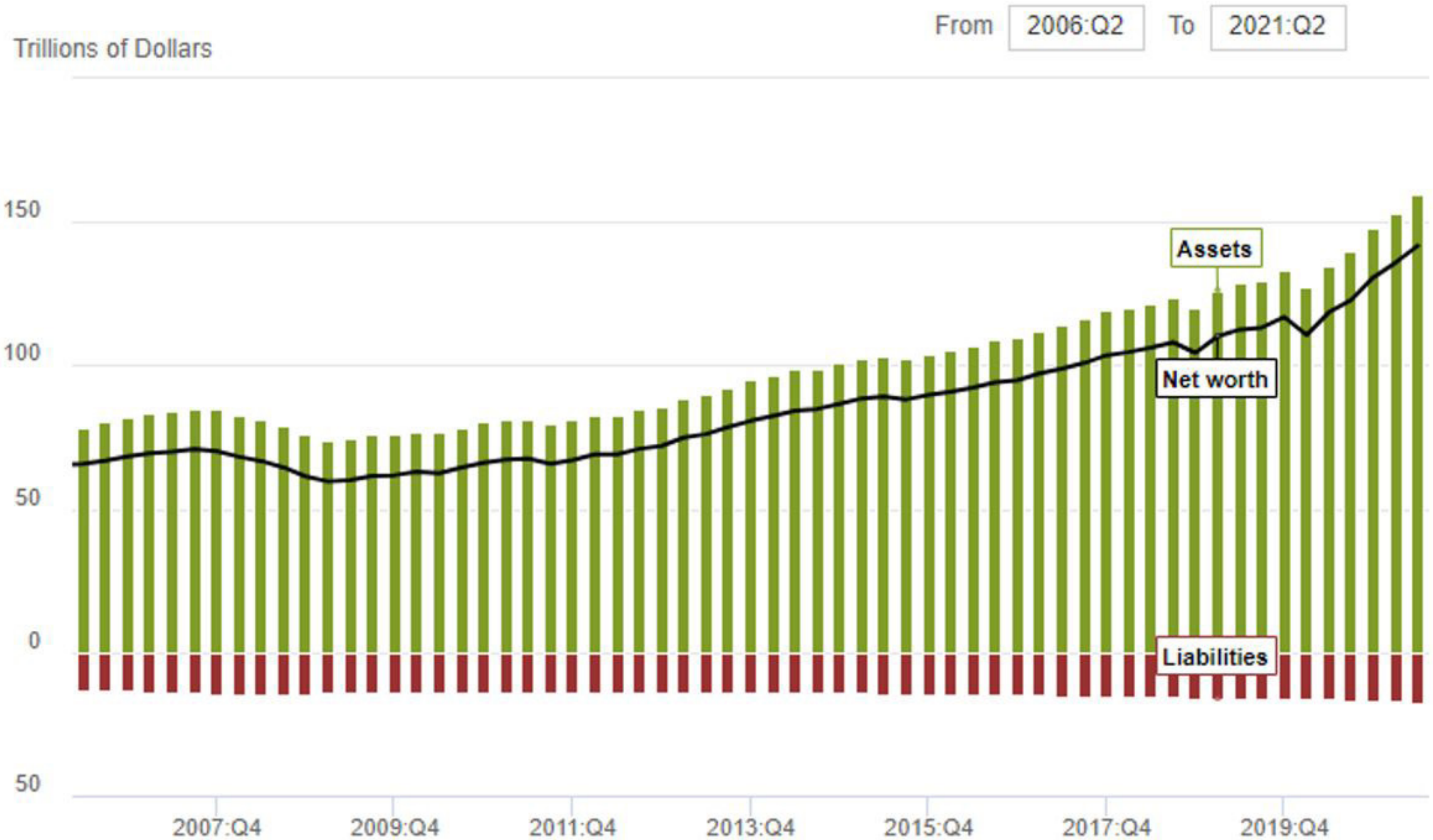
Week in Review

Friday, September 24th, 2021

1. US Household Wealth Sets Record Levels

The Federal Reserve released data this week that showed US household wealth reached a new record of $141.7 trillion at the end of June. The increase was boosted by strong stock market gains and rising home values. The overall increase over the first quarter of 2021 was $5.9 trillion or 4.4%, and on a year-over-year basis, the increase was $24 trillion or 20.3% - both historically high levels. The level of growth in US household wealth is truly unparalleled as it has occurred during a period of economic dislocation due to the coronavirus pandemic and suggests the unprecedented levels of monetary and fiscal policies have fortified balance sheets and unlocked higher asset prices.

