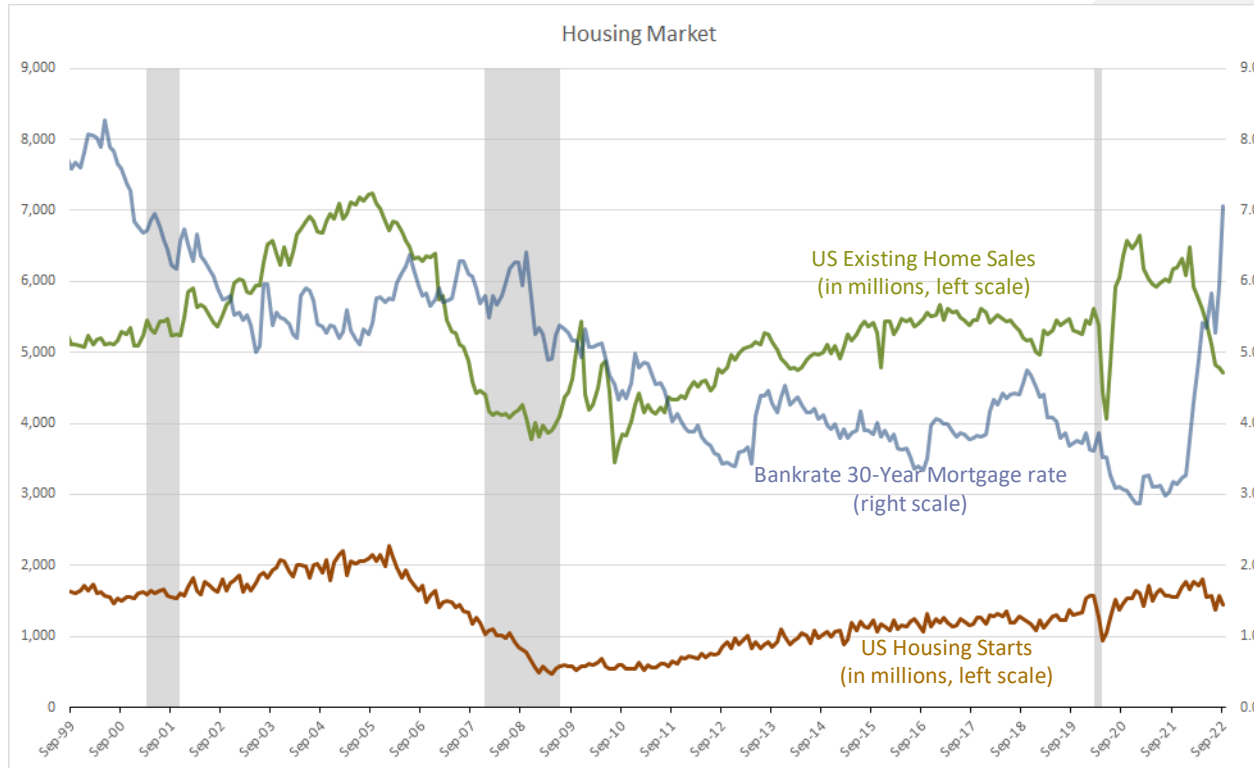
Source: U.S. Department of Labor, Atlanta Federal Reserve, Bloomberg, CLA Wealth Advisors



Macroeconomy: Housing



Home sales are starting to fall due to higher mortgage rates



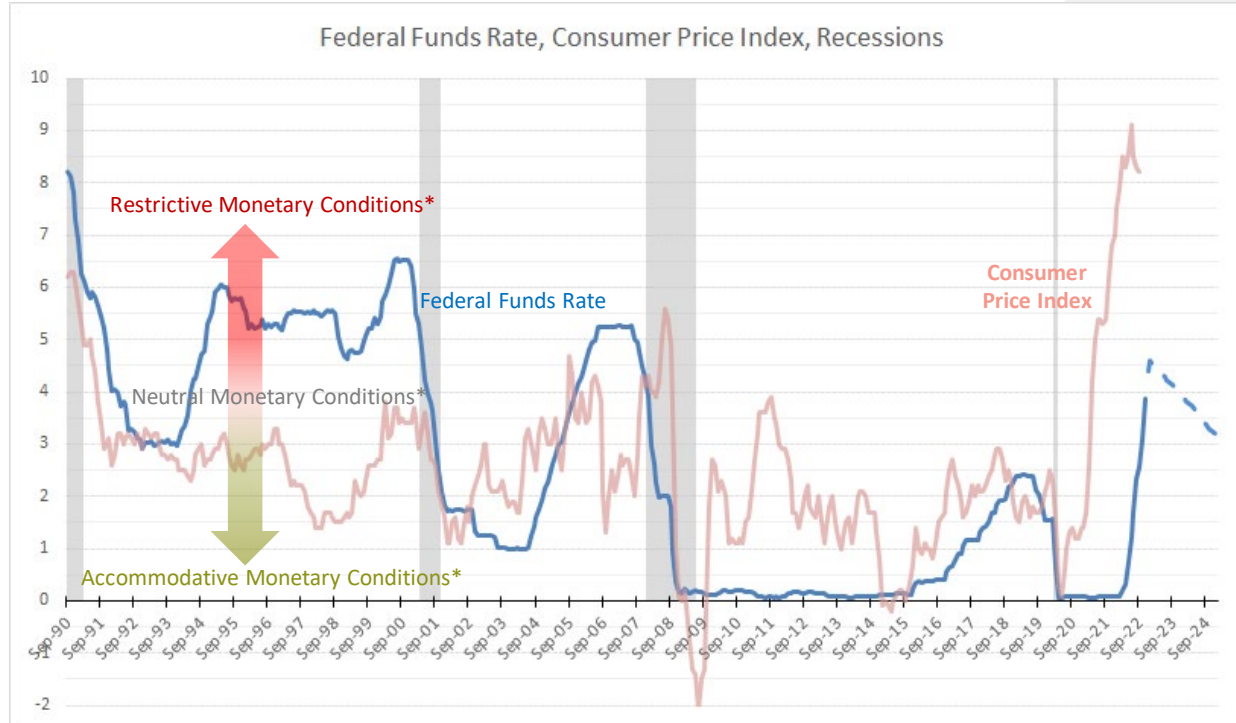
Grey areas denote recessions.



