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Investment Institute

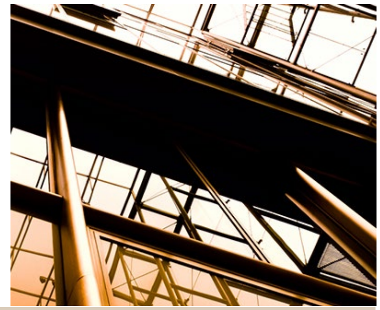
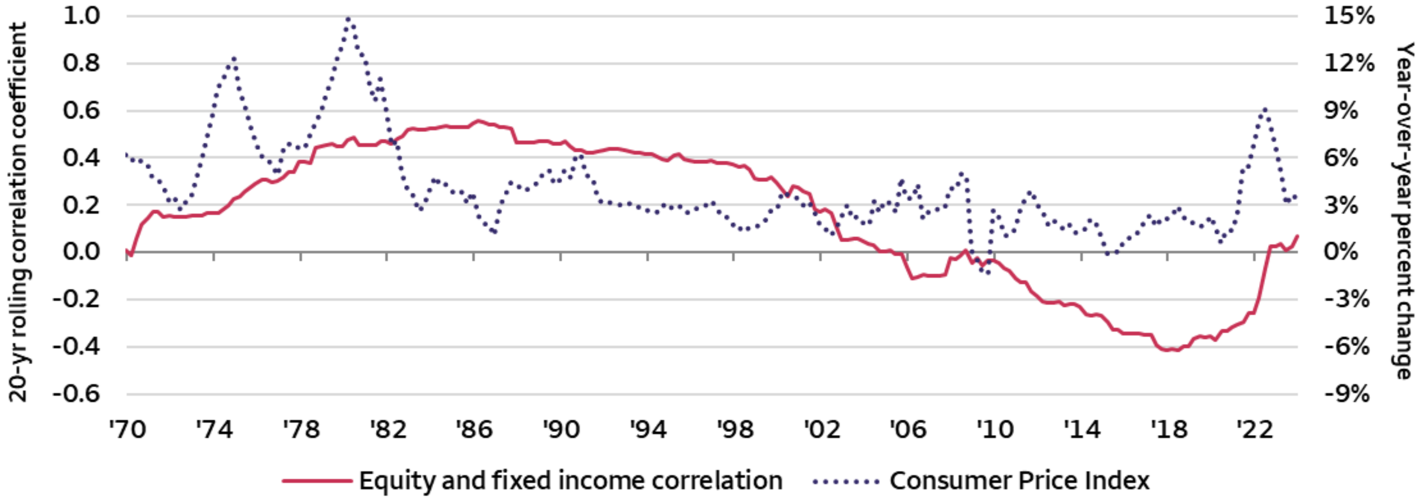


Chart of the Week

Weekly market analysis on key market indexes **March 5, 2024**

Historical perspective on stock-bond correlation



Sources: Bloomberg, © 2024 - Morningstar Direct, All Rights Reserved*, Wells Fargo Investment Institute. Quarterly data from January 1, 1970 to December 31, 2023. Equities represented by S&P 500 Index. Fixed income represented by a blend of IA SBBI U.S. Long-Term Government Bond Index and IA SBBI U.S. Long-Term Corporate Bond Index until 1976, and then Bloomberg U.S. Aggregate Bond Index. Correlations for U.S. markets; calculated using monthly total returns. **Past performance is no guarantee of future results.** An index is unmanaged and not available for direct investment.

Correlation between stocks and bonds has increased significantly in the past two years

The correlation between equity and fixed-income performance was frequently positive from 1970 – 2000, negative for much of 2000 – 2021, and has increased significantly since 2022. Two key macroeconomic factors have historically driven performance — inflation and economic growth. In the past, stocks and bonds have had similar sensitivities to inflation but opposite sensitivities to economic growth.

Although economic growth can affect stock-bond correlations, inflation historically has been the main driver in the relationship. The chart shows that, for the most part, stock-bond correlations have been positive during periods when inflation was rising or falling rapidly (e.g., the 1970s and early 1980s) and have been negative or zero during periods when inflation was at or near 2%. We attribute the recent rise in stock-bond correlations to the spike in inflation post-pandemic, followed by rapid disinflation.

What it may mean for investors

We think that the stock-bond correlation will revert to being negative or near zero in the coming years based on our forecasts for inflation (which we expect to continue slowing before stabilizing slightly above pre-pandemic levels) and interest rates (which we expect to remain at current levels or slightly higher for the next few years). If our forecast is correct, bonds should provide the typical diversification benefits during periods of increased stock market volatility.

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Excerpted from *Asset Allocation Strategy Report* (February 15)

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Definitions

Bloomberg U.S. Aggregate Bond Index is a broad-based measure of the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market.

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

IA SBBI U.S. Long-Term Corporate Bond Index is a custom index designed to measure the performance of long-term U.S. corporate bonds.

IA SBBI U.S. Long-Term Government Bond Index is a custom index designed to measure the performance of long-term U.S. government bonds.

S&P 500 Index is a market capitalization-weighted index composed of 500 stocks generally considered representative of the U.S. stock market.

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