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Market Update: September 2021

Global markets ended September in negative territory, with stocks and bonds off by 4.5% and 1.8%, respectively. U.S. blue-chips stocks, represented by the S&P 500 Index, broke a streak of 7-straight monthly gains, but still managed to eke out its sixth-consecutive quarterly advance. The popular index is showcasing a return of nearly 16% for the first nine months of 2021.

> **You have concerns about the virus, then you add on top of it concerns about the debt ceiling, and some arguably more mixed economic data recently … I don't know if we'll get out of this mode anytime soon.**
>
> **Liz Ann Sonders, Charles Schwab & Co. – WSJ 9/30/21**

Along with worries over the Delta variant and supply-chain bottlenecks, investors also grappled with the rising default risks of China's struggling real-estate developer, China Evergrande Group.

> **The Covid-19 surge also complicated office and school openings, turning what had been expected to be a September boom into a downturn.**
>
> **Sarah Chaney Cambon – WSJ 9/29/21**

Stocks, particularly shares of technology companies, were hurt by rising interest rates, with Treasury yields reaching their highest levels in three months. If that wasn't enough … investor mood swings were also impacted by uncertainties over monetary policy, proposed tax increases, and trillion-dollar spending bills.

Economists have lowered their forecasts for economic growth in the third quarter, but many expect growth to reaccelerate. There are also early signs that the slowdown in spending … particularly for meals, hotels, and airlines … is bottoming out as Covid-19 cases fall.

> **The consumer is in great shape. They have the firepower; they have the ability to spend.**

Aneta Markowska, Jefferies LLC – WSJ 9/29/21

While surveys have been suggesting that investors are concerned about rising market risks, their actions say otherwise.

> **There is a complete divergence in terms of what's in people's heads and what they are actually doing. I think we've seen high levels of nervousness emerge, but we haven't seen high levels of fear emerge. Fear is what causes the positioning to come down. Nervousness causes them to move things around.**

Lori Calvasina, RBC Capital Markets – WSJ 9/21/21

A recent survey by Bank of America showed that cash balances among fund managers remained relatively low … while a net 50% of fund managers are overweight in allocations to global equities.

> **One of the things that we've been talking about is this allocation toward equities, which seems like a very bullish outlook. But really, our feeling is that it's a result of people having nowhere else to invest. With yields as low as they are … there is really no alternative.**

David A. Jones, BofA Securities – WSJ 9/23/21

The Federal Reserve continues to communicate that the current inflation spike is only "transitory". Twelve months ago, the Fed projected a core inflation rate of 1.8% for 2022. Their latest forecast now sees a 2.3% rate of inflation next year.

The message from the Fed's latest projections is that "transitory" is lasting an awfully long time.

Greg Ip – WSJ 9/23/21

Along with maintaining zero-based interest rates, the Fed has also been stimulating the economy by purchasing $120 billion of bonds each month. Their plan is to gradually bring down the bond purchases to zero (also known as "tapering") before raising interest rates. At the September meeting, the Fed signaled that it would start tapering in November, and that the process would be gradual and likely conclude sometime in the middle of next year.

Higher inflation typically brings higher interest rates, and, given their sensitivity to rising rates, bond markets would likely sell off. Also, significantly higher inflation historically has depressed equity valuations, a potential headwind for stocks.

We expect inflation to be higher than it has been over the past decade, but not high enough to be a major concern.

Tim Murray, T. Rowe Price – September Insights

Although both the U.S. and European economies have slowed recently, the Organization for Economic Cooperation and Development asserts that the global recovery has been slowed but not derailed. They expect any shortfalls in growth this year will simply spill over to 2022.

Weekly unemployment claims in the U.S. remain at pandemic lows, but are still about 100,000 higher than prepandemic levels. Overall, the U.S. economy is operating with about 5.3 million fewer jobs when compared to the February 2020 prepandemic employment data.

The big picture is that we expect the labor market recovery will continue.

Nancy Vanden Houten, Oxford Economics – WSJ 9/23/21

In the end, stock prices will depend on the outlook for global growth and inflation. For now, investors apparently believe the Delta variant will fade, supply bottlenecks will disappear, and growth will resume as inflation moderates. But there are certainly plenty of scenarios that would diminish growth rates or enhance inflationary pressures.

> **Wall Street analysts and most policymakers anticipate a "Goldilocks" scenario of stronger growth alongside moderating inflation in line with central banks' 2% target … Rather than fixating on Goldilocks, economic observers should remember Cassandra, whose warnings were ignored until it was too late.**
>
> **Nouriel Roubini, Roubini Macro - Project Syndicate 9/21/21**

The housing market, while still very strong, appears to be slowing down, as children go back to school and workers return to their offices.

Homeownership is generally considered the key to building wealth. But with home prices at record highs, many potential buyers find themselves priced out of the market. Affordability issues can ultimately contribute to greater inequality, impact educational opportunities, and fuel political tensions.

> **The record-setting rise in home values during the pandemic is triggering fresh debates about housing affordability world-wide, as policy makers search for ways to rein in price appreciation without driving prices sharply lower or derailing the global economic recovery.**
>
> **Cherney/Fairless – WSJ 9/27/21**

Much of the current economic debate seems to be centered around China … so let me try to frame some of the issues:

> **Chinese governments have been meddling in the stock market since the 19th century. Again, and again, the authorities inflated bubbles with cheap credit, planted government officials on corporate boards, micromanaged daily operations and subverted the rights of outside shareholders.**
>
> **Jason Zweig – WSJ 9/24/21**

As of the end of August, $43 billion in net assets were held in U.S. mutual funds and exchange-traded funds investing primarily in China. According to Morningstar, U.S. investors increased their holdings by 44% over the past twelve months alone.

The MSCI China index has lost about 30% since its peak in February. In fact, since inception (1992) the index has returned just 2.2% annually … even including dividends. Over that same period the S&P 500 Index has returned more than 10% annually.

> **We are entering an era of one globe, two systems … one can only operate either within China's orbit or outside it. For Western firms, straddling both sides will become unsustainable.**
>
> **Kwok/Patterson – WSJ 9/22/21**

China's crackdown on private businesses has essentially carved-off hundreds of billions of dollars of market value in just the past few months.

> **These are not regulatory events. These are policy interventions to reshape Chinese society, guided by Xi's (Xi Jinping) personal agenda, intended to effect objectives that aren't always knowable.**
>
> **Andrew Foster, Seafarer Capital Partners – WSJ 9/24/21**

At around one-fifth of all economic activity, the housing market is where most of China's household wealth is kept. So, when China's second largest real-estate developer, China Evergrande Group, is on the brink of collapse, the markets certainly take notice.

> **There is never just one cockroach. While we don't know the extent, I will bet you a dollar to 47 donuts that China has dozens of other "Evergrande lite" problems.**
>
> **John Mauldin – Thoughts from the Frontline 9/25/21**

Evergrande is drowning in debt … with billions owed to some 1.4 million homeowners and contractors for unbuilt homes on over 800 projects spread across nearly 200 cities. Chinese authorities are preparing for the worst, and attempting to prevent unrest and contain the impact on economic growth.

> **The looming collapse is a microcosm of China's overheated housing market … Evergrande's problems are the biggest test of Beijing's rejuvenated campaign to end debt-fueled speculation and stop home prices from surging while the government tries to lower inequality and keep housing affordable for the masses.**
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> **Xie Yu/Elaine Yu – WSJ 9/18/21**

Global stock indexes generally include around 5% of their total market value to companies domiciled in China. Investors probably shouldn't stray far from this allocation benchmark, as they struggle to reconcile their support for Chinese equities.

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