Economic & Market Outlook

Executive Summary

~ Markets believe the fight against inflation is over and have shifted their focus to rate cuts.

~ During the fourth quarter, all asset classes rallied as the "soft landing" narrative gained credibility.

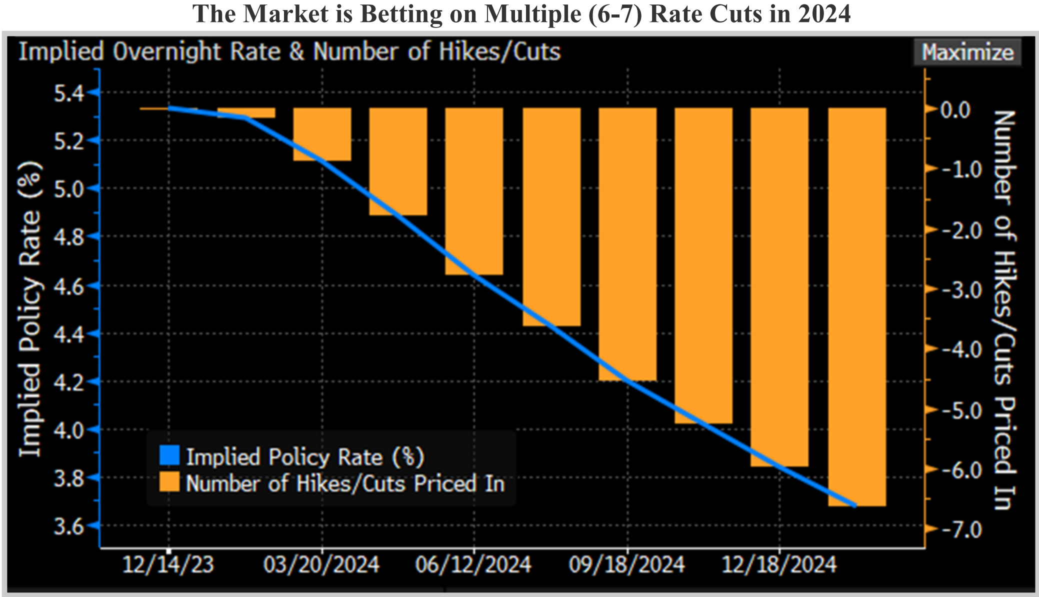
~ If a soft landing fails to materialize, it could pose a risk to stocks, which trade at 23x trailing earnings.

~ A case can be made for alternate economic realities, like "no landing" or even a "hard landing." We believe it is still too early to declare victory.

Mission Accomplished!

When the Federal Reserve speaks, market participants listen. The addition or elimination of a single adjective in the Fed's written or oral communication is enough to move markets. So, on 12/13/23, when Chairman Jerome Powell said interest rate cuts might be coming "into view," the financial markets heard "mission accomplished." The fight against inflation was over, and it had yet to come at the cost of economic growth. A soft landing was in the works. To be clear, Jerome Powell didn't explicitly declare victory, far from it, but that was the market's takeaway.

The Market is Betting on Multiple (6-7) Rate Cuts in 2024



Source: Bloomberg

By the following day (12/14/23), over six interest rate cuts had been priced into the market, implying the federal funds rate would fall from 5.3% to 3.7% over the course of 2024. The Federal Reserve's internal projections (dot plots) were less aggressive but told the same story. The median estimate, among Federal Reserve governors, was 4.6% by year-end 2024. Furthermore, not a single Fed policymaker (19 in total) was calling for rate hikes.

A Soft Landing: "Central bank's reign in inflation without inducing a recession."

Financial markets also appear to be pricing in higher odds of a soft landing. During the fourth quarter, financial assets (stocks and bonds) performed incredibly well. The bulk of the move occurred during the months of November and December. 10-year interest rates fell from 4.9% to 3.9%, leading to a massive rally in bonds of all types. Investment-grade bonds returned 8.5% in these two months alone. The S&P 500 climbed 14.1%, but even more noteworthy was the 22.4% advance in smaller capitalization stocks. This development stood out because small-cap stocks had sat out the entire year's advance. In fact, these smaller companies were down -4.5% on the year as of 10/31/23, significantly lagging the market.

	YTD through 10/31/2023	Last Two Months	Full Year
Magnificent 7*	78.4%	16.0%	107.0%
US Large Caps	10.3%	14.7%	26.5%
US Mid Caps	-2.7%	20.7%	17.4%
US Small Caps	-4.5%	22.4%	16.9%

** Apple, Amazon, Alphabet, Facebook, Microsoft, Nvidia, & Tesla*

The poor performance of small caps was commonly attributed to their balance sheet health and cyclicality. On the balance sheet front, small caps are more sensitive to changes in interest rates. 38% of floating rate debt outstanding sits on the balance sheets of smaller public companies compared to only 6% at larger public companies with the remainder at private equity-backed companies. For small public companies, almost half of their debt matures before 2030, whereas larger public companies hold debt that is further termed out. Larger corporations also sat on bigger cash hoards. On the cyclicality front, information technology and healthcare dominate large capitalization indices, whereas financials and industrials dominate the small capitalization indices. In other words, until late October, the market was unwilling to price in the prospect of a "soft landing," which held back the equity returns of smaller companies believed to have weaker balance sheets and greater exposure to the economic cycle. During the months of November and December, the soft landing narrative gained credibility, leading to a strong reversal in small-cap performance.

We normally wouldn't read too much into the behavior of one sub-asset class, but when we look across asset classes, everything seems to be sending a similar message. Here is a broader recap of what transpired in the months of November and December:

- Treasury rates (10-year) fell from 4.9% to 3.9%, a sign that either inflation is under control and/or the real US economy is about to slow.

- Inflation break-even rates (10-year) fell 0.3% from 2.4% to 2.1%, an inch above the Fed's 2.0% inflation target, again a sign that the market thinks inflation is under control and/or the economy is about to slow. It is also worth noting that 1-year break-even rates closed the year at the Fed's targeted inflation rate of 2.0%.

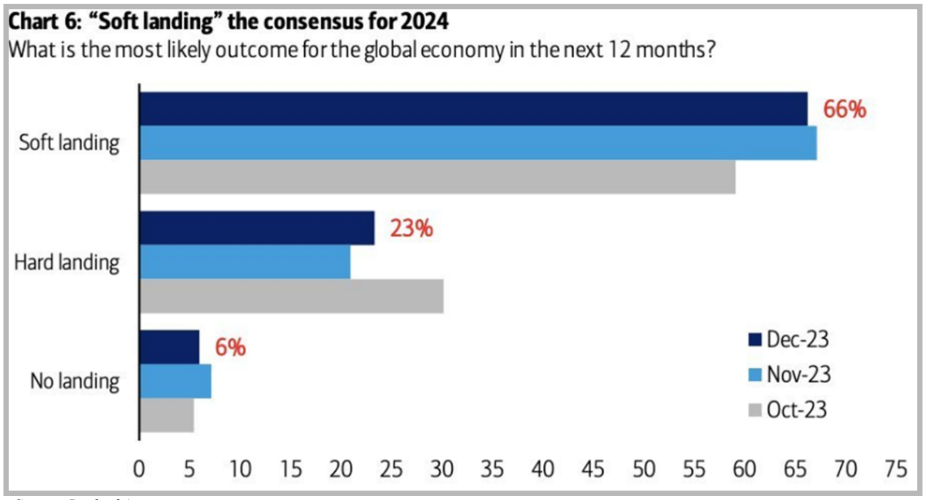
- US equity (Russell 3000) valuations (forward PE ratio) climbed from 18.5x to 21.5x. In other words, equity participants were willing to pay 16.2% more for a dollar of prospective earnings, signaling equity investors were more excited about prospective earnings on 12/31/23 than they were on 10/31/23, implying they viewed a recession as unlikely.

