

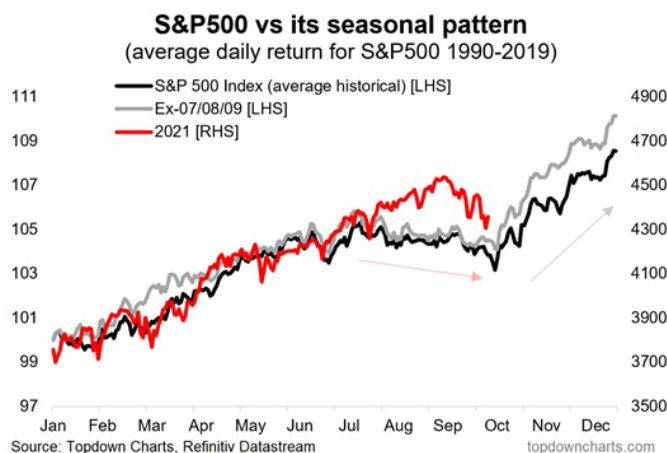
The Advisor

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Market Update -Fourth Quarter, 2021

Speaking of seasonality - the month of September is a traditionally weak period for markets and this year was no different as it lived up to its reputation with the S&P 500, Dow Jones Industrial Average and Nasdaq all losing ground. To put this seasonality into visual context we turn to Topdown Charts. Take a look at the chart below that covers the S&P 500 going back to 1990. It is fairly straight forward to see the pattern but we want to highlight the period around July & August when the S&P 500 broke away from its historical cadence and continued to climb until, well, September. There was a significant disconnect as it appears the market ran ahead of itself only to cool off and begin retreating back towards historical norms. In other words, the recent weakness appears fairly normal.

The good news is that the fourth quarter has been a historically strong period for the markets. The bad news is October is the most volatile month so be prepared for swift moves, up and down. The other word of caution is despite the historical record shown in the chart, it is comprised of data from the past; it is a rearview mirror. The future may bring something entirely different.



Inflation and rising interest rates are still at the core of this market. Yes, there are a number of additional headwinds that we can group together as other, including the abovementioned seasonality trends, U.S. debt ceiling, commodity price increases, Covid, supply chain bottlenecks and even China's Evergrande. Nonetheless, it appears this market has all roads leading back to inflation, rates and Fed policy which begs the question, what's next? In answering this, we'll echo the great Yogi Berra when he said, "It's tough to make predictions, especially about the future," but we can start with the Fed signaling that the committee will likely begin tapering their bond-buying program "soon." We believe "soon" to be the November meeting when the Fed will make the announcement and for tapering to begin in December.

The committee and Fed Chair Powell have maintained a position of transparency and consistent communication. We believe this has given the market ample time to digest the policy and rate environment unlike the taper tantrum in May of 2013 when comments to Congress from Fed Chair Ben Bernanke sparked a nearly 6% decline in the S&P 500. Much of the panic was rooted in the perception of an abrupt shift in FOMC policy that caught the market by surprise. However, the selloff was short lived as it reversed course and the S&P 500 climbed over 17% to close out the year.

In the midst of constant parsing Fed speak, keep in mind the fundamental premise that a healthy economy should be able to stand on its own. The Fed reigning in their accommodative policies because the economy is strengthening should be viewed as a positive. A perpetual zero percent interest-rate world with infinite bond buying is not a good thing. The alternative, and what is a good thing, is an economic environment that is capable of fueling GDP growth that leads to increasing corporate profits.

In addition to the Fed's policies the market is also challenged by the yield curve which is controlled by supply and demand. It is beyond the scope of this discussion to dig into all the intricacies of the bond market but it will suffice to say that inflation expectations play a critical role. Currently, we are facing both acyclical inflation, defined as pressures more closely related to specific industries, and cyclical inflation, or pressures related to the general level of economic health. Determining the causes, impact

and duration of each form is for another debate. The takeaway for our purposes is that inflation erodes the value of future dated assets. The expectation of inflation pushes bond yields higher and forces corporations to not only operate in a higher rate environment but it also discounts future earnings. It is not too hard to see how the intersection of Fed policy, interest rates, and inflation make finding equilibrium in the bond and equity markets a difficult proposition. It takes constant price discovery over time as economic data evolves and all the while market participants are obsessed with predicting and pricing various outcomes. What a great recipe for fear and uncertainty. But if we step back from the prevailing myopic view of the moment and look at things in the aggregate, we can find evidence that despite all of the noise, fits and starts – markets are resilient in providing tremendous opportunity.

We compiled the chart below of the 10-yr U.S. Treasury yield along with the Nasdaq 100 and S&P 500 price levels from 2012 through the end of Q3 2021. We highlighted the 2013 taper tantrum for reference. What do you see? We see, given enough time, markets appear capable of performing well in all different kinds of rate environments. Yes, even rising rate environments. To be clear, we are not saying rates are irrelevant and we understand there are many interconnected factors in play here but we feel it is a mistake to miss the forest for the trees. Which is to say, markets end up being a reflection of the underlying companies they represent – not purely the economic environment. Make no mistake about it, headwinds or tailwinds, companies will find a way to compete and, in the end, it will always come down to some combination of revenue, operating results and earnings.

To our clients, thank you for the opportunity to serve your investment needs and please do not hesitate to contact us if you experience any material changes in your personal situation or would like to discuss any specific matters. To our other readers, if you would like a second perspective on your investment accounts, please feel free to contact us. As fiduciaries, we will happily provide you with an unbiased opinion.

In closing, we invite you to head over to our website to check out an article we wrote about some of the challenges long-term investors face. Hopefully you will find it helpful as a word of encouragement when volatility strikes. For those of you reading this quarter's newsletter in print, you can find the article at, www.aimainc.com/blog

The US10YR, S&P 500, Nasdaq 100 (2012 - Q3 2021)



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