

Better Inflation News Spells Opportunity

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Last month, I wrote that good news on inflation could be the catalyst that gets the market moving. Well, that good news materialized on August 10: Inflation rose 8.5% in July, down from 9.1% the previous month.

Make no mistake, 8.5% inflation is very bad for consumers. Our grocery bills are 8.5% higher than they were a year ago. But for investors, what counts is the direction of inflation. While the rate of price increases is still high, it looks like it might have peaked in June. The stock market rallied more than 4% over the subsequent week before giving back some of its gains.

The takeaway here is that the market moves based on what it thinks will happen going forward. And the signals are that it believes inflation will continue to moderate, relieving pressure on consumers and corporate earnings. I anticipate that the monthly inflation numbers will continue to drop. Remember, the CPI data are lagging indicators: They reflect what's already happened but not what's happening right now. And what's happening currently is that commodity prices are continuing to fall and, based on my own observations at the grocery store, prices of consumer staples are falling too.

So with an ugly first half of the year in the books, we should see stocks start to perform better. It's highly unlikely that this will be a smooth ride, though, so investors should buckle in. One major headwind for stocks is that the Federal Reserve plans more aggressive interest-rate increases as it continues to fight inflation. All eyes will be on next month's meeting of the Fed's policy-setting committee. Will the Fed raise interest rates .75%, as it's done twice so far this year? Or will it choose a less aggressive approach? Bringing inflation under control without stalling out the economy won't be easy.

In the meantime, we have an opportunity to invest. It may be wisest to nibble in the near term, and if and when the good news continues, to get more and more fully invested.

Don't hesitate to reach out to us if you'd like to discuss your investments.