- High-yield credit spreads contracted from 4.4% to 3.2%. Credit spreads represent the incremental yield investors demand above the risk-free rate (Treasuries) to compensate them for the possibility a borrower might default on its obligations. The narrowing of credit spreads indicates credit investors are less worried about a borrower's ability to repay its obligation, something you are unlikely to see if markets believe a recession is on the horizon.

- The cost of at-the-money, one-year put protection fell from 6.0% to 4.9%. In other words, the price investors are willing to pay for insurance protecting them from a decline in the S&P 500 costs 1.1% less. Yet another sign investors felt sanguine about the inherent risk in buying equities.

The performance of almost every financial market/instrument seems to indicate the market is assigning a greater probability to the Fed engineering a soft landing. The market believes the fight against inflation has been won (or is almost over) and that the Fed's pivot to less restrictive (or even loosening) monetary policy will keep our economy humming along. Why else would Fed Futures fall, Treasury rates fall, inflation break-even rates fall, equity valuations rise, credit spreads tighten, and put protection cheapen?

Professional Money Managers See "Soft Landing" as the Likely Outcome



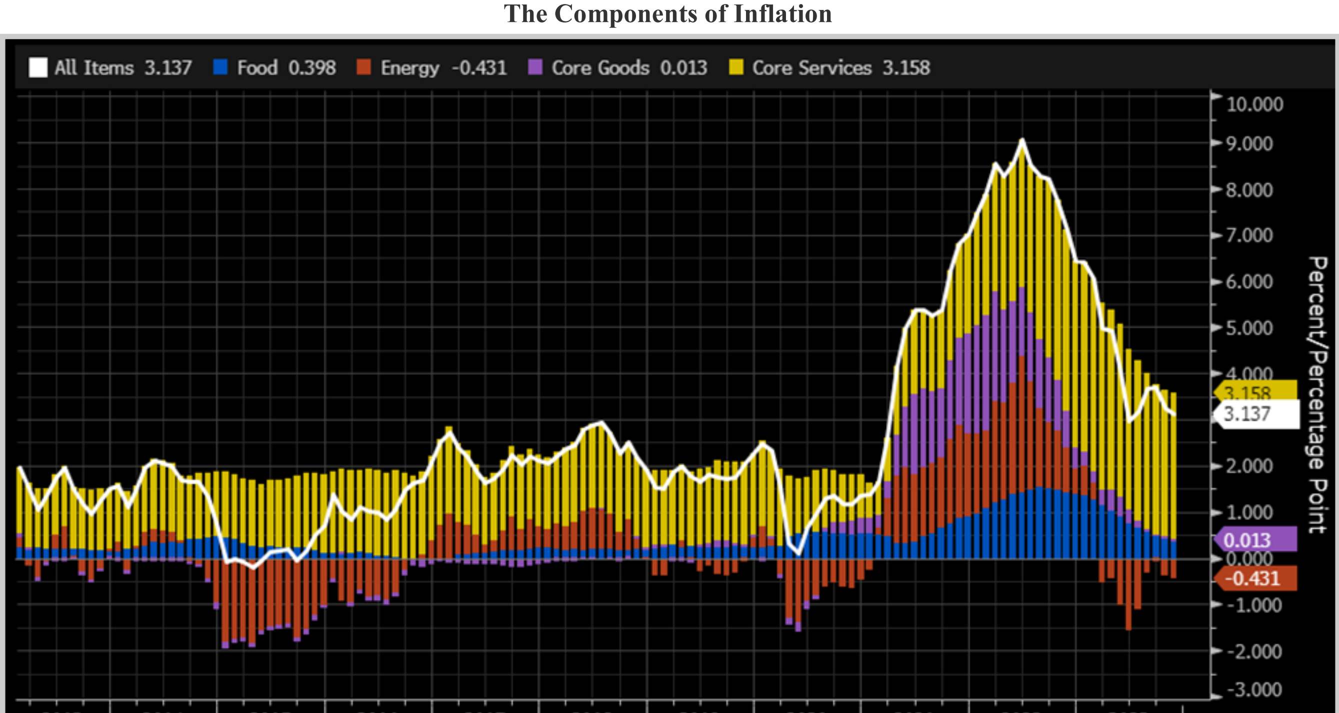
Source: Bank of America

At Annandale, we are hesitant to jump to any conclusions. A soft landing could be in the works, but we can also make credible cases for alternate paths, like no landing or even a hard landing. Every potential outcome is on the table.

No Landing: "In a no landing scenario, US economic growth would continue to be resilient… Core inflation would remain sticky and settle one or two percentage points above central bank targets."

A no landing scenario would suggest that the Fed's battle against inflation is ongoing. Headline CPI currently stands at 3.1%, significantly lower than the 9.0% peak recorded post-COVID but still surpassing the Fed's 2.0% target. To date, declining inflation has been driven almost entirely by "tangible things" as opposed to services. COVID immediately disrupted global supply chains, reducing the supply of "tangible things" we consume relative to our demand for those "tangible things." Food, energy, and goods prices skyrocketed. As supply chain pressures eased, these inflationary pressures reversed. Food, energy, and goods inflation are virtually nonexistent today, but services inflation remains.

