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Investment Institute

Market Commentary

Weekly perspective on current market sentiment October 27, 2021

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Last week's S&P 500 Index: +1.6%

The big picture

Key takeaways

- Risks exist in every economic cycle, and that continues to be the case now.
- We want investors to focus on the big picture and the positives that we believe will benefit financial markets in the coming year.

Are investors concerned about numerous risks as they look out over the economic and financial market landscape? Sure they are. A brief list of risks includes rising inflation, upcoming Federal Reserve (Fed) tapering, supply chain disruptions, surging gasoline prices, and the outlook for COVID-19 variants and vaccinations. Our job as strategists is to sift through the various risks that almost always exist at any point in the economic and market cycle and weigh how these risks may affect our current outlook. This set of current risks is no different.

The biggest risk we see out there right now is the general level of inflation. Supply chain disruptions and labor shortages have helped drive up the price of everything from groceries to wages. These price increases are filtering through many segments of the economy and creating headwinds for businesses small and large. Consumer wallets are feeling the effects of higher prices every time they fill their tanks up with gas or buy pork steaks for a weekend barbecue.

But our view continues to be that inflation is in the process of topping out. However, that is going to take a number of months and high Consumer Price Index (CPI) readings are likely to linger well into 2022. We believe headline inflation will decelerate next year relative to this year but remain above the low prepandemic levels. The risk is that inflation stays higher for longer than we or the Fed anticipate and our central bankers take action by draining liquidity and hiking interest rates sooner and to a magnitude greater than financial-market participants expect in an effort to slow the economy and, ultimately, inflation. Stocks would likely react negatively.

We encourage investors to "not miss the forest for the trees." In other words, we believe investors need to focus on the big picture and not just a few components of the current economic and investing climate. Doing this can allow one to grasp some of the meaningful positives that currently exist.

The Fed is still supportive of easy monetary policy, despite the likelihood that the process of tapering bond purchases will begin before the end of this year. We like to remind readers that tapering is not tightening. We believe an actual increase in the fed funds target rate is likely at least 12 months away if not longer. In addition, while the economy has slowed in recent quarters, we expect this year and next to produce growth that is well above the historical trend. Don't forget that around 58% of the U.S. population has been fully vaccinated. That percentage should slowly rise from here. And finally, fiscal stimulus is still having a positive effect on the economy and further (infrastructure) spending seems assured.

Keep the big picture in mind when making investing decisions. The future still looks bright from here.

Risk Considerations

Forecasts and targets are based on certain assumptions and on views of market and economic conditions which are subject to change.

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. Stock markets, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors.

Definitions

Consumer Price Index (CPI) produces monthly data on changes in the prices paid by urban consumers for a representative basket of goods and services.

An index is unmanaged and not available for direct investment.

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