Federal Reserve Policy



The Fed may raise rates from 0% in 2022 to ~ 5% in 2023



Grey areas denote recessions.

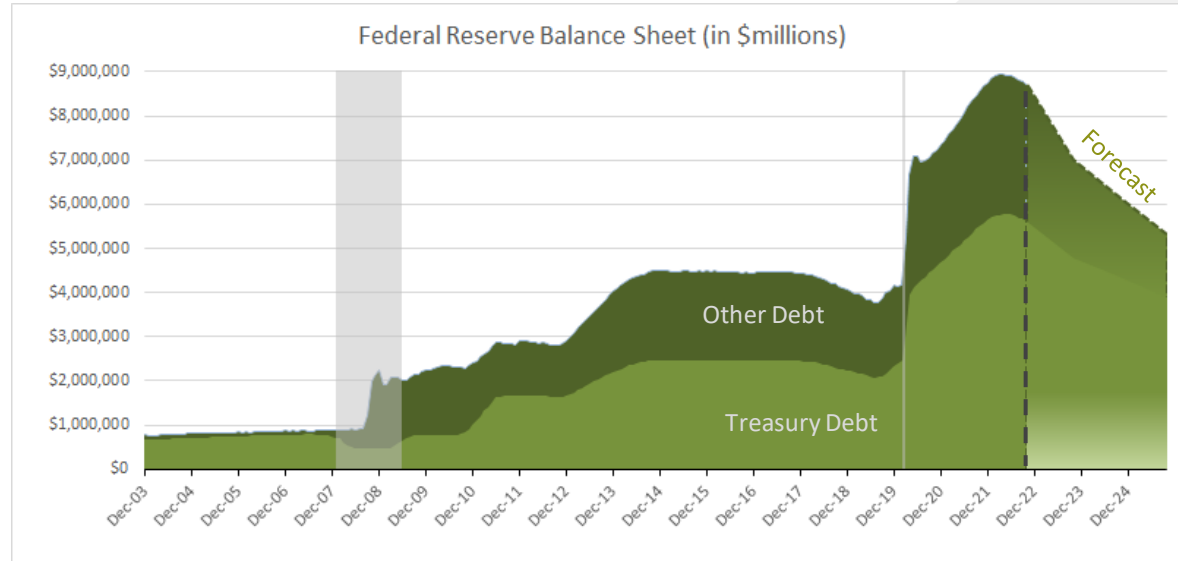
Source: Federal Reserve Board, Bloomberg, NBER, CLA Wealth Advisors



Federal Reserve Policy



Further tightening seen with \$95bln / month of balance sheet runoff



Grey areas denote recessions.

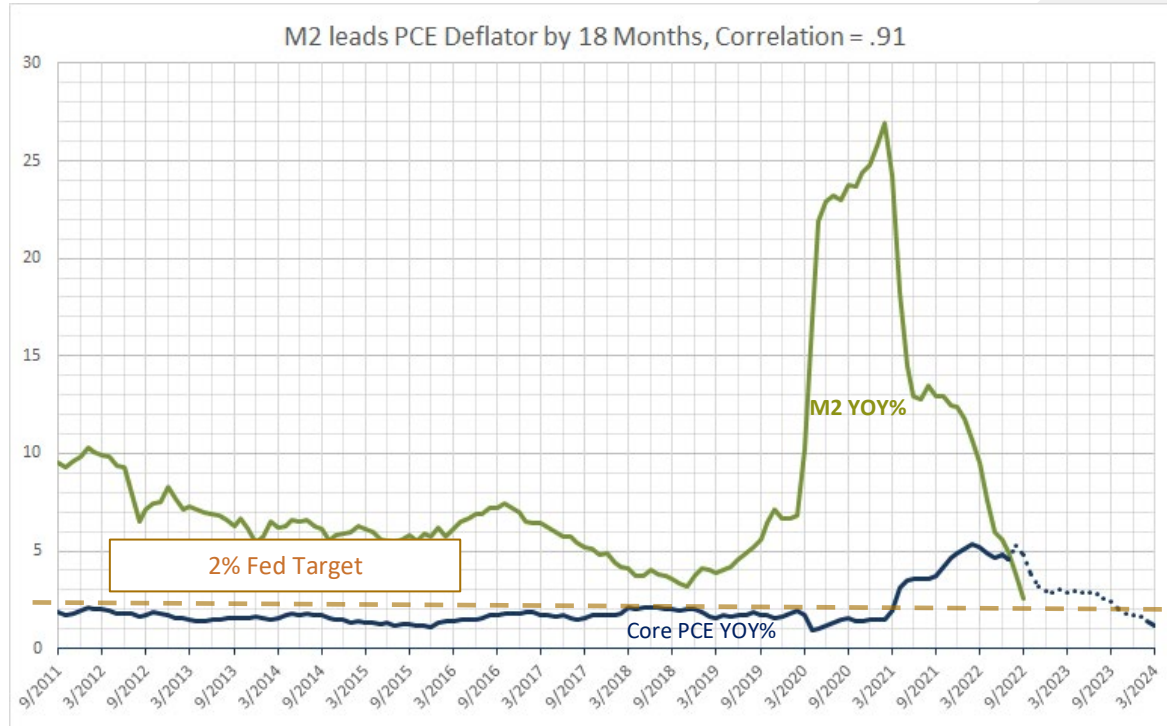
Source: Bloomberg, Federal Reserve, NBER, CLA Wealth Advisors