The Components of Inflation

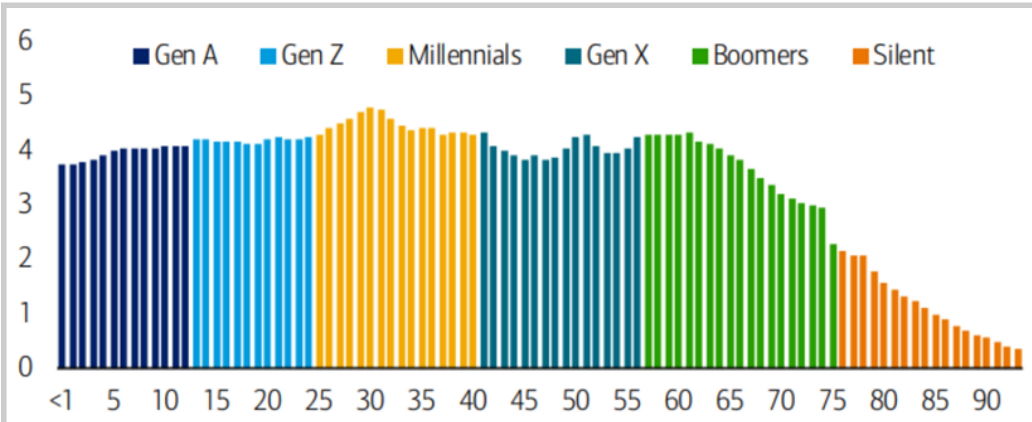


Source: Bloomberg

If services inflation doesn't subside, achieving the Fed's goals will prove challenging. Services account for 58.7% of the CPI basket. If food, goods, and energy inflation are nonexistent (0.0%), services inflation must fall to 3.2% for the Fed to hit its 2.0% target. Today, services inflation sits at 5.5%, only 1.7% off its peak, and it is falling at a decelerating rate.

The biggest component of services inflation is shelter (housing costs), which makes up 32.3% of the CPI basket. Consider the fact that 30-year mortgage rates surged from just under 3.0% to around 8.0%, yet national home prices did not decline. In fact, housing prices climbed 33.5% during that period, indicating there is significant demand to own a home. Demographically this makes sense, as millennials (ages 25 to 40 now), make up the largest population cohort in the US, and that cohort skews young (around 30 years of age). If rates fall, additional housing stock (supply) would likely hit the market, but will it be enough to satiate the needs of millennials?

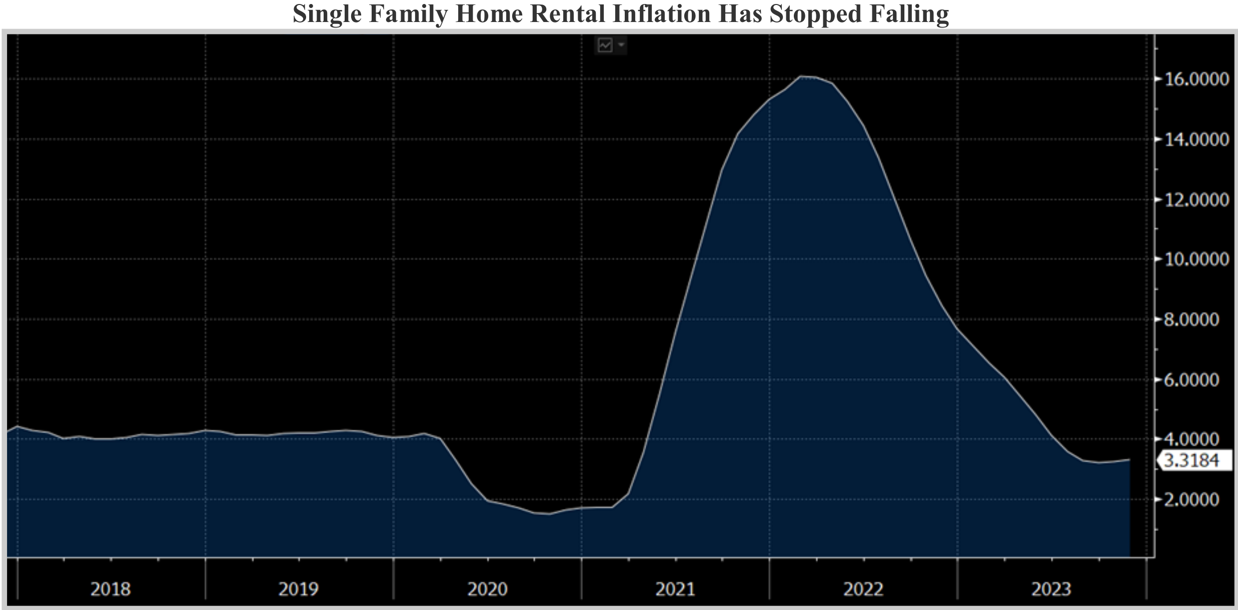
Millennials Account for the Largest Population Cohort in the US



Source: Bank of America

Calculating the cost of shelter is difficult given two-thirds of American households own homes rather than rent. Our government tries to estimate "owners' equivalent rent," the hypothetical rent a homeowner would pay if they were to rent an equivalent home. The goal of this calculation is to find out how much individuals would pay for consumptive as opposed to investment purposes. I.e. individuals are often willing to pay more for ownership than rent, because they view mortgage principal payments as a form of financial savings. One way to estimate equivalent rents is to track the price of single-family rentals, which Zillow does. Evident in the chart below, rental inflation for homes has cooled, but it seems to have stabilized and is now trending upward. Does this foretell a pickup in our government's calculation of owners' equivalent rent? Is a soft landing predicated on falling home prices?

Single Family Home Rental Inflation Has Stopped Falling



Source: Bloomberg

What about the other 40.0% of services, the components not tied to shelter? If housing inflation doesn't abate, the Fed will need services inflation (ex-housing) to fall to 1.5%. Today services inflation (ex-housing) sits at 4.1%. It did briefly fall from a high of 6.7% to 3.9%, but over the last 5 months it has slowly edged higher. The cost of childcare is up 4.6% year-over-year. Legal services +12.4%. Car repair +12.7%. Gardening and lawn care +13%. And thanks to Taylor Swift, the cost of admission to events is up 8.1%. Some items, like gardening and lawn care or Taylor Swift tickets are discretionary in nature. Their higher prices are reflective of the strength of US consumers, which begs the question, how do we ever get services inflation down if nominal wage growth is outpacing inflation?

Wages (White Line) Are Growing Faster than Inflation (Blue Line)

Source: Bloomberg

The US economy is already operating at full employment. The U-3 unemployment rate stands at 3.8%, marking the longest period it has remained below 4.0% since the Vietnam War. Recently, initial and continuing jobless claims have been falling, which indicates fewer workers are being laid off and those that have been laid off are finding employment elsewhere. Simply put, if employers want to increase output by investing in more labor, finding labor will be difficult and likely, require higher wages.

To boot, US household balance sheets are in great shape despite a rapid increase in the rate of interest. We discussed this in our last letter, but the gist is US households used excess savings during COVID to pay down debt and refinanced major debt balances (like mortgages) when interest rates were near record lows. At present, debt payments constitute 9.9% of disposable personal income. If you exclude the COVID-related debt moratorium, we can't find a time they have been lower. Homes make up 29% of US household assets, and, as mentioned earlier, they currently stand at record prices. Financial assets (investments) account for 58% of US household assets and stock market indices have almost recouped their 2022 losses. Lastly, 8% of US household assets sit in deposits on bank balance sheets. This is an insignificant part of the average households' assets, but it is worth noting that deposit balance earning 3-5% equates to 67.5% of the US household's liabilities, which are likely accruing at a lower rate. To be fair, these statistics are skewed by the wealthy, but the argument remains the same. Given the strength of our labor market and the stimulating effect of higher home/stock prices, why should demand-driven inflation fall?

