From the desk of GS Wealth Management

MONTHLY ECONOMIC UPDATE

March 2022

MONTHLY QUOTE

"You must expect great things of yourself before you can do them."

- Michael Jordan

MONTHLY TIP

Anyone who starts a business needs an operational strategy. A good one includes metrics, a day-to-day plan detailing who will do what, and an assessment of external and internal risks.

THE MONTH IN BRIEF

U.S. Markets

Escalating tensions in Eastern Europe upended markets in February, sending stocks lower for the month.

The Dow Jones Industrial Average dropped 3.53 percent while the Standard & Poor's 500 Index fell 3.14 percent, and the Nasdaq Composite lost 3.43 percent.[1]

Ukraine's Influence

The buildup of Russian troops on the Ukrainian border dominated the market last month, even before it culminated in a late-February invasion. Volatile stock prices turned lower as hopes for a diplomatic solution faded over the course of the month. The S&P 500 Index fell into correction territory on the eve of the invasion.

As investors woke up to learn that the invasion was underway, stocks suffered steep declines in early trading on February 24. However, they soon staged an extraordinary rally that saw the S&P 500 end the day 1.5 percent higher, after being down more than 2.6 percent. The Nasdaq Composite closed 3.3 percent higher after dropping nearly 3.5 percent during the day. That momentum continued into the following day but then faltered on the final trading day of a difficult month for investors.[2]

Economy Watch

Prior to the geopolitical tensions, investors had been focused on market fundamentals like economic data and corporate earnings. Continued positive corporate earnings surprises buoyed investors, outweighing hot inflation numbers.

With the Omicron variant waning, investors were looking forward to an economic recovery in 2022, but the economic impact of the invasion may dampen that forecast. Those events have also placed the Fed in a more difficult position. It's looking to lower inflation this year but must balance a potential slowdown in economic growth due to geopolitical events.

Sector Scorecard

Except for Energy (+7.07 percent), all industry sectors closed the month with losses, including Communications Services (-7.44 percent), Consumer Discretionary (-4.07 percent), Consumer Staples (-1.41 percent), Financials (-1.38 percent), Health Care (-0.97 percent), Industrials (-0.84 percent), Materials (-1.27 percent), Real Estate (-4.80 percent), Technology (-4.88 percent), and Utilities (-1.91 percent).[3]

What Investors May Be Talking About in March

The Federal Open Market Committee (FOMC) is meeting on March 15–16. The Fed is expected to announce the first of several federal fund rate hikes in 2022 and provide greater clarity on its monetary tightening plans.

While the market consensus is that the Fed will hike interest rates by 0.25percent, the Russian invasion of Ukraine has added a layer of uncertainty. Raphael Bostic, President of the Federal Reserve Bank of Atlanta, commented in a late-January interview that the Fed has not ruled out a 50-basis point hike.[4]

In the past, markets have reacted to FOMC meeting updates and the follow-up remarks made by Fed Chair Jerome Powell at post-meeting press conferences: March may be no different.

Investing During Periods of Inflation

What does inflation mean for your investments?

In August of 2020, the Fed announced that it is willing to allow inflation to run higher than normal in order to support the labor market and broader economy. This major policy shift allows inflation to run above the Fed's 2% goal for some time before the Fed would consider increasing short-term interest rates in an attempt to combat higher prices.[5]

These robust changes to the Fed's long-standing inflation policy further illustrates the importance of understanding how inflation is reported and how it can affect your investments.

What Is Inflation? Inflation is defined as an upward movement in the average level of prices. Each month, the Bureau of Labor Statistics releases a report called the Consumer Price Index (CPI) to track these fluctuations. It was developed from detailed expenditure information provided by families and individuals on purchases made in the following categories: food and beverages, housing, apparel, transportation, medical care, recreation, education and communication, and other groups and services.[6]

How Applicable Is the CPI? While it's the commonly used indicator of inflation, the CPI has come under scrutiny. For example, the CPI rose 1.4 percent for the 12-months ending in January 2021 – a relatively small increase. However, a closer look at the report shows movement in prices on a more detailed level. Used car and truck prices, for example, rose 10 percent during those 12 months.[7]

As inflation rises and falls, three notable effects are observed:
First, inflation reduces the real rate of return on investments. So, if an investment earned 6 percent for a 12-month period, and inflation averaged 1.5 percent over that time, the investment's real rate of return would have been 4.5 percent. If taxes are considered, the real rate of return may be reduced even further.[8]

Second, inflation puts purchasing power at risk. When prices rise, a fixed amount of money has the power to purchase fewer and fewer goods.

Third, inflation can influence the actions of the Federal Reserve. If the Fed wants to control inflation, it has various methods for reducing the amount of money in circulation. Hypothetically, a smaller supply of money would lead to less spending, which may lead to lower prices and lower inflation.

Empower Yourself with a Trusted Professional. When inflation is low, it's easy to overlook how rising prices are affecting a household budget. On the other hand, when inflation trends higher, it may be tempting to make more sweeping changes in response to increasing prices. The best approach may be to reach out to your financial professional to help you develop an investment strategy that takes both possible scenarios into account.

The Fed

In minutes from the Federal Open Market Committee (FOMC) two-day meeting ending January 26, the Fed reaffirmed its plans to raise interest rates and shrink the Fed's balance sheet. Some officials expressed concern about financial stability and the stubbornness of inflation.[9]

"Some (Fed) participants reported that their business contacts remained concerned about persistently high inflation and that they were adjusting their business practices to cope with higher input costs—for instance, by raising output prices or utilizing contracts that were contingent on their costs," according to the minutes. "Participants generally expected inflation to moderate over the course of the year as supply and demand imbalances ease and monetary policy accommodation is removed."

MARKET INDEX	Y-T-D CHANGE	February 2022
DJIA	-6.73%	-3.53%
NASDAQ	-12.10%	-3.43%
S&P 500	-8.23%	-3.13%

BOND YIELD	Y-T-D	February 2022
10 YR TREASURY	0.33%	1.84%

Sources: Yahoo Finance, February 28, 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, February 28, 2022
2. CNBC.com, February 23, 2022
3. SectorSpdr.com, February 28, 2022
4. CNBC.com, January 30, 2022
5. CNBC.com, August 27, 2020
6. Bureau of Labor Statistics, 2021
7. InflationData.com, 2021
8. This is a hypothetical example used for illustrative purposes only. It is not representative of any specific investment or combination of investments. Past performance does not guarantee future results.
9. CNBC.com, February 16, 2022