Federal Reserve Policy



Inflation has likely peaked and should normalize by early 2024



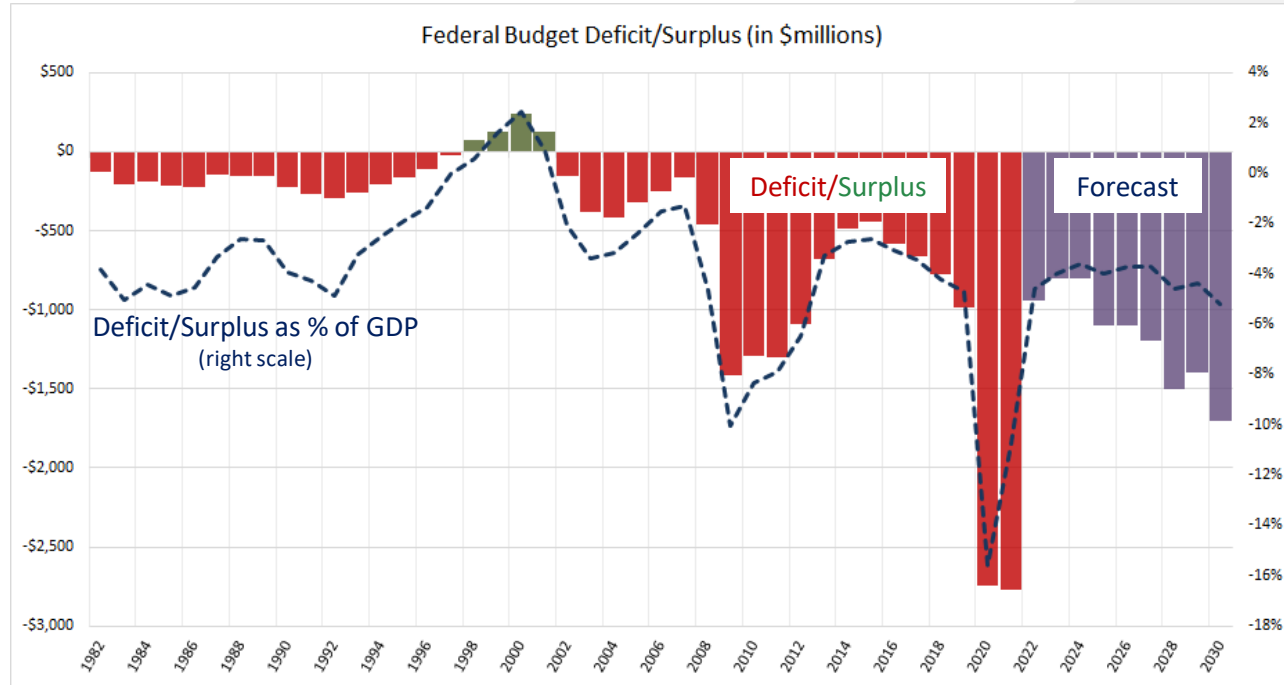
Source: Bloomberg, CLA Wealth Advisors



Fiscal Policy



Deficit spending set to continue after mid-term elections



Source: Bloomberg, CBOE, CLA Wealth Advisors



Economic Views — Summary



Half Full

Projected corporate profits remain robust.

The unemployment rate is low.

Inflation appears to have peaked.



Half Empty

Tight labor markets indicate possible headwinds to future growth and additional wage pressures.

The Fed has stated its intention to continue its “tightening” cycle (reducing its balance sheet and raising the Fed funds rate) to fight inflation.

Inflation is forcing consumers to reduce savings and tap lines of credit in order to keep up.

Federal deficits are projected to remain high, which could “crowd out” the private sector by driving up borrowing costs.



Financial Markets Insights

We'll get you there.