Assets, Liabilities, and Net Worth



Source: Federal Reserve

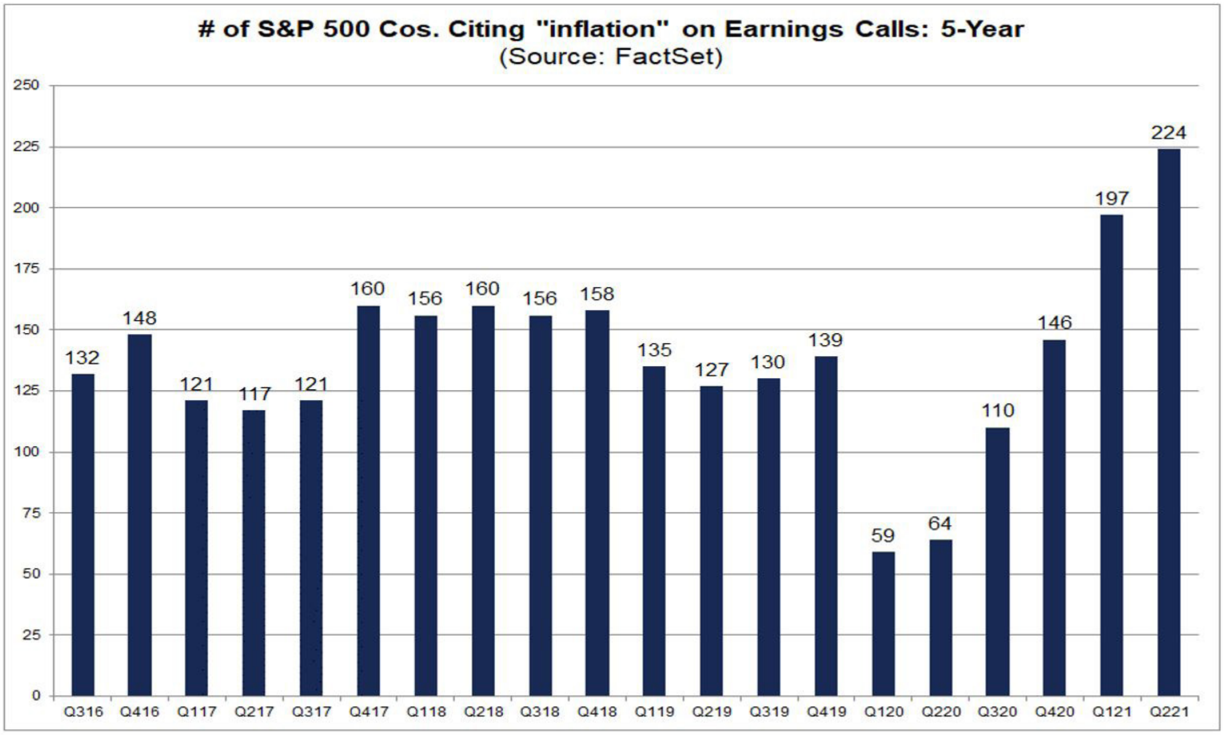
With the Federal Reserve open to easing monetary stimulus potentially later this year, economic growth and employment will likely need to be the driver for the next leg to support rising household wealth.

2. The Federal Reserve Leans a Little More Hawkish

The Federal Open Market Committee (FOMC) met this past week. The FOMC is the committee that decides how to manage monetary policy and has pursued a very accommodative set of policies to stimulate the economy throughout the coronavirus pandemic. The twin mandates that the FOMC seeks to achieve are full employment and a reasonable level of inflation which they have pegged at around 2%. Between the two mandates, the focus on employment has been favored in terms of the policies pursued, but in the meeting this week, the door was opened to change course as early as later this fall, albeit slowly.

Currently, the Fed is purchasing approximately $120 billion a month in treasuries and mortgage-backed securities. In this week's commentary, the Fed stated that "if progress continues as broadly as expected, the Committee judges that a moderation in the pace of asset purchases may soon be warranted". During a question-and-answer period, further hints were conveyed that this could include a reduction of approximately $15 billion per month, culminating in a full phase-out of the purchases by mid-2022. The FOMC did not discuss raising the Federal Funds Rate (the rate at which commercial banks borrow and lend their excess reserves to each other overnight). The Federal Funds Rate is unlikely to be raised before the full phase-out of securities purchases and is not anticipated until late 2022 or 2023.

A potential change in policy comes as data increasingly suggests that inflation, currently elevated, is impacting businesses and could be a headwind to the economy if left unchecked. The following chart displays the record prevalence for which companies in the S&P 500 mentioned inflation as a factor impacting their businesses when discussing their second-quarter results.



Source: Factset

However, statements from the Federal Reserve indicate the belief that the current elevated level of inflation is expected to be transitory. This belief supports their actions to only change monetary policy at a measured pace. The market's response to the latest FOMC news was neutral to positive with only a slight change in interest rates. This suggests that the Fed has successfully communicated its intentions and the pace of change is expected to be supportive of economic growth and the markets.

Thinking Ahead

September has historically been a volatile month for the markets. With a week still to go in the month, September 2021 is living up to the reputation with political and international concerns impacting sentiment, adding to the ever-present shadow of COVID. Political reasons have led the list. Issues include the debate on raising the US debt ceiling, a higher tax proposal, and fiscal spending policy, including whether infrastructure spending packages will proceed or not. International concerns have also been elevated this month highlighted by the potential debt default of a large Chinese development company (Evergrande). Evergrande has raised concerns about the broader credit markets, the underlying growth rate in China, and lower commodity prices. All in all, the markets have so far weathered the turbulence well.

Pallas Capital Advisors will continue to monitor economic, political, and corporate data for implications to the markets.

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