Email Body 9-21-2021

**Inflation, Delta, and the Economy, Where is it at?**

With the California Recall election out of the way, we can move on to more important matters such as whether the inflation we are currently experiencing is transitory or not, whether there is a crisis at our southern border or not and whether or when will the next Covid-19 variant pop up and what will be the governments mandated responses to it. It is all a lot to take in and the rules keep changing so fast that you cannot keep up. Nevertheless, we continue to take it day by day with a grain of salt and somehow, we manage to survive and even thrive. Keep getting up every morning, take a deep breath and give thanks that we get to see another sunrise.

Hospitalizations in San Diego County and California are trending down and are now at about 27% of the January 2021 peak. San Diego County and California case levels are rapidly declining with seven-day and fourteen-day averages case levels down between 40%-50% of their late-August peaks. San Diego County and California case fatality rates (i.e., the number of covid associated deaths divided by confirmed cases) have increased over the past three weeks but are more than 50% below the long-term averages. Nationally per the CDC, the rolling seven-day average daily cases has dropped from its August 30 peak of 176,452 to its September 19 level of 87,661 or over a 50% drop. Clearly, Delta has peaked in the U.S. Per Johns Hopkins total hospitalizations of covid-19 cases are down about 15% since late August and is accelerating. Don’t look for any extreme Covid-19 measures from the government to slow down the economy.

Market volatility is created mostly by short-term events that receive outsized publicity in the modern era. So it was on Monday when the Dow Industrials index fell almost 1,000 points intraday when it was announced that Evergrande, a Chinese real estate company, is on the verge of defaulting on $300 billion in debt. U.S. markets were Déjà vuing to 2008’s Lehman Brothers debacle where another company with too much debt would have frozen the bond market absent industry and government intervention. The good news is that Chinese authorities are taking action to stem the red ink and restructure the company preventing major fallout in China’s financial markets and abroad. The reality is that it is long-term trends such as population growth and productivity improvements that drive GDP up and with it the financial markets. Both trends are in reasonable shape in the U.S. and should represent growth opportunity for longer-term oriented investments.

Over the next twelve months economic fundamentals appear to be on solid ground. Retail sales and manufacturing numbers continue to move higher; consumer and business confidence is growing, and corporate sales and earnings continue to exceed expectations. The Federal Reserve is expected to begin reducing bond purchases by the end of the year and to possibly raise short-term interest rates by 2023. Expect a snail’s pace in these changes going forward. The result is likely to be a good market for stocks for the next year. Bonds will tread water or may even drop a little as interest rates begin to rise.

Risks to this scenario are likely some years out (e.g., no guarantee) and they begin and end with gargantuan Federal debt and Federal Reserve money printing. In 2020 only 39% of citizens paid any income taxes. Unless that changes or unless we somehow reduce government spending relative to GDP, the Federal Reserve is going to have to keep interest rates low and continue printing money to allow the government to pay its bills. Ultimately, the result will be a higher level of inflation (i.e., I estimate longer-term 2%-4%) and a reduction in the value of the dollar relative to other currencies.

I say this not to scare you, but to prepare you for what I think is ahead. Investments in companies with growing sales and earnings and reasonable levels of debt, will successfully navigate the pitfalls of the future. Investment strategy should be based on a portfolio’s objectives, ability to tolerate volatility and its investment time horizon. Assets you intend to utilize or spend in the near-term (i.e., 1-3 years) should be exposed to less risk. Assets that can remain invested over a longer time frame (i.e., 4-5 years) should remain invested consistent with your investment goals and risk profile. Successful investing is not about timing the market. It’s about being able to ride through the inevitable volatility that creates the opportunity for positive returns.

I am always available to you via phone, zoom conference or in person. I look forward to talking with you over the next few weeks. If you have any questions or if we can be of any help, please do not hesitate to contact Linda or me.

As always, stay safe and healthy!

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