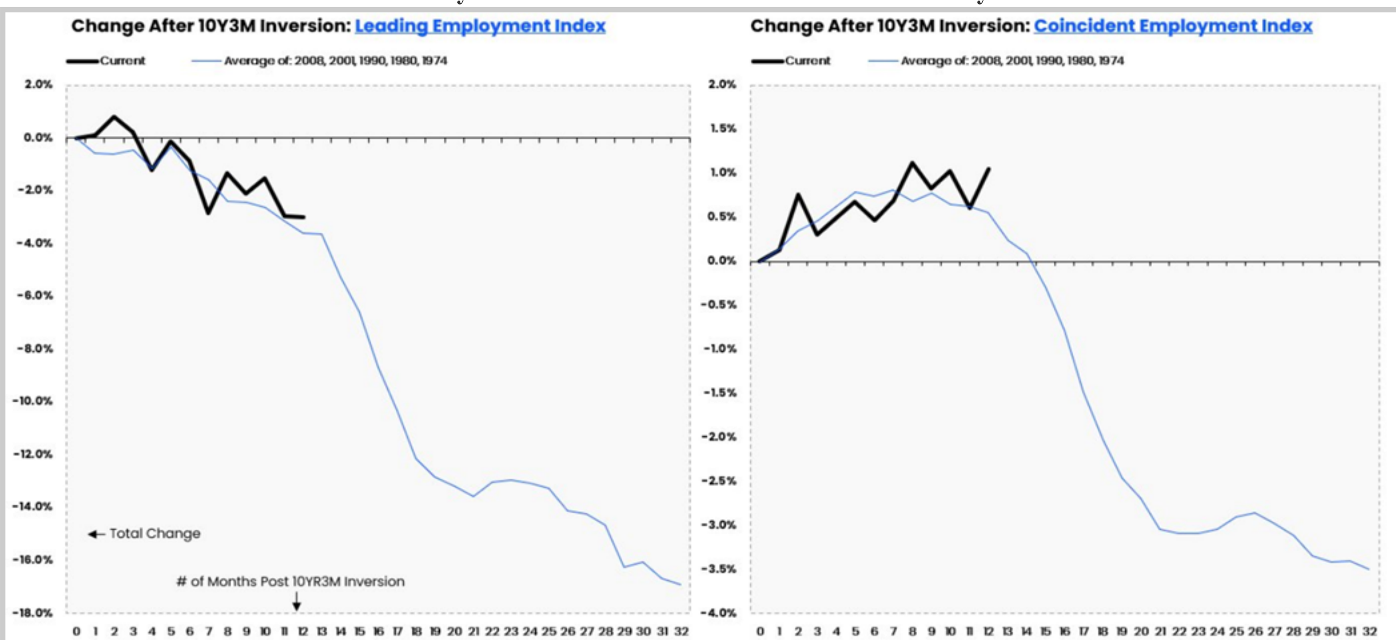
There are numerous other arguments for continued inflation. The current administration has drained the strategic petroleum reserve. The move towards deglobalization. Work from home has increased labor mobility and given power to workers over employers. We live in a period of heightened geopolitical tensions, where commodities and global trade patterns have been weaponized. Terrorists like the Houthis are disrupting supply lines by attacking container ships near the middle east.

Given this backdrop, can the Federal Reserve or market afford to declare victory on inflation and cut interest rates prematurely?

Hard Landing: "a pronounced contraction in economic activity."

Now, let's examine the opposite side of the ledger and present the case for a hard landing, signifying a recession. Every yield curve inversion in U.S. history has been followed by a recession. While some recessions unfold shortly after inversion, others take longer to develop. The current cycle appears to be evolving more slowly, attributed to the "long and variable lags" of monetary policy discussed in our last quarterly letter. Still, just because nothing bad has happened yet, doesn't mean it won't occur.

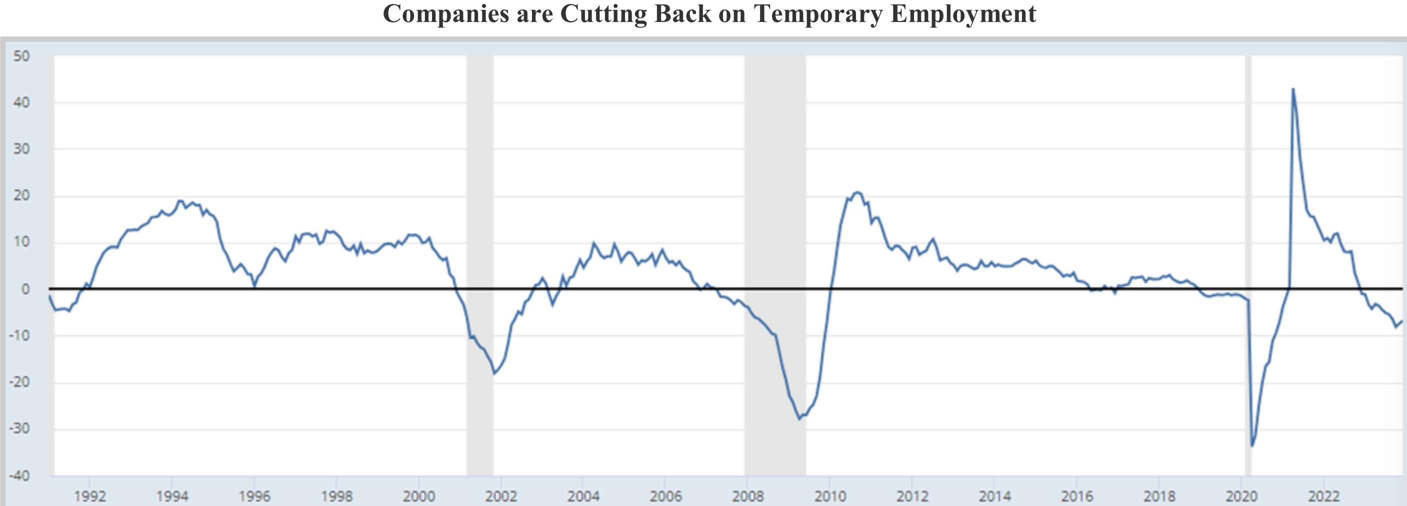
This Cycle Doesn't Look That Different from Past Cycles



Source: EPB Research

We are already witnessing some weaknesses in economic statistics, though these have not yet translated into headline economic measures such as the employment rate or GDP growth. The number of job openings relative to the workforce has steadily declined since early 2022. Similarly, the hiring rate, now at 3.5%, is at its lowest level since 2014 (excluding the pandemic). The quit rate is also decreasing, indicating a decline in confidence among individuals to leave their current jobs in search of better prospects elsewhere. Temporary help (part-time employment) has experienced a significant, year-over-year decline of -9.1%. This is noteworthy as employers tend to cut or forgo temporary roles before reducing full-time positions. If these early indicators continue to deteriorate, we may witness an increase in unemployment claims.

