Monthly Market Review

October 2021

What happened in October?

The MSCI All Country World Index rebounded **+5.1%** in October as it reached a new all-time high. Meanwhile, the Barclays US Aggregate Bond Index was flat, broad commodities gained **+5.8%**, and gold appreciated **+1.5%**.

Corporate earnings remain robust as companies pass higher costs onto consumers.

84% of S&P 500 companies have reported earnings for the third quarter, and results continue to be strong. In aggregate, companies have generated year-over-year earnings growth of +41% and have outpaced consensus expectations by +10%. Earnings reports show that although companies are facing higher cost pressures, they have been able to pass price increases onto consumers because consumer demand remains elevated in the wake of the unprecedented fiscal support that has been provided throughout the pandemic. However, as inflation rises, the risk these costs can no longer be passed on increases; therefore, this dynamic requires close monitoring.

The Fed begins to taper asset purchases but doesn't expect to raise rates any time soon.

At Wednesday's Federal Open Market Committee meeting, Fed Chairman Powell communicated that the Fed would begin to taper its monthly pace of bond purchases from $120Bn to $105Bn, and the pace of tapering will likely increase into 2022. Although the Fed will begin the tapering process, it does not believe it is prudent to raise interest rates at this time, citing its view the US economy remains far from maximum employment. Chairman Powell also expressed that although inflation has been more persistent than expected, the Fed still expects it to decelerate by the second half of 2022 as supply chain bottlenecks abate and job growth accelerates. On a related note, Goldman Sachs recently laid out its roadmap for supply chain normalization that includes its expectation that three to four million Americans will return to the labor force in the next few quarters—which should help ease supply chain bottlenecks—as pandemic insurance is phased out and children return to school (see Chart of the Month).

Following Powell's comments, equities rallied, and bonds tumbled, which we interpret as a positive sign for risk sentiment. The aggregation of market signals we're tracking to gauge stagflation risk indicate that stagflation is not a material concern currently.

Facebook bets big on the metaverse.

We wrote in July that investors should get used to the term "metaverse," a term that has many interpretations, but we define as the continued integration of the physical and digital worlds. Last week, Facebook announced that it will be investing tens of billions of dollars into the metaverse and will be changing the name of the company to Meta. Facebook's initiative is not surprising to us because its social media platform combined with its virtual reality technology (i.e., Oculus) and sizeable balance sheet put the company in good position to serve as a leader in this developing theme. We recently favored increasing exposure to companies that stand to benefit from the realization of the metaverse.

Congress is making progress on budget reconciliation, and two large spending bills could be approved in the coming weeks.

Democrats are edging closer to a deal on the Build Back Better Act—a $1.75 trillion social and climate spending package—while the $1.2 trillion infrastructure bill the Senate passed in August remains idle. Democratic lawmakers expect to vote on both bills next week.

Per the Wellspring communication we sent last Saturday, the new version of the Build Back Better Act poses fewer tax changes than its predecessor. Click here for details regarding potential tax changes.

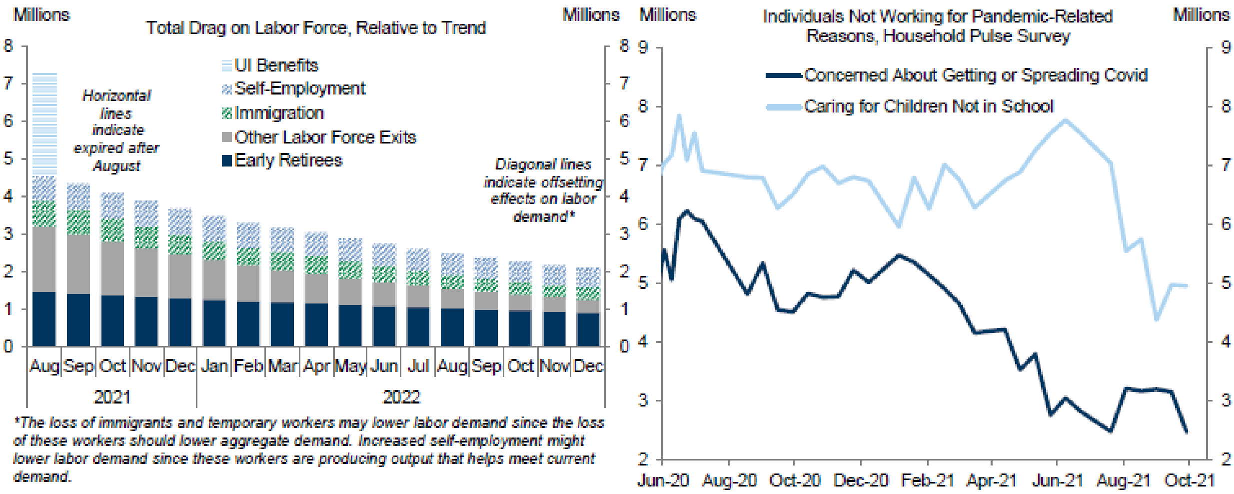
Positioning Highlights

Although equity valuations are elevated, our economic outlook remains constructive, and thus we favor remaining overweight risk assets.

- **Maintain overweight exposure to equities.** We favor increasing exposure to equities as the economic recovery progresses.
- **Increase exposure to growth stocks within equities.** We favor increasing exposure to growth stocks because of our expectation that high economic growth will persist while inflation remains under control.
- **Maintain underweight exposure to defensive assets.**
  We favor maintaining an underweight posture in defensive asset classes (e.g., fixed income) because we expect defensive assets to underperform while economic growth remains elevated.

Chart of the Month

We expect US job growth will continue to increase in the coming months as (1) pandemic insurance is phased out, (2) children return to school, and (3) the severity of the COVID-19 pandemic continues to decline.



Source: Goldman Sachs Global Investment Research, Census Bureau

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