March 15, 2022

Turmoil & Uncertainty

Our previous newsletter outlined several issues that we felt would become prominent topics in 2022: inflation, interest rates, and stock/bond/real estate valuations. What we didn't see happening was an invasion of Ukraine by Russia. For many reasons, politically as well as economically, what happens in Ukraine very much matters to the U.S. and the rest of the world.

As predicted, inflation has fully established itself as a major impediment to the growth of our economy for the foreseeable future. Estimated GDP growth for first quarter 2022 is nil. The Labor Department reported that consumer prices jumped 7.9% last month compared with 12 months earlier, the steepest year – over – year increase in 40 years. Inflation is destroying real wages and destroying the consumer's ability to consume. A recent Reuters poll said that ninety-two percent of Americans say they are concerned about inflation. Can you name anything else that 92% of Americans agree about?

This leads us to interest rates. The Fed is in a box – of their own making – yet the Fed Chair Jerome Powell is still lamenting inflation is not hurting the economy at this time. For political reasons, the Fed is way behind the curve to raise interest rates and reverse the effects of the trillions of dollars that were printed since March 2020. Any move the Fed makes to increase interest rates, designed to slow the pace of inflation, won't be felt in the economy for at least six months. If the Fed isn't aggressive enough with its plan on interest rate increases, they risk inflation really getting out of hand (anyone remember the late 1970's and early 1980s?). On the flip side, if they raise rates too quickly, they will tank the stock, bond, and real estate markets and court the risk of sending the economy into a severe recession.

All this at a time when our economy is trying to recover from the Covid19 pandemic. While 4.4 million people went back into the labor force over the last 12 months, there are still 3.5 million fewer people employed today than in January 2020.
Despite wages increasing and government benefits for unemployment tapering off, still 1 in 5 U.S. adults quit their jobs last year – citing low pay, no opportunity for advancement, and feeling disrespected at work according to a Pew Research Center report.

Lastly, for the reasons stated above, Wall Street has turned pessimistic on 2022. Investor confidence has reversed 180 degrees as the market realizes that low interest rates and federally created dollars will no longer be available to continue pushing valuations into the stratosphere. What this means for the equity, bond, and real estate markets is continued volatility and uncertainty in the foreseeable future. It is impossible to predict where valuations for these three sectors will end up by the end of this year. We still think there's a good chance that we may be heading into a period of stagflation – signifying slowing economic growth coupled with high inflation. Our philosophy remains to protect our clients' assets from large scale declines, implement inflation protection strategies and continue to seek opportunity for growth from reliable and proven investments.

As always, we at Kapusta Financial Group, would like to thank you for the trust and confidence you place in our team.