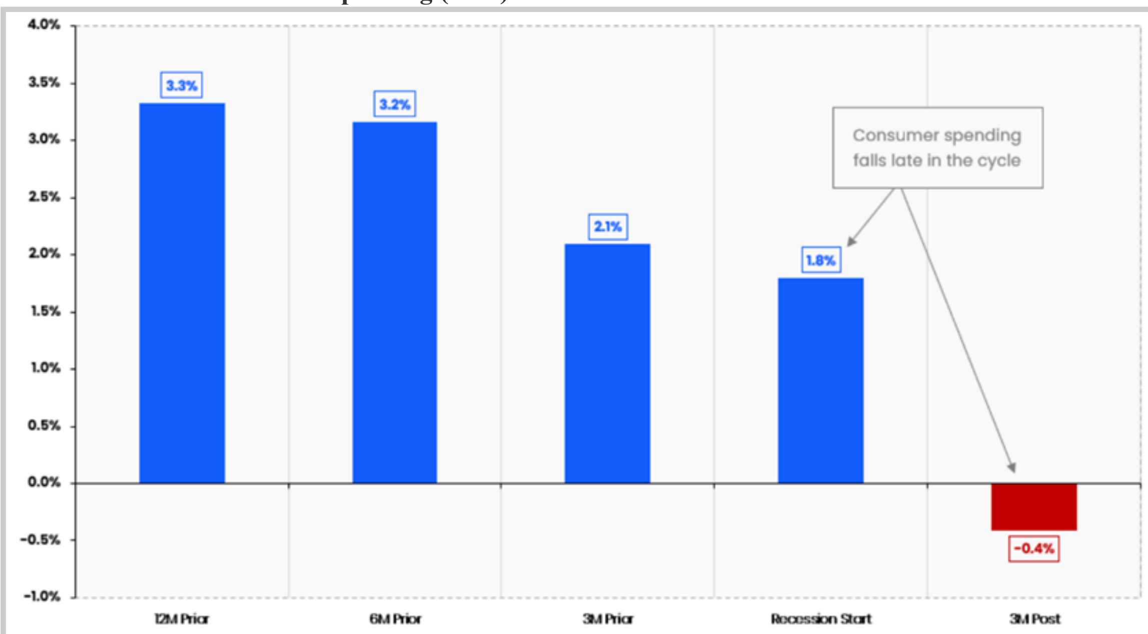
Companies are Cutting Back on Temporary Employment



Source: Federal Reserve of St. Louis

The U.S. consumer, currently in a strong position, may soon face challenges. During COVID, a combination of stimulus checks and an inability to spend pushed savings rates to historic levels, reaching a peak of $2.3 trillion in excess savings. However, these excess savings won't last indefinitely. Over the past two years, savings rates have declined, and accumulated excess savings have more than halved. Additionally, revolving consumer credit (credit card balances) is increasing as a percentage of disposable income at a time of record-high interest rates, further eroding the existing savings buffer. Those anticipating a slowdown in consumer spending as a sign of an impending recession may find themselves blindsided, as this tendency typically occurs after the economy has already turned.

Consumer Spending (Real) Before & After the Start of a Recession



Source: EPB Research

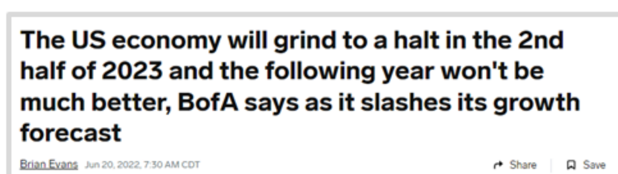
Lastly, the Conference Board, a non-profit economic research organization, publishes an index of leading economic indicators. This index, tracking 10 economic measures meant to identify turning points in the economy before they appear in coincident or lagging indicators, has declined for over 20 consecutive months. It now sits at -7.6%, a level historically associated with recession.

The Future is Always Uncertain

We cannot predict the path the economy will take. Credible cases can be made for a soft landing, no landing, and a hard landing. We are even open to considering paths we hadn't previously contemplated. Predicting economic turns is a challenging task, as the economy is a complex organism. Betting on a soft landing may even change the probability of it occurring. It's intriguing how market participants can express confidence in the prospects of a soft landing after being mistaken about 2023.


World Bank warns global economy could tip into recession in 2023

By David Lawder


The US economy will grind to a halt in the 2nd half of 2023 and the following year won't be much better, BofA says as it slashes its growth forecast

Brian Evans Jun 20, 2022, 7:30 AM CDT Share Save


The banking crisis will tilt US into recession, say Fed economists

By Bryan Mena and Nicole Goodkind, CNN
4 minute read · Updated 3:46 PM EDT, Wed April 12, 2023

Nonetheless, we are hopeful for a “soft landing,” or better.

The Implication for Stocks

The immediate trajectory of inflation and economic growth does matter for equity investors, particularly those with shorter time horizons. Equity valuations, the price an investor is willing to pay for a dollar of earnings, can change in a moment's notice. Valuations are erratic and dictated by the mood of the market.

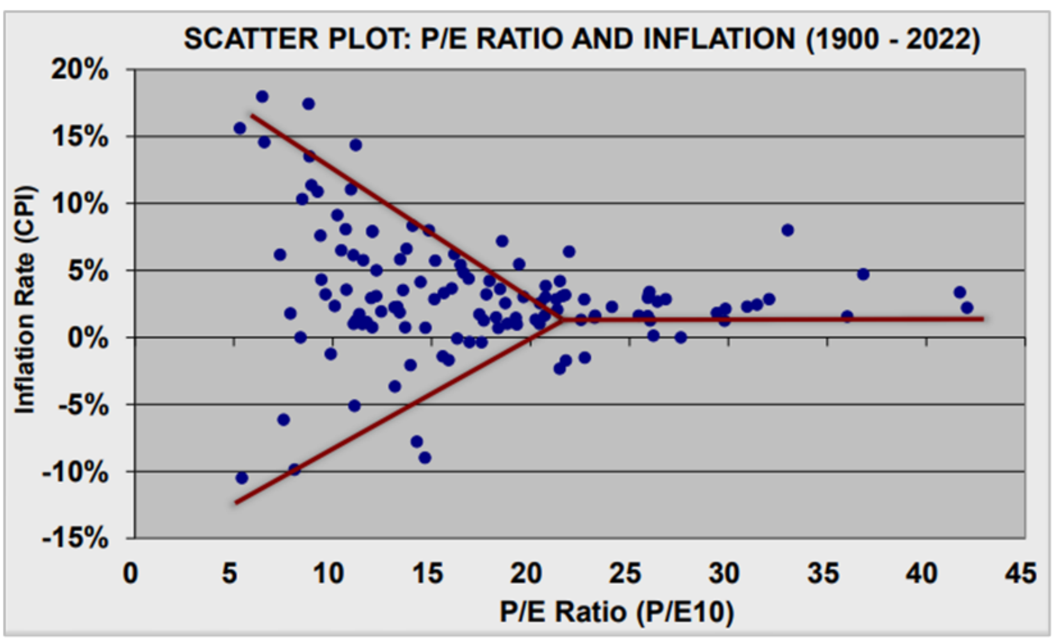
Currently, the market is betting on the best-case outcome: a soft landing. The combination of moderate inflation (around the Fed's 2.0% target) and moderate economic growth is what investors refer to as a Goldilocks economy. The market currently trades at a lofty 23x trailing 12-months earnings. While there is precedent for this earnings multiple going higher, as seen in the late 1990s, it rarely happens during periods of heightened inflation (no landing) or recession (hard landing). If either of the other two scenarios gains traction, the market may become less willing to capitalize earnings at such a high rate.

