October 2021
Investment Commentary

Over the past few weeks as our Investment Committee discussed the market's recent volatility, we couldn't help but think of the parable of the blind men and the elephant. In the parable, a group of blind men walk up to an elephant and try to describe what they have found to one another. The first man, holding the knee, believes he has found something akin to a tree. The second man, touching the swinging tail, believes he has found a snake. The third man, feeling the tusk, states that he has discovered a large spear. The story goes on to describe how the conversation escalates into a full argument, as each of them suspects the others of being dishonest. The obvious lesson here is that it is easy to lose perspective when our view becomes singularly focused on one or a few specific details.

In today's environment, the details that every market pundit seems to be over-analyzing and arguing over revolve around one of the following risks to the market. We have tried to summarize the most important ones below:

- **The Labor Shortage:** There are currently 10.9 million listed job openings but only 8.7 million unemployed individuals in the US.[(3)] This is leading businesses that are trying to meet the increased demand of post-quarantine consumers to increase their wages to try to attract more workers. Restaurant wages alone rose by 16% over the past year, which is the fastest rate since the 1990s. *The risk is that these higher wages will decrease the long-term profit margins of corporations.*
- **A Constrained Supply Chain:** The increase in consumer demand, combined with the fact that many companies are struggling to find qualified employees, has led to supply chain issues. In fact, during the last month there were 110 shipping vessels just floating off the ports of Long Beach and Los Angeles, California, which together are responsible for 40% of all US cargo imports.[(6)] *The risk is that these types of bottlenecks will lead to a slowdown in economic activity and rising prices as people bid on products that are hard to obtain.*
- **Rising Inflation:** We are now experiencing the highest level of inflation, or rise in the price of goods and services, in 13 years. More importantly, recent data shows that American consumers expect inflation to be between 4% and 5% in the near future.[(5)] *The risk is that both businesses and consumers will reduce their purchases if prices rise too rapidly, leading to an economic slowdown.*
- **A Slowing China:** Last month, China's second-largest property developer, Evergrande, came close to defaulting on their $300 billion of debt. The collapse of Evergrande, and some of China's other real estate giants, could have significant ripple effects throughout the rest of the nation because 70% of the wealth of China's urban population is in the housing market.[(4)] *The risk is that China, which now accounts for roughly 17% of the global economy, may grow at a slower pace than it has during the past decade, leading to slower economic growth around the entire world.*
- **An Energy Crisis:** It is now apparent that there are not enough global gas and oil reserves as we prepare to enter the winter season. Typically, when energy prices rise rapidly, US producers, which account for the largest share of gas production in the world, increase their output. Recently, however, American politicians and investors have encouraged them to refrain from adding fossil fuel capacity, instead pushing them to focus on becoming more green-friendly. As a result, these companies have been more focused on returning excess cash back to investors through dividends or stock buybacks instead of investing in more production. *The risk is that these rising costs will lead to even faster inflation and make it harder for families to meet*

<u>their monthly bills. The UK will be especially affected by this crisis due to their lack of energy storage facilities within the country and their reliance on imports.</u>

- **A Less Supportive Government:** Over the past year the United States government printed more money than it did during the entire Great Depression while bringing interest rates to near-zero levels. Now, however, politicians are seemingly waking up to the fact that, as a nation, we may have increased our debt burden too rapidly. For example, in the last decade our national debt increased by $13.6 trillion, which is the equivalent of adding $2.6 million of debt every minute for the last ten years.(2) As a result, the Federal Reserve is signaling that it may soon stop providing as much financial support for the economy and Congress is looking to push through an increase in the corporate tax rate from 21% to around 26%. *<u>The risk is that the government pulls its support right when one of the above risks become a real problem for the economy.</u>*

Clearly, each of these individual risks could have a large negative impact on both the stock market and the overall economy, which is why so much attention has been given to them. As investors, however, our job is to determine the likelihood of each risk occurring and then work to ensure that our portfolio allocations align with our overall investment goals within this new and ever-changing environment.

Specifically, we believe that, when possible, investors should look to ensure that they are not too overweight in the technology sector which historically underperforms when corporate tax rates increase, and interest rates rise. Conversely, short-duration bonds, financials, utilities, and real estate investments may warrant increased exposure since they should remain largely insulated from many of the above discussed risks.

Equally important to reviewing our portfolio allocations, though, is forcing ourselves to occasionally take a step back from the details of every single risk facing the market to ensure that we do not become today's "blind men." We need to view our current environment within the larger context of the longer-term market performance.

Despite a plethora of traumatic historic events ranging from terrorist attacks and presidential impeachments to high unemployment and real estate bubbles, the stock market has been able to continually grow over time. In fact, since 1950 the stock market has risen during 73% of any 1-year period and close to 80% of any rolling 5-year period. (8)

With this understanding, a 5% or even 10% correction over the next few months should be viewed as less of a threat and more as an expected occurrence that will only make future growth more sustainable. This is not to say a large recession will never happen again (it will) but with household net worth in the US currently at its highest level in recorded history, it is hard to imagine that the stock market will not achieve some additional growth over the next two years. (7) The difference is that going forward this growth may come with significantly more bumps in the road.

The Glen Eagle team wishes each of you a happy, healthy, and blessed Fall & Holiday Season!

The Glen Eagle Investment Team

1) MFS Research "By The Numbers 10.4.21" 2) MFS Research "By The Numbers 10.4.21" 3) Fox Business "Labor shortage poses biggest threat to US economy, most CFOs say" 4) Bloomberg "Everyone Needs to Worry About Evergrande" 5) Apollo Chief Economist 6) The Guardian "A record number of cargo ships are stuck outside LA. What's happening?" 7) JPMorgan "Guide to the Markets" 8) MFS Research "By the Numbers 03.22.21"

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