Ropes Wealth Says Better Safe Than Sorry

This year's first-quarter earnings season started strong, with several big U.S. banks posting better-than-expected results, but the enthusiasm is waning as we proceed through the season. The latest blow was Tesla reporting a 24% drop in first-quarter profit, reflecting a string of price cuts enacted this year, sending the electric car maker's stock tumbling more than 10% Thursday. Tesla said its automotive gross margin for the quarter dropped under 16%, excluding regulatory credits, from around 24% in the previous quarter. Its gross profit margin per vehicle sold fell to approximately $6,800, from around $15,700 a year earlier.

And in another sign of the pressure on the economy, the Conference Board said Thursday its Leading Economic Index (LEI), a forward-looking measure of economic conditions, fell -1.2% in March from the month before, leaving it at its lowest level since November 2020.

In other data, housing starts fell -0.8% in March, pulling the annual pace down from 1.432M to 1.420M, a two-month low. Year-over-year, housing starts fell -17.2% in March, the eleventh consecutive month of decline. Building permits, meanwhile, decreased -8.8% in March, pulling the annual pace down from 1.550M to 1.413M, also a two-month low. Year-over-year, building permits declined -24.8% in March following a -16.5% decrease in February, and marking the eighth consecutive month of decline. Rounding out the bad news, year-over-year existing home sales dropped -22% in March, the twentieth consecutive month of decline. Despite a fall in sales, the months' supply of existing homes remained at 2.6 months for the second month, averaging 2.7 months over the past three months showing inventory remains tight. To that point, after hitting its lowest level in 10 years, the National Association of Home Builders (NAHB) Market Index has steadily risen in early 2023 as limited inventory is helping boost demand.

The Fed remains mixed on how to handle the slowing data coupled with inflation still above 2%. St. Louis Fed President James Bullard notably said this week that despite recent market turmoil, he has lifted his expectations for policy from two to three more rate hikes. "*The labor market just seems very, very strong,*" Bullard explained. "*And the conventional wisdom is that if you have a strong labor market that feeds into strong consumption ... And that's a big chunk of the economy...it doesn't seem like the moment to be predicting that you have a recession in the second half of 2023,*" he said.

In contrast, Chicago Fed President Austan Goolsbee commented on the recent bank failures, noting, "*My message is be prudent, be patient…if banks are pulling back it behooves us to pay attention to the data and ask how much of our normal monetary policy job is getting done for us by the credit conditions.*" As the saying goes, "*don't fight the Fed,*" but does anyone know which Fed member we are supposed to be listening to?

Something else we need to pay attention to is the debate around the debt ceiling. This week, Speaker Kevin McCarthy has introduced the "*Limit, Save, Grow Act*" as a solution. The bill would raise the $31.4T debt ceiling by $1.5T, which would reportedly be sufficient to avert a default until Q1 2024. At the same time, the bill aims to limit federal spending and reduce budget deficits by $4.5T over the next decade by bringing discretionary spending back to last year's levels and capping future growth in spending at 1% a year for the next 10. "*If Washington wants to spend more it will have to come together and find savings elsewhere just like every single household in America,*" McCarthy said on the House floor Wednesday afternoon.

While most in Washington agree the debt limit will eventually be increased, the question remains whether or not it will be a clean increase or if it will be tied to other provisions or conditions. In a surprise to no one, Senator Manchin broke ranks with the Democrats to say Biden's insistence for a no-strings debt ceiling increase reflected a "deficiency of leadership." Either way, the longer the saga plays out, the more it weighs on the uncertainty in the market, and on consumers' and international perception.

We continue to urge you to brace for volatility but stand firm on your long-term plan. Ensuring cash is set aside for your short-term needs (but in amounts below the FDIC limits and/or in short-term government securities) makes sense. As suggested last week, consider taking required minimum distributions now from retirement accounts. It could also be a good time to make gifts of stock to your charities with the market still more or less cooperating. There has been a nice bounce in prices in 2023 after last year's downturn that we believe sets markets at the right levels for the earnings slowdown and mild recession ahead. But shocks to the system, like a debt ceiling divide, may take progress off course temporarily. Better to be safe than sorry with your short term needs and plans and we will continue to steward the long-term strategy through it all.

Thank you as always for your interest in our investment commentary. If you would like to speak personally with a member of our team at any time, please click **here**.

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