A hard landing (recession) is detrimental to equity valuations for obvious reasons. Earnings growth will experience a temporary setback, and individuals will likely be despondent about economic prospects and future corporate earnings growth. Moreover, in a recession, many investors are compelled to sell financial assets (like stocks) for basic living needs. It isn't easy to justify risky equity investments if you are unemployed and worried about future cash flow needs.

No landing (a resurgence in inflation) is also an unwelcome outcome depending upon how severe inflation gets, but the impact is slightly less obvious. As inflation rises, investors are forced to demand a greater return on their assets so that they can achieve a real return (return in excess of inflation). Inflation also introduces greater uncertainty into the economy that investors will demand additional compensation for. Simply put, higher interest rates and greater risk premiums equate to lower valuations. The confusing part is what happens to earnings growth. Most companies experience higher nominal sales, but depending upon the pricing power of that company it may or may not see an erosion in operating margin. On the net, inflation is bad for equity valuations.

The chart below effectively captures the range of possibilities. During periods of extreme inflation or deflation (recessions), valuation multiples are almost always low. Valuations at or higher than today's levels usually coincide with a Goldilocks economy.

Investors Hate Extremes in Inflation or Deflation (Recessions)

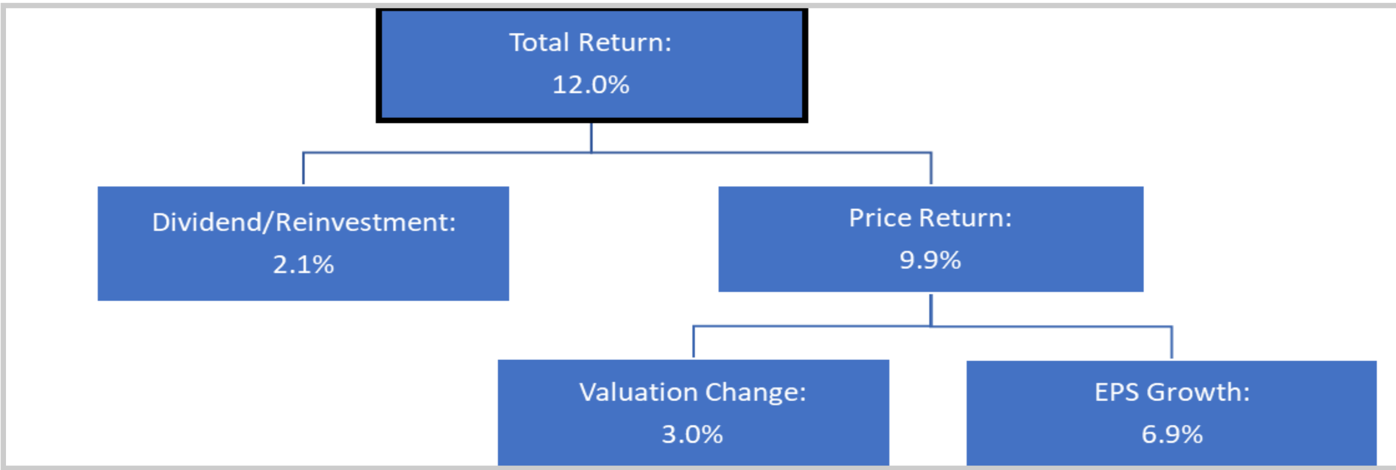


Source: Crestmont Research

Stocks for the Long-Run

Equity investors with longer time horizons should be less concerned with our economy's near-term trajectory. Over the last decade, the S&P 500 has compounded at an annual rate of 12.0%, about 2-3% above its long-term average. 3.0% of that return has come from changes in valuation, which is why the last decade has been so great. But changes in valuation are not a dependable source of returns. You can't expect the next investor will always be willing to buy your investments at a higher price, and as previously discussed, that variable can work against you if investors believe a hard landing or no landing is likely. The good news is that the other 9.0% of the S&P 500's return has come from relatively stable return sources. 2.1% from dividends and dividend reinvestment and 6.9% from earnings per share growth.

The Drivers of S&P 500 Returns: 2013-2023



Source: Annandale Capital

You can make an argument that those stable return sources will be lower going forward. Today, the S&P 500 carries a 1.5% dividend yield compared to 1.9% a decade ago, so all else equal, we should expect slightly lower returns from dividends and dividend reinvestment. Furthermore, earnings per share growth may decelerate from 6.9%. Since 1988, when the S&P began reporting detailed data, earnings per share have only grown 6.6% annually. Still, the combination of dividends, dividend reinvestment, and earnings per share growth could easily sum to 8.0% to 9.0% on a go forward basis.

The 1997 Analog

Will valuations turn into a headwind for equities? If a hard landing or no landing is around the corner than we would say it is likely, but again, we don't know which scenario will unfold. And it doesn't matter so long as equity investors have an appropriate time horizon, measured in decades opposed to years.

In late 1997, US stocks traded at valuations comparable to today's. The S&P 500 traded at 22.2x trailing earnings and sported a 1.5% dividend yield. Over the next decade, the US would witness the blow-up of Long-term Capital Management, the popping of the technology and telecom bubble (a 49% decline in stock prices), and a recession. Stock valuations would fall from 22.2x to 16.4x, a 3.0% per annum headwind. Still, US equities returned almost 6.0% per annum thanks to the stability of long-term earnings growth and the power of dividend reinvestment, a below-average outcome, but positive, nonetheless.

If you held for an additional decade, you would witness one of the greatest financial crises in history, leading to the steepest decline in GDP in history. During the great financial crisis, stock prices (not inclusive of dividends) fell by 57.0%. Still equities returned 7.2% per annum, another below-average outcome, but positive, nonetheless.