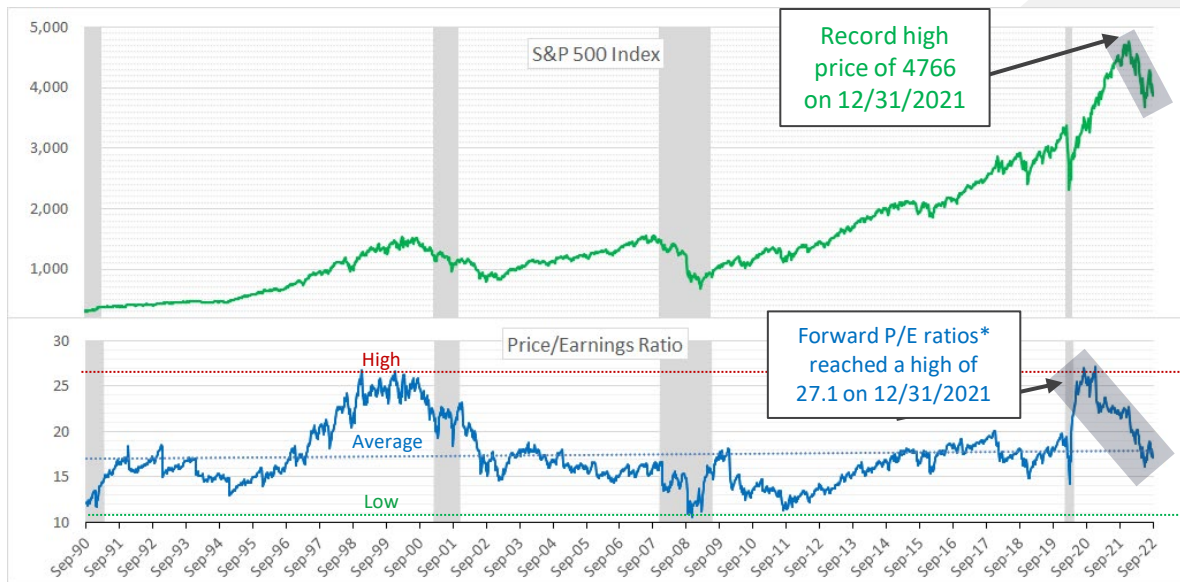
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Equity Markets



The equity sell-off now returns valuations back to attractive levels



Grey areas denote recessions.

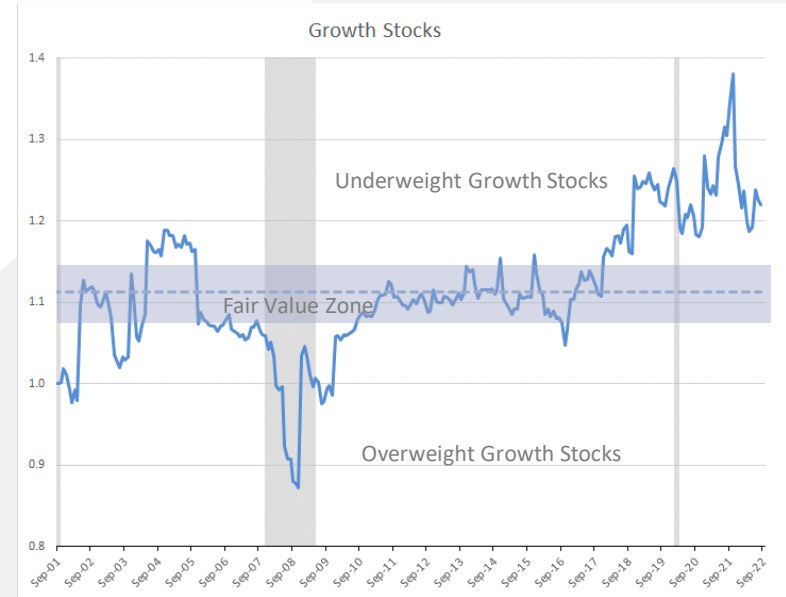
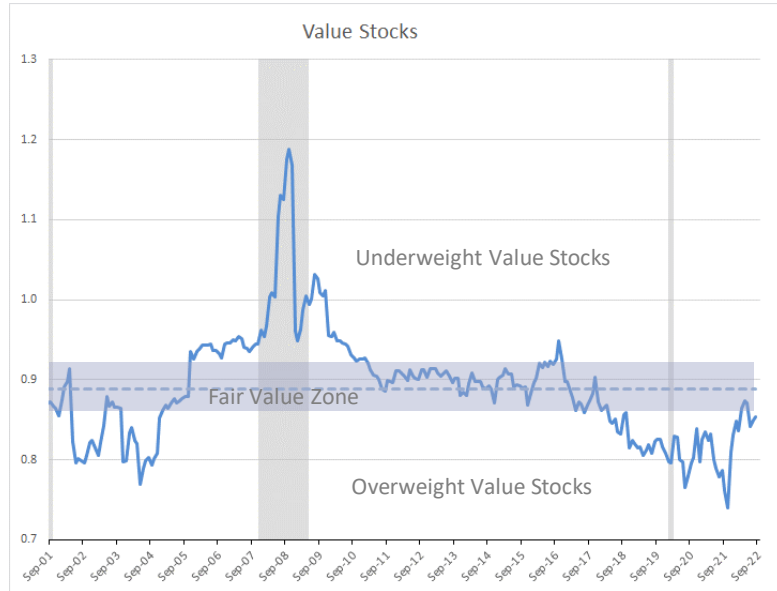
* BEst P/E Ratios are used.

