From the desk of GS Wealth Management

MONTHLY ECONOMIC UPDATE

February 2022

MONTHLY QUOTE

"What lies behind us what lies before us are tiny matters compared to what lies within us."

- Ralph Waldo Emerson

MONTHLY TIP

Students who want to enter college this fall should complete the FAFSA early in the year to increase eligibility for student aid. After completing it, they should apply for scholarships as soon as possible.

THE MONTH IN BRIEF

U.S. Markets

Rising yields, elevated inflation, and a hawkish-sounding Fed took turns rattling the stock market in January, with technology-heavy Nasdaq particularly hard hit.

The Dow Jones Industrial Average dropped 3.32 percent, while the Standard & Poor's 500 Index fell 5.26 percent. The Nasdaq lost 8.98 percent.[1]

Fear of the Fed

Anxiety about the Federal Reserve's pivot from its accommodative monetary policy toward monetary normalization hung over the market all month.

Early in the month, the Fed released the minutes from its December meeting, which suggested a more hawkish tone than what investors were expecting.

Inside the Fed minutes, the first update that unsettled markets was the likelihood of an interest rate increase in March, which would be sooner than many had expected. The second update that upset investors was news that the Fed was considering reducing its balance sheet, a step toward tightening that had not been widely anticipated.

More from the Fed

Following its January meeting, Fed Chair Powell indicated that reducing the balance sheet might come at a faster pace than the balance sheet reductions in 2014 and 2018.

Bond yields trended higher in response to Powell's news. Higher yields hurt technology and other high-valuation companies the most.

Economic Recovery

Amid the stock market turbulence, the underlying fundamentals showed a solid economic recovery. Unemployment fell, housing was strong, and fourth-quarter Gross Domestic Product rose beyond consensus expectations. But hot inflation tempered enthusiasm.

Earnings Underway

A strong start to the fourth quarter earnings season caught investor's attention. Of the 33 percent of the companies comprising the S&P 500 Index that reported by month's end, 77 percent reported earnings above Wall Street estimates. While the total "beat" percentage was higher than average, the amount by which earnings actually beat analysts' estimates was by a narrower margin.[2]

Stocks rallied sharply in the final two sessions, taking the edge off an otherwise challenging month for investors.

Sector Scorecard

Except for Energy (+17.07 percent), all industry sectors closed the month with losses, including Communications Services (-8.27 percent), Consumer Discretionary (-13.23 percent), Consumer Staples (-1.05 percent), Financials (-1.33 percent), Health Care (-7.07 percent), Industrials (-5.54 percent), Materials (-7.70 percent), Real Estate (-8.48 percent), Technology (-10.09 percent), and Utilities (-3.86 percent).[3]

What Investors May Be Talking About in February

With the fourth quarter earnings season well underway, investors will continue to focus on earnings reports throughout the month. Expect investors to continue to focus on quarterly reports from high-valuation growth companies.

Earnings from such companies may have a high bar to clear with investors amid expectations for a continued climb in bond yields.

As investors saw in January, these high-multiple stocks can come under pressure as bond yields trend higher. The reason for this is twofold. First, when rates tick up, it's more difficult to forecast future earnings. Second, higher rates may increase a firm's cost of capital.

The Fed

The Federal Open Market Committee (FOMC) at its January meeting left rates unchanged, though officials signaled that rates would likely be raised at its next meeting in March.

The Fed also approved one last round of bond purchases, bringing quantitative easing to an end by March.

The FOMC did not offer details on its plan to shrink the Fed's balance sheet. But Fed Chair Powell indicated that shrinking the Fed's asset holdings may occur at a faster rate than in past periods of balance sheet reductions.[4]

MARKET INDEX	Y-T-D CHANGE	January 2022
DJIA	-3.32%	-3.32%
NASDAQ	-8.98%	-8.98%
S&P 500	-5.26%	-5.26%

BOND YIELD	Y-T-D	January 2022
10 YR TREASURY	0.27%	1.78%

Sources: Yahoo Finance, January 31, 2022.

The market indexes discussed are unmanaged and generally considered representative of their respective markets. Individuals cannot directly invest in unmanaged indexes. Past performance does not guarantee future results. U.S. Treasury Notes are guaranteed by the federal government as to the timely payment of principal and interest. However, if you sell a Treasury Note prior to maturity, it may be worth more or less than the original price paid.

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CITATIONS:

1. WSJ.com, January 31, 2022
2. Insight.FactSet.com, January 28, 2022
3. SectorSpdr.com, January 31, 2022
4. WSJ.com, January 26, 2022