PATRICK H. YANKE, CFP® | Finance

Financial Outlook for 2022

It's always difficult to pen an article on the economy for a periodical magazine. Forecasts are valid as long as the current assumptions hold. There are a number of wildcards at play in this economy. I'm going to take that risk with this article and give a perspective on the economy and markets from my view near the end of 2021.

There are currently two divergent perspectives on the economy. Most economists see a healthy economy headed toward solid growth in 2022. That may be true overall when all economic factors are aggregated. However, a pessimistic perspective sees some cracks in the foundation that deserve attention. Small businesses are an important component of the U.S. economy and the employer for nearly half of all private-sector jobs. Their health matters, too, and it isn't as solid.

Talking to investors, I sense some significant uncertainty over the year ahead. Areas of concern include COVID variants, supply chain disruptions, inflation, and mid-term elections.

COVID

We seem to have signed up for the variant-of-the-month club. As each variant comes through without the world ending, panic should eventually subside and we will likely get used to it as we have the annual flu season. That isn't to say that COVID will have no economic impact. Its greatest impact will be from policymakers maneuvering the levers of government power to control the spread. Their success now and in the future are both up for review and debate.

SUPPLY CHAINS

COVID restrictions have had a significant impact on shipping. Producers are working to keep up with demand but there are bottlenecks in the delivery process. Shippers have pricing power to raise fees to "rush" goods to market and that is driving up costs. These higher costs are a negative for producers and consumers… but a boon to the shipping industry. Retailers and consumers are willing to pay more to expedite their goods above the lowest priority shipping.

INFLATION

Neither the economy nor Federal Reserve officials have had to contend with meaningful inflation in the last three decades. That recently changed. You may have noticed. According to Darrell Spence, an economist with Capital Group, "When stimulus-induced demand met COVID-restricted supply, it created distortions in the economy. That fueled rapidly rising prices wherever there were bottlenecks."

Fed officials continue to forecast that high inflation levels in the U.S. are transitory. Prices should retreat once the distortions are corrected. Spence expects inflation to remain elevated throughout 2022. He doesn't see this as the "new normal," but it may take longer than Fed officials expect for inflation to moderate. It takes time for supply and demand to come back into balance.

From an investor standpoint, stocks and bonds have both generally done well during periods of elevated inflation. It's mostly at the extremes—inflation above 6% or negative—that financial assets tend to struggle. Since inflation erodes company profits and investor returns, investors may reduce the impact by sticking with companies with pricing power—those with the ability to pass increased costs on to customers.

MID-TERM ELECTIONS

Financial markets have generally taken a pause before major election cycles. They tend to spend election years relatively flat and then move after the outcome is known. Given the uncertainty around a tightly balanced Congress, I expect to see that trend continue this year. Although mid-terms tend to favor the minority party and that may herald legislative gridlock, uncertainty will be the trend ... until it isn't.

Wall Street has done well this year. Main Street has struggled. Rising inflation and a reluctant workforce have stressed the average small business to extremes. How long can the economy and markets flourish if Main Street continues to flounder? That is something only time will answer. However, this is an imbalance that needs immediate attention.

Investors should consider maintaining a balanced approach to their investments with broad diversification and adjust as new inputs are digested.

These are just my views on the year ahead. Hopefully, they are still relevant when published. Always consult appropriate tax, legal, and investment professionals to determine appropriate investment decisions for your financial situation.

Patrick Yanke is a Raleigh-based financial advisor. Opinions expressed here are mine and not necessarily those of Raymond James. The information is not a complete summary or statement of all data necessary for making an investment decision and does not constitute a recommendation. This article is not meant to provide tax or legal advice. Please consult the appropriate professionals. www.yankefinancial.com.