Zevin Asset Management

Q3 2023

MARKET OUTLOOK

"We are navigating by the stars under cloudy skies." That was how Jerome Powell, Chairman of the U.S. Federal Reserve, recently described the central bank's task of taming inflation. We can't think of a more accurate way to describe the central bank's job, but those words don't exactly instill confidence in the single most important organization responsible for steering the largest economy in the world. What the Chairman was referring to is the long and variable lags between interest rate moves and the resulting economic response. The general rule of thumb is it takes between six months and two years for an economy to adjust to higher lending rates. It has been about 18 months since global central banks began this tightening cycle by increasing interest rates and they are likely nearing the end. But just as a ship's captain has difficulty navigating without the aid of visible stars, it's hard for central bankers to know they've adjusted interest rates enough when the final effects won't be seen for months to come. Pause too soon and central banks run the risk of letting inflation reemerge. On the other hand, lift interest rates too high and they run the risk of pushing the economy into recession.

With various inflation measures clearly in a downtrend earlier this year and economic conditions still quite robust, equity markets rallied strongly in the first half of 2023. Through midyear, markets reflected expectations of a "soft landing" where the global economy and inflation would slow, but a recession would be avoided. Hand in hand with the soft landing would typically come a pause in monetary tightening and then interest rate cuts, conditions that equity markets love. But starting in the spring and confirmed several times through the summer, OPEC (the Organization of Petroleum Exporting Countries) announced crude oil production cuts. Oil prices shot up and led to increased uncertainty for the future path of interest rates. If higher oil prices are maintained and lead to generalized inflation, perhaps more rate hikes will follow? It's hard enough to steer a ship without stars but even more so when oil producing nations are shooting torpedoes at you. All that is to say, increased uncertainty for the future path of monetary policy resulted in global stock markets selling off over the past quarter.

Looking forward to the rest of 2023 and into next year, we are concerned that the likelihood of a soft landing might be lower than the optimism of earlier this year. Recent stock market weakness reflects this changing trend. Leading economic indicators are softening and with oil prices around $100 per barrel again, central banks will need to be more vigilant compared to earlier in the year when oil was trading in the $70s. Along with higher oil prices, bond yields have pushed higher, which is also acting to create the current volatile equity market conditions. Over the next several months we expect further cooling in economic conditions. While a recession cannot be ruled out, it's unlikely to be severe. Global central bankers' messaging has been clear: interest rate increases are close to ending and they are very sensitive to economic signals indicating a pause is warranted. With all these crosscurrents in mind, we continue to invest prudently following our time-tested disciplines. We remain confident that a well-diversified, globally invested portfolio should lead to long-term prosperity.

IMPACT UPDATE

Last quarter, Zevin Asset Management continued to share our perspective on racial equity investing, filed our first resolution of the season, and sent letters to pharma companies and their trade associations to advance health equity. In other news, we continue to defend corporate diversity, equity, and inclusion (DEI) initiatives against political headwinds and joined global efforts to protect our fragile biodiversity. You can learn about these and other initiatives and updates in our **Q3 2023 Impact Update**.

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