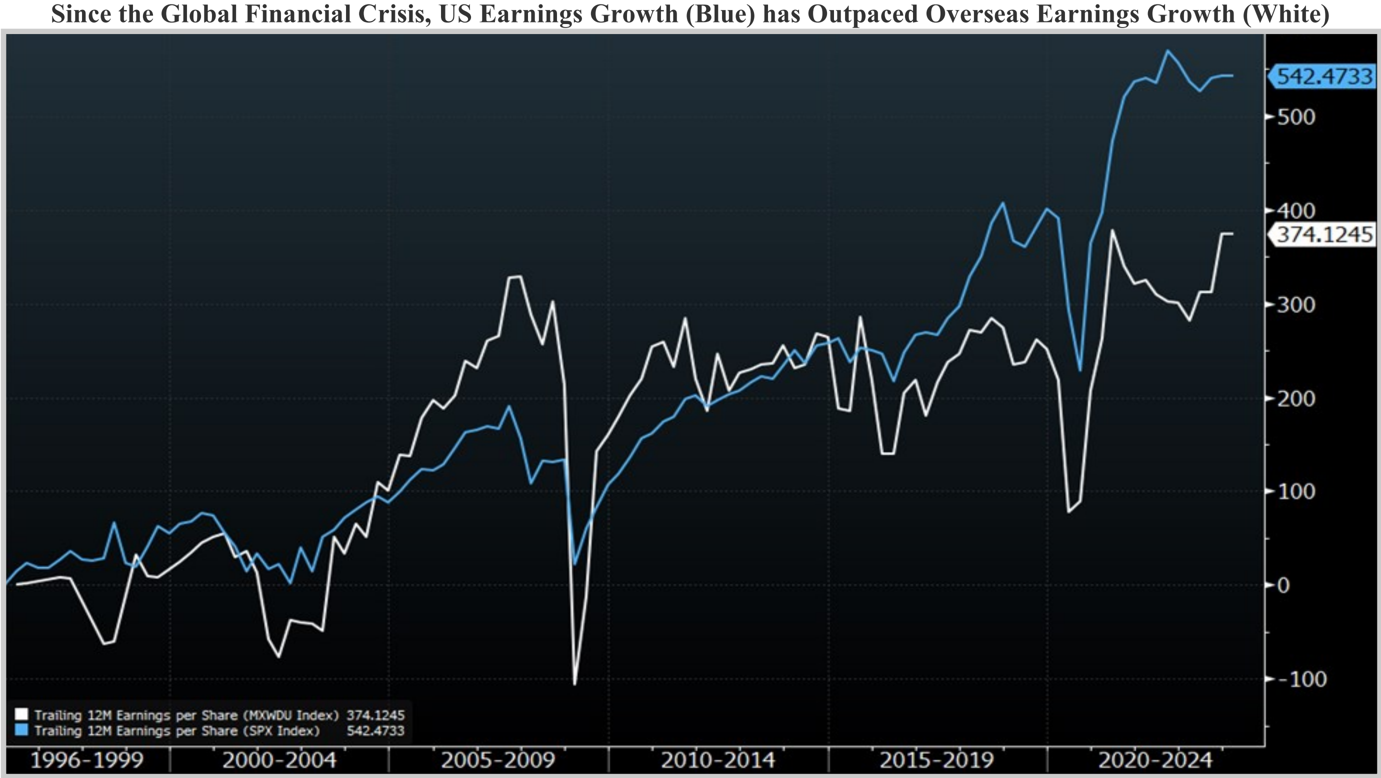
Hopefully, the point we are trying to stress is obvious. In the long-run, dividends and earnings per share growth is all that matters to the US equity investors. Even the unlucky investor, who only invests at peak valuation multiples, could have had a good outcome so long as they stuck with it.

Going Global

It isn't our goal to be the unlucky investor, even if the long-term outcome will turn out fine. We recognize that heightened US equity valuations pose a potential risk, and part of our job is to manage portfolios in an uncertain world. To that end, we always maintain some level of diversification across sub-asset classes.

Outside the US, equity valuations are considerably cheaper. The MSCI All Country World Index (ex US) trades at only 14.3x trailing earnings and 12.7x next year's estimates. On top of this, the index sports a +3.0% dividend yield. The knock against overseas equities would be their historical growth rates. Since the great financial crisis, corporate profit growth outside of the US has been subpar, which you can see in the cart below which shows the percentage growth for the S&P relative to the MSCI All Country (ex-United States) Index.

Since the Global Financial Crisis, US Earnings Growth (Blue) has Outpaced Overseas Earnings Growth (White)



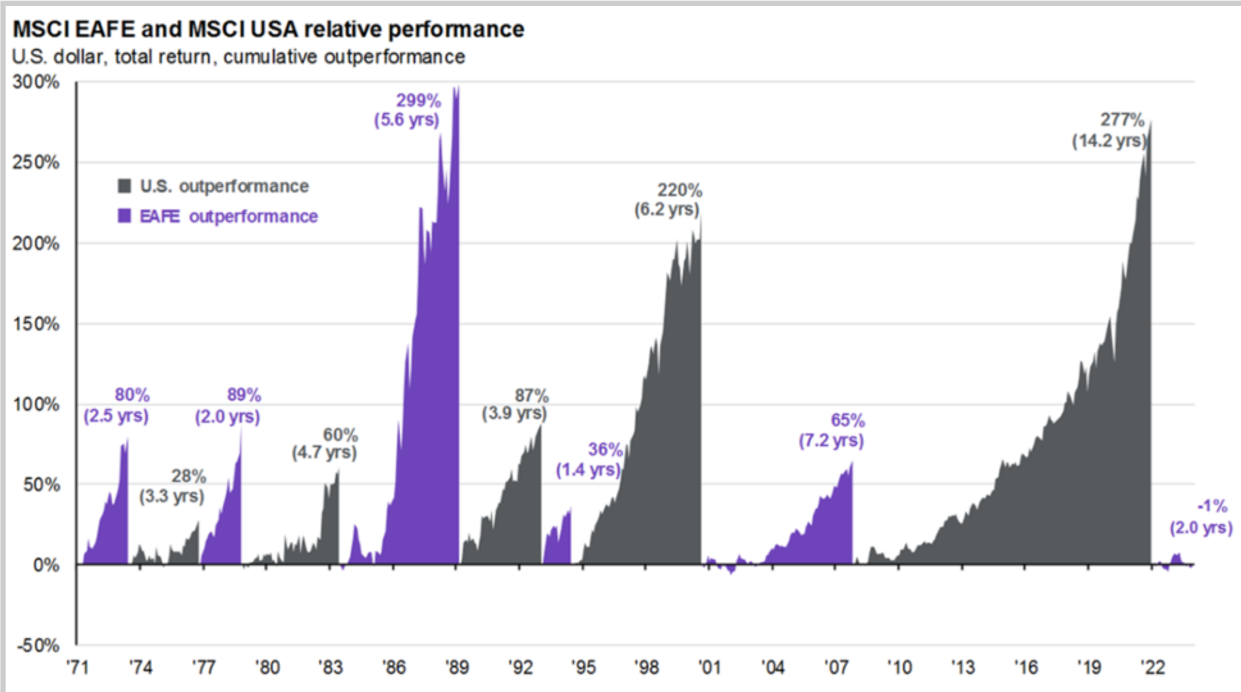
Source: Bloomberg

The good news is the slog in earnings growth outside of the United States may be coming to an end. Japan for instance makes up 13.5% of the ex-US index. Japan has long been home to some of the world's most wonderful businesses, but capital allocations among Japanese management teams has been abysmal. Because of past economic and market trauma, Japanese executives spent decades paying down debt and hoarding cash, as opposed to investing back into their business or returning cash to shareholders. In fact, Japanese companies in aggregate hold no debt. As you can imagine, those excess cash coffers sat idle on balance sheets earning next to nothing, given record low interest rates, which destroyed the profitability of Japanese firms, and in turn Japanese earnings growth.

