MACROECONOMICS

Certainly Uncertain

May 16, 2023

Macroeconomic uncertainty is highly elevated relative to history. Elevated macroeconomic uncertainty has historically been associated with poor equity market performance and high financial market volatility

We show macroeconomic uncertainty is likely to remain elevated due to a variety of factors:

- Historically, macroeconomic uncertainty has been very slowly resolved—on the order of quarters and years, not weeks and months
- Economic and financial conditions are only beginning to feel the impact of aggressive monetary policy tightening
- Central banks, for the first time in decades, are likely to face material trade-offs between employment and inflation, which has historically been an impetus for greater macroeconomic uncertainty
- There is an exceptional degree of disagreement between market-based and subjective expectations of interest rates, inflation, and growth—as well as disagreement across different asset classes

Investors should consider protecting their portfolio from a less certain range of economic outcomes by:

- Reducing equity risk in their strategic allocations and diversifying to assets that may outperform in negative growth shocks (bonds) and positive inflation shocks (commodities)
- Adding exposure to alternatives, particularly those that tend to capitalize on elevated volatility and outperform in equity market drawdowns, such as trend following and global macro