CONWAY• JARVIS LLC

Investment Outlook

Volume 30 Issue 6.4 December 31, 2021

Update

Bidding Adieu to 2021

After a bit of choppy action and a bump in volatility early in the Christmas week, Santa Claus righted the sleigh and delivered the goods for those cooler-headed investors who held fast following the mid-December Fed meeting. That was the meeting where Chairman Powell announced a doubling of the pace of the taper, now ending in March, and would be adapting future policy to changing economic conditions. Nothing dramatic there. In fact, we viewed that as good news. In our most recent Outlook, we warned of rash *interpretations* of Fed statements by talking heads looking for a dramatic lead into the next commercial. If you get your financial news from TV, you might get the impression that inflation is perilously out of control and there will be three Fed Funds increases in 2022. We can't find any such language in the transcript of Powell's statement.

Could there be rate increases in the coming year? Of course, if conditions warrant. It's too soon to make any such predictions but that never stopped the drama merchants at CNBC. We expect the latent effects of yet another strain of the virus and the end of tapering in March to do much to temper the economy's current torrid pace of recovery. We also expect supply chain constraints to ease a bit over time. A combination of these factors is expected to moderate GDP growth in the first half of '22. So, while normalizing key rates *may* begin next year, it's by no means a *probability* that would dictate a significant change in strategy for investors. They might prepare for a less robust investing landscape as liquidity is withdrawn, but that doesn't necessarily foreshadow negative market returns.

A recent poll of 400 investment professionals yielded a modestly bullish view of the stock market in 2022 with 55% expecting positive returns of less than 10% and 20% looking for stocks to do better than that. The remaining 25% are bracing for a flat to negative return. In our view, a recovering economy amid the scarcity of investment alternatives to equities explains why only 2% of those polled saw a bear market arriving in 2022 and why we remain correction-tolerant in our approach. There is a consensus among experts that monetary policy will be a headwind for valuations in the coming year. Their #1 fear is inflation with a policy misstep by the Fed a distant second. To what extent fiscal policy will offset the drawdown in liquidity is presently unknown. That's one of those changing conditions the Fed must adapt to in formulating policy.

Despite the narrative being pushed by the media, the Fed has consistently separated *tapering* from *tightening* in all of its statements. They might find tightening by the first half of '22 unavoidable if inflation doesn't abate following the completion of the taper. However, history points to the *speed* of tightening credit, rather than its commencement, as the culprit in triggering stock market routs. We're all for the Fed lightly tapping the brakes on the economy if needed. We remain mindful that raising key rates is the Fed's first step in *normalizing* the yield curve in a recovering economy. It's a sign of continuing expansion and good news for long-term investors. We have great confidence in this Fed Board and it's why we count ourselves among the modestly bullish crowd as we enter the New Year. Stay tuned.

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