Shinzo Abe, the former Prime Minister of Japan, instituted numerous corporate governance reforms to rectify this situation. For example, the Tokyo Exchange Group recently finalized its market restructuring rules. Among the latest measures was one that directed listed companies to "comply or explain" if they are trading below a price-to-book ratio of one – an indication a company may not be using its capital efficiently. The exchange warned such companies could face the prospect of delisting as soon as 2026." There is also significant pressure to reform from outside investors, such as Warren Buffett. These reforms appear to be working. Japanese companies are now paying out record levels of dividends, about 20% of earnings compared to 2-3% in 2001. Stock buybacks have also been on the rise, as well as M&A activity. If this mindset sticks, it could dramatically alter the profitability of Japanese companies, and lead to structurally higher earnings growth.

We aren't suggesting overseas earnings growth will outpace US earnings growth but given the low starting valuations, they don't necessarily have to. Right now, overseas equities trade at a two standard deviation discount to US equities. If overseas corporate profits can grow at 5.0%, in line with historical averages and 1.6% below US averages, then they would be poised to deliver over 9.0% annual returns after accounting for dividend reinvestment. There is also the possibility that perceptions about investment abroad change, and valuations eventually turn into a tailwind.

The US Stock Market has Experienced a Prolonged Winning Streak. Will it Continue?

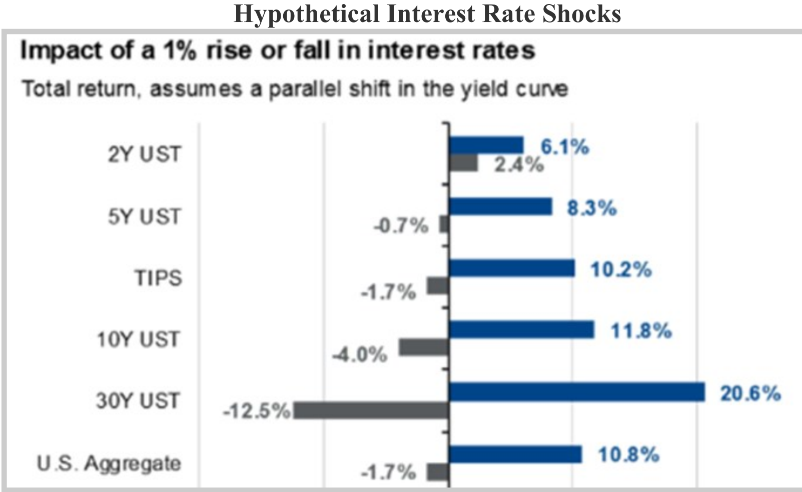


Source: JP Morgan

Fixed Income

Diversification at the asset class level is even more powerful, and essential for investors who don't have the time horizon necessary for successful equity investing. Unlike equities, the potential outcomes for "safe" bonds (like Treasury and Agency securities) are more narrowly defined. This is particularly true for short-term maturities. This should go without saying, but a 1-year Treasury purchased at year-end is going to return 4.8%. A 2-year Treasury's return prospects over a given year are more varied, but still narrow. If interest rates don't move, they will return 4.3%. If interest rates decline by a percentage point, then they could return upwards of 6.1%. Conversely, if interest rates climb by a percentage point, their return would be impaired at only 2.4%. As you go out further in duration, the bond's sensitivity to changes in interest rates climbs.

Hypothetical Interest Rate Shocks



Source: JP Morgan

Now think about prospective bond returns under the three different scenarios: soft landing, hard landing, and no landing. In a soft-landing, today's interest rates are likely at or near appropriate levels apart from short-term rates, which are influenced by the Federal Reserve. For argument's sake, let's assume they would remain largely unchanged. In a hard landing, rates would almost certainly fall, by how much we don't know. In a no landing scenario, rates would need to move higher, but again we can't say by how much.

Here is the math for a portfolio comprised of 50% bonds (aggregate index) and 50% stocks using three rate shocks (flat, -1% and +1%) compared to a portfolio of just stocks. This is admittedly guesswork, but we have crossed out scenarios we think would be unlikely to occur, like a hard landing that coincided with positive equity returns. In both the soft landing and hard landing scenario, the addition of investment grade fixed income is beneficial to the portfolio.

Hypothetical Returns of a 50% Bond & 50% Stock Portfolio

	No-Landing	Soft-Landing	Hard-Landing
	Interest Rate Shock:		
Equity Returns:	1.0%	0.0%	-1.0%
20.0%	~~9.2%~~	12.3%	~~15.4%~~
10.0%	4.2%	7.3%	~~10.4%~~
0.0%	-0.8%	2.3%	~~5.4%~~
-10.0%	-5.9%	-2.7%	0.4%
-20.0%	-10.9%	~~-7.7%~~	-4.6%

Source: Annandale Capital

We like to think about it in terms of how much equity risk are we offloading versus how much upside are we compromising. In this case, we are offloading half of our equity risk, but if a soft landing materializes and equities rally 20%, we still capture 61.5% of the upside. If the soft landing materializes and equities rally only 10% then we capture 73.0% of the upside. In the event of a hard landing, the addition of bonds is extremely beneficial. For instance, a 20% decline in stocks matched with a 1.0% decline in rates equates to a loss of only 4.6% or 23.0% downside capture. The only scenario in which it doesn't make sense to trade off equity risk for rate risk is when rates rise (no landing), but the cost of this tradeoff is insignificant if equity returns are negative.

We would highlight that real yields (nominal minus expected inflation) are at their highest levels in over a decade. Said differently, 10-year rates sit 1.7% above the market's expected level of inflation, which gives us some wiggle room to hold bonds even if the no landing scenario materializes. Furthermore, many of our client's own pipeline stocks carry annual inflation escalators as well as oil & gas royalty interests which should benefit from higher inflation.

Real 10-Year Yields

Source: Federal Reserve St Louis

Conclusion

There is a perception that investment management is about divining the future and then betting accordingly. It is true that some level of prognostication is required, but it is far less than you might think. Investment management is more about managing portfolios in the face of uncertainty. You can estimate what is being discounted by the market, but you cannot predict its future. If every investor is all in on a certain outcome, and that outcome doesn't materialize then the consequence can be grave. It is akin to going to the 1940 Kentucky Derby and betting $5 to make $2 on Bimelech, then losing it all when he places 2nd. We feel comfortable that our portfolios are adequately diversified to handle a multitude of environments and reward the patient investor.

As always, thanks for the trust you have placed in us. We are hopeful for a soft landing and prepared, to the extent possible, for alternative scenarios in the months ahead.