WELLS FARGO Investment Institute

Market Commentary

Weekly perspective on current market sentiment | **September 21, 2022**

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Last week's S&P 500 Index: -4.8%

Track a few simple factors

Key takeaways

- Rising prices, wars, food shortages, supply-chain problems, and a host of other issues are keeping financial market participants on their toes.
- Of course, the 800-pound gorilla in the room that influences all of these factors is inflation.

The world is a complicated place these days. Rising prices, wars, food shortages, supply-chain problems, and a host of other issues are keeping government officials, and financial-market participants, on their toes. What we want to do in this week's commentary is break these complications down into just a few simple factors that should allow investors to cut through the noise, and pay attention to what we believe is going to drive economic conditions going forward. Of course, the 800-pound gorilla in the room that influences all of these factors is inflation. The Consumer Price Index (CPI) reading for August, showing prices increasing 8.3% over the last 12 months, was not far from the 40-plus year high posted in June. Inflation remains at the top of the global list of issues to be concerned about.

Potentially the biggest overriding factor in seeking to determine the course of the economy going forward is Federal Reserve (Fed) monetary policy. Almost every major central bank on the planet, including the Fed, is hiking interest rates in an attempt to get inflation down to more acceptable levels. The Fed is likely to hike rates another 75 basis points (100 basis point equals 1%) at this week's monetary policy meeting, and is likely continue to hike rates over the balance of this year and into next. In addition, the Fed is allowing maturing Treasury and mortgage-backed securities to roll off its bloated balance sheet starting this month. The proceeds from these maturing securities will no longer be reinvested. Economists refer to this as quantitative tightening, and it is aimed at limiting money-supply growth. The U.S. money supply surged during the pandemic and has been a contributor to inflation (too much money chasing too few goods).

We view ongoing supply-chain disruptions as another important factor to monitor. Have some of these disruptions eased in recent months? Yes, but headwinds still exist for a variety of industries such as automobiles and trucks (lack of chips). China is still enforcing its zero-COVID policy, which has idled factories and resulted in less production of industrial components used in many consumer goods. Union labor negotiations with west coast longshoremen and railroad workers appear to be close to ending positively, but the rank and file have yet to approve the final terms. We believe a disruption slowing the distribution of goods would be a big negative for the economy.

And finally, consumer confidence should help in an effort to determine spending strength looking ahead. Confident U.S. consumers with jobs have tended open their wallets and spend. Consumer spending drives nearly 70% of U.S. Gross Domestic Product (GDP). Consumer confidence has suffered this year, but spending has given the economy an unexpected bump in the July/September quarter. Confidence remains a potential vulnerable point for the economy into 2023.

It may take time as investors sort through these various factors in coming months. Financial markets are likely to remain volatile as uncertainties remain. We believe portfolios should be focused on quality domestic, larger-cap equities, and short-term fixed-income opportunities. We recommend a disciplined plan to incrementally invest sidelined funds while aiming to do so on down days and weeks.

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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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