Source: Standard & Poor's, Bloomberg, NBER, CLA Wealth Advisors



Equity Markets

Relative value — value and growth



Grey areas denote recessions.

Source: Bloomberg, S&P, CLA Wealth Advisors



Financial Markets – Equity Takeaways



Half Full

It is difficult to “time the market” because equity prices change based upon future expectations, so staying invested is the best course.

Market selloffs provide an opportunity to harvest losses.



Half Empty

Should a recession ensue, current earnings projections may prove to be too optimistic.

Equity price/earning ratios are near their long-term average but when adjusted for higher interest rates, they may have farther to fall before stabilizing.



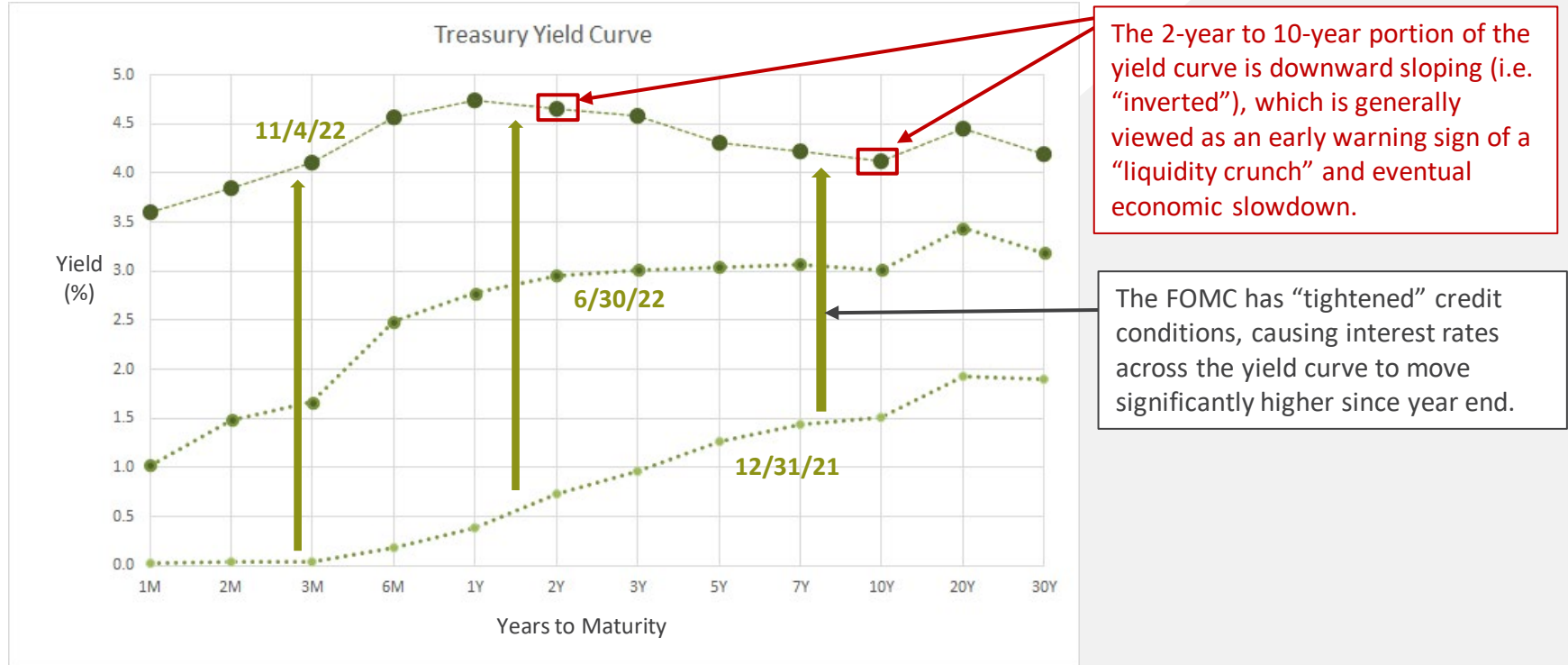
Financial Markets — Fixed Income

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Interest Rates – Yield Curve Changes



Source: Bloomberg, CLA Wealth Advisors



Financial Markets



Interest rates — credit markets do not show significant stress



Grey areas denote recessions.

Source: Bloomberg, CLA Wealth Advisors



Financial Markets — Fixed Income Takeaways



Half Full

Higher interest rates beginning of 2022 enable corporations and individuals to earn attractive yields for generating income on excess cash.

Market pricing of future rate hikes aligns with Fed messaging.



Half Empty

Real interest rates remain negative.

The Federal Reserve is going to raise rates until inflation returns to its 2% target, which means they may “overshoot.”

Credit spreads have widened but remain near their long-term averages.



