MARKET
MINUTE

SEPT. 13, 2022

INFLATION DATA BLOWS UP MARKET'S NARRATIVE

Until today, the market was self-indulging in the thought that we had reached "peak" inflation and that the Federal Reserve's hawkishness was all smoke and mirrors. Markets reasoned that inflation would continue to decline and a Fed that appears predisposed to be dovish would blink and pause interest rate raises.

That narrative has been gaining steam since the June lows resulting in a furious bear rally, which was only briefly interrupted by Chairman Jerome Powell's eight-minute speech following the Fed's August meeting in Jackson Hole. After a short sell-off, the rally resumed after Vice Chair Lael Brainard's comments, where she said rate hikes would be re-evaluated if they pose a disproportionate risk to the economy. This time, Powell's comments immediately following Brainard's comments didn't slow the markets, as he reiterated the Fed's stated goal of bringing inflation back to the 2% range. The markets again reverted to their preferred narrative and they resumed their rally leading into today's inflation reading.

The problem with fixating on one outcome is that you ignore other potential results. The inflation number for August came in at 8.3% versus expectations of 8.1% – blowing up the "re-evaluation" or "pause" argument for the final time. Markets plummeted on the news, with the Dow dropping 1,000 points by mid-day. It's the largest one-day drop for the Dow since June 2020.

It's clear inflation isn't going to self-correct back to the Fed's target of 2%. We've previously said the only reason inflation came down from the 9.1% June reading was due to a decrease in gas prices. We dropped from a national average of $5 per gallon to $3.7 per gallon in the past two months. But the price of oil is still highly volatile and most of the decline over the past two months was due to lower global demand, not additional supplies. It wouldn't take much to see oil spike again; a natural disaster or geopolitical crisis could move prices quickly. The problem is that nearly everything else – including groceries, gas and rent – is continuing to rise. If gas rises to $5 per gallon, we could see the Consumer Price Index (CPI) get back to 9% or 10%.

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The market's reaction today was predictable. The Fed will likely not only raise rates next week by at least 75 basis points but could potentially raise them higher and keep them elevated for longer to get inflation in check. It seems like the market *finally* got the message today.

It's easy to get discouraged on a day like today. However, if your plan is sound and you are meeting your goals, then stick to the plan. If you're worried about the current state of the market, talk to your advisor and reset to a risk level that's comfortable for you. And keep things in perspective: Markets are still higher than they were two years ago. If you have cash on hand, it might make sense to look at the potential for dollar-cost averaging into this market.

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