Financial Markets — Private Credit, Real Estate and Equity

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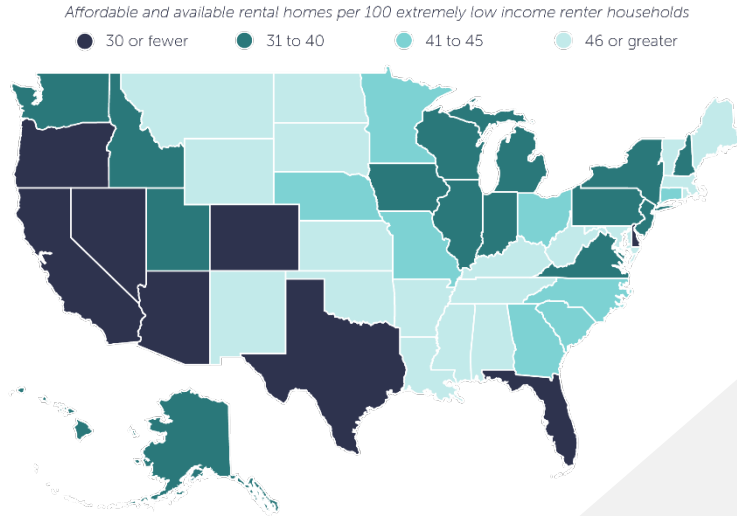
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Private Real Estate



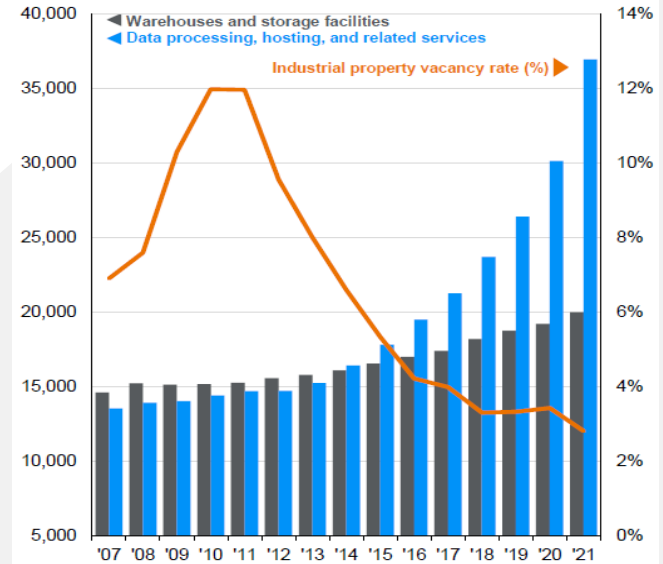
Multi-family residential and industrial sectors look attractive

No state currently has an adequate supply of affordable housing.



Industrial establishments and vacancy rate

Thousands of square feet, percent



Source: NCREIF, Case-Shiller, J.P. Morgan Asset Management

Source: BLS, J.P. Morgan Asset Management



Financial Markets – Private Market Takeaways



Half Full

The large and fragmented real estate market leads to a “perpetual” opportunity to acquire and improve properties.

The multifamily market is experiencing record high rents across primary and secondary cities.

Tax benefits of real estate are increasingly valued by investors.

Bipartisan support exists for new Opportunity Zone legislation.

Real interest rates are still historically low, making real estate more affordable.



Half Empty

The Federal Reserve is currently in a “tightening” phase.

Building costs have moved higher along with inflation.

Exhaustion of rental assistance and mortgage forbearance programs.

Skilled labor shortage.

Continued proposals to repeal/adjust 1031 exchange tax benefits.

Nominal interest rates increased sharply in 2023.





Portfolio Outlook

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Portfolio Construction Themes for 2023



Theme 1

Macro — Inflation appears to have peaked and should return to more reasonable levels during the latter half of 2023 and early-2024.

Theme 2

Equity — Prices have returned to more reasonable price/earnings multiples — especially in small cap and international stocks. *Important:* Equity prices are based upon market expectations, approximately six months into the future. Therefore, equity prices tend to move well before any recovery in the macroeconomic data becomes evident.

Theme 3

Fixed income — After suffering its worst performance in decades, fixed income has become reasonably attractive, especially in high quality, intermediate maturities.

Theme 4

Alternatives — both public and private markets offer an illiquidity premium that diversifies client portfolios by increasing expected return and/or lowering expected risk (volatility).



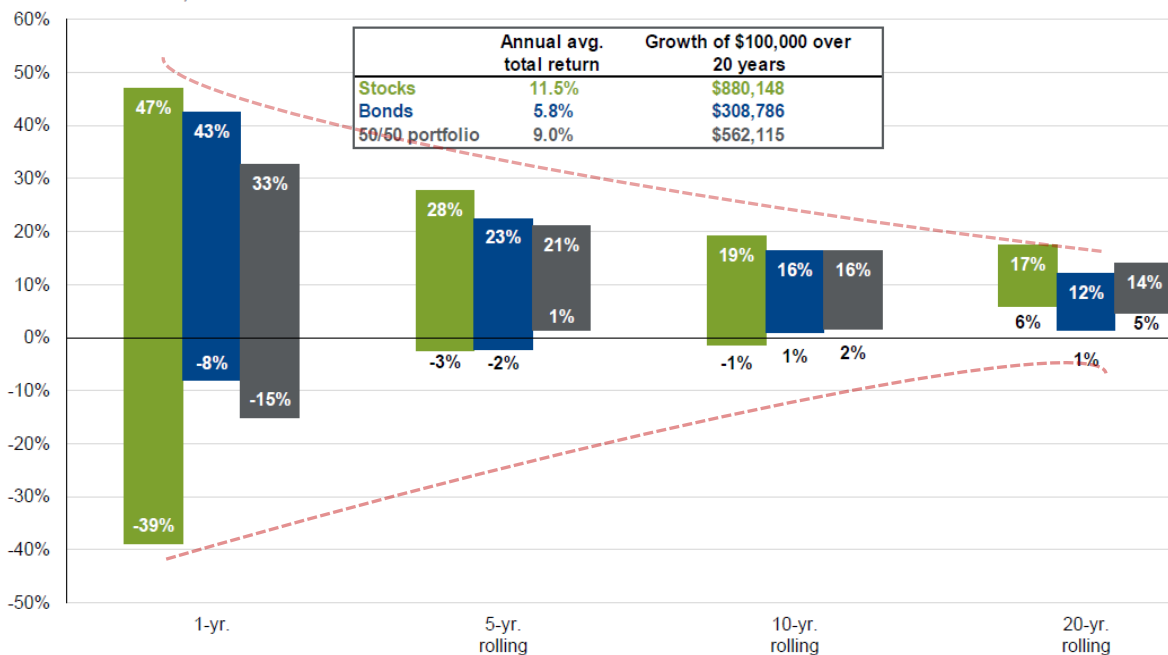
Stay the Course as a Long-Term Investor



Align your risk/return targets with your financial plan

Range of stock, bond and blended total returns

Annual total returns, 1950 - 2021



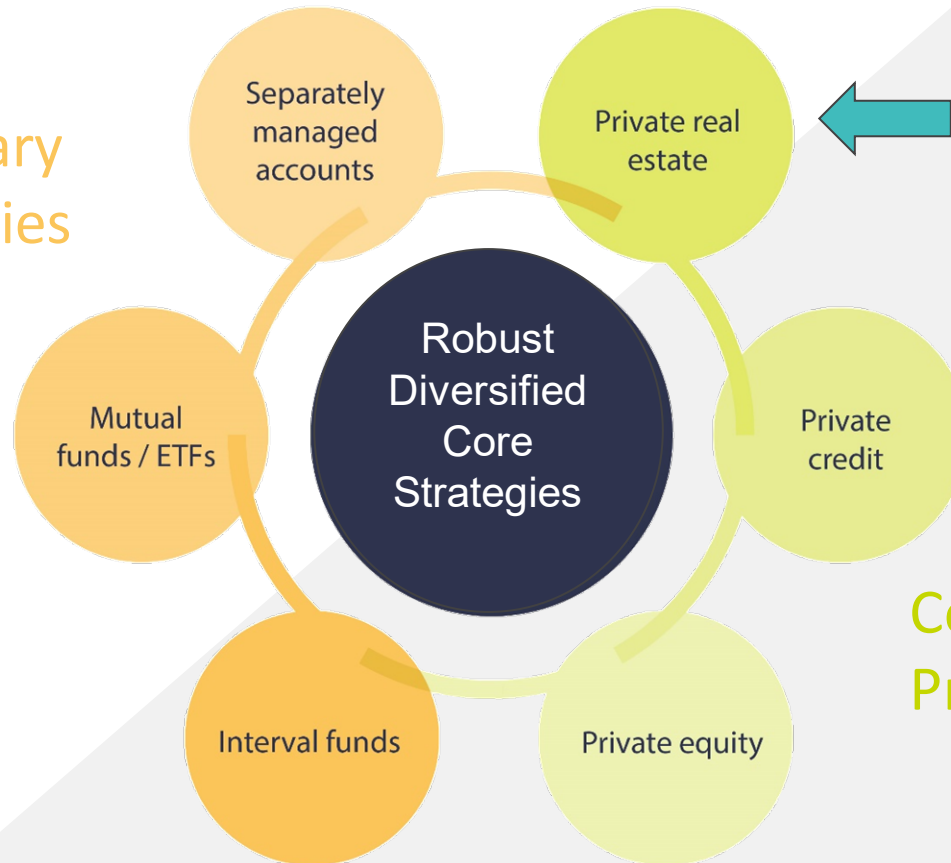
Source: Bloomberg, FactSet, Federal Reserve, Robert Shiller, Strategas/Ibbotson, J.P. Morgan Asset Management.



How We Construct Portfolios at CLA



Complementary
Public Strategies



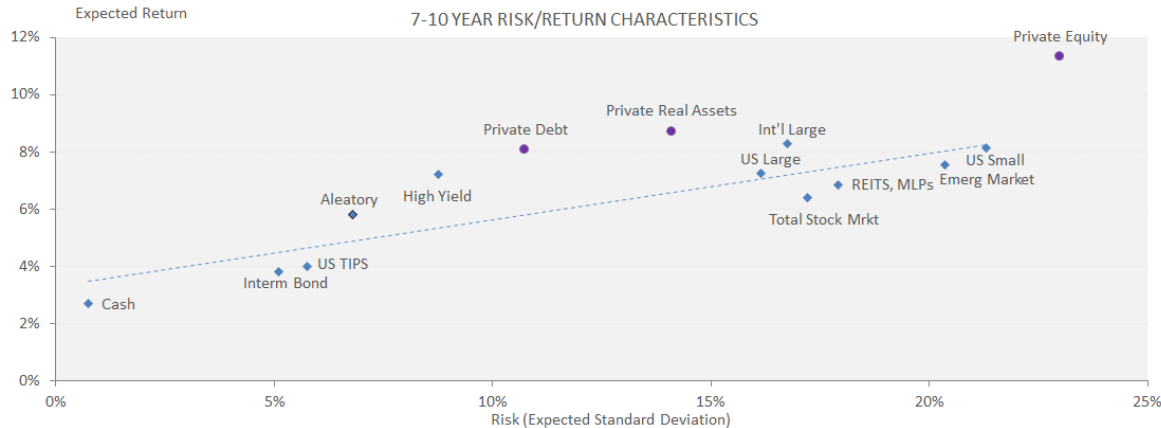
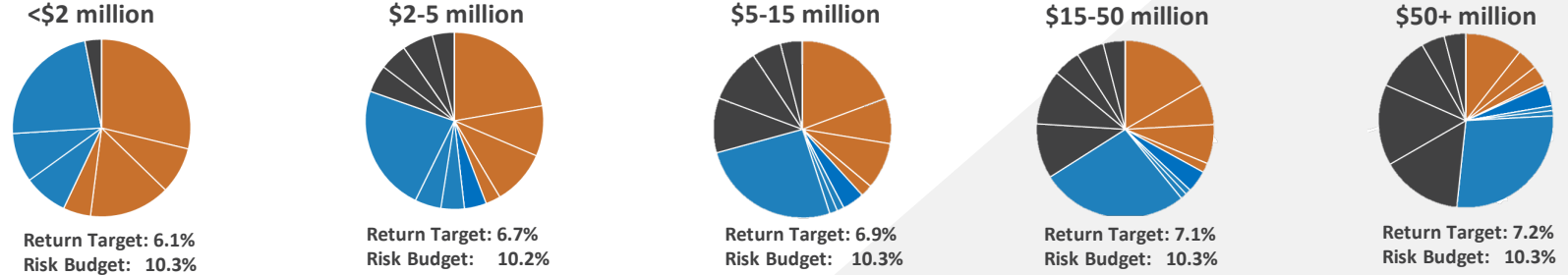
Real Estate is an
important part of a
**CLA Total Return
Portfolio**

Complementary
Private Strategies

Diversification of Portfolios is Key



Sample Balanced "60/40" Accounts



Key

- Equities
- Fixed Income
- Alternative





Policy Update

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Policy Outlook – Legislative and Regulatory Takeaways



Half Full

Congress plans to address priority issues in “lame duck”:

- Federal government spending (set to expire Dec. 16)
- The debt ceiling
- The Defense Authorization Act
- Key tax provisions

SECURE Act 2.0 and other bipartisan packages could get attached to legislation.

Congress and the Biden administration will work together on bipartisan and “must pass” legislation next year.



Half Empty

Priority issues could get delayed until next Congress.

Risk of potential default would affect the nation’s creditworthiness, increases cost to borrow.

A shutdown would disrupt government, cause delays in services and resources.

Businesses could pay significantly higher taxes if certain expired and expiring provisions are not extended.

A divided government may result in gridlock next year.



Industry Outlook

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Industry Insights



- **Macroeconomic focus areas:** Interest rates, business profitability, labor (finding talent and wage pressures)
- **Specific highlights:**
 - Fears about inflation, supply chain concerns and high commodity prices area receding with the focus now on interest rates and its impact on rising cost of capital, leverage and business profitability.
 - Regulated industries: Government spending levels and labor markets are critical.
 - Private industries: Interest rates, business profitability and labor are focus areas.
 - Opportunities: Focus on technology (digital) to drive efficiency to maintain margins and utilize outsourcing to address any labor needs.



2023 Outlook – Industry Takeaways



Half Full

Organizations are focusing on not only revenue & profitability but building fortress balance sheets – creating strength and flexibility

Business owners and leaders are focusing on what they know now, what they can manage and what they control

Tight labor markets are driving innovation and creating a focus on “ideal” work

Pricing and customer contracts are front of mind driving more regular review of terms

Business owners and leaders are focusing on planning for succession



Half Empty

Tight labor markets and rising cost of capital may challenge unprepared business owners.

Concerns around the “right” time to sell is front of mind for business owners looking to transition their business

Inflation is driving increase in cost structure and putting pressure on margins

Supply chain challenges continue to disrupt – driving the need to have excess working capital to meet customer demands



Challenges = Opportunities

- Workforce
- Inflation – Increasing Cost Structure
- Profitability
- Supply Chain
- Succession
- Outsourced Solutions
- Digital Strategy
- Owner Transition Planning
- Business Planning / Industry Consulting



Stay the Course



Financial Market Equity

- Overweight value stocks / underweight growth stocks.
- Small stocks are priced more attractively than large cap stocks.
- International equities are attractively priced relative to domestic equities.
- Low-cost passive ETF strategies can provide efficient access to the market.

Financial Market – Fixed Income

- Investors seeking current income should consider short maturities (1-3 years).
- Total return investors should consider intermediate maturities (5-7 years).
- High quality credit (A-rated or higher) should be favored until credit spreads widen further.

Financial Market – Private Market

- Private credit is a core holding due to its high current income potential, low interest rate risk, seniority in the capital stack and covenant protections.
- Multifamily housing has strong demographic tailwinds due to a lack of affordable housing.
- Industrial properties have strong underlying fundamentals.
- Consider high quality office space with an emphasis on innovation and amenities.
- Manager selection in private equity is of critical importance.



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Contact us to discuss how we can serve you and help you achieve your goals



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