# TouchStone Market Commentary

## Moving Parts

With all the volatility lately, we thought it would be a good idea to comment on some of the factors that are moving the markets.

From an investing perspective, the last 12 months can best be described as a stock market that was convinced Covid was behind it and projected a fast (very fast) return to normal. Well of course we all know that "normal" is not yet upon us. This made for a potentially vulnerable investment landscape.

Then September came.

- Supply chains became strained – as you all know, getting goods and services these days is often frustrating. When mines and factories are not fully open, it leads to two things…shortages of the things needed to make other things….and higher prices for all (just try buying a car in the last 6 months).

- In some cases, companies can pass along their higher costs to the end purchaser. In other instances, companies cannot pass along the costs as fast and must absorb them in the short run. For the former, higher prices can lead to lower demand from consumers. For the latter, it means lower margins. In both cases, it can lead to share price volatility as the market adjusts. This is exacerbated when markets are priced for perfection (as it was).

- The increased costs are ramping up inflation fears. This almost always leads the Central Banks to raise interest rates. But one of the questions is: can the economy withstand higher rates? We don't know…no one does.

- Bottom line: rising inflation and interest rates are always a symptom of market malaise *in the short run*. In the long run the market adjusts and puts faith in other sectors of the market. It is that period now when the debate is raging…are we in a prolonged period of inflation or is inflation temporary while supply chain issues are addressed. No one knows the answer, and on a daily basis the market moves from one camp to the other. The result is a stock market that can swing back and forth hundreds of points even within the same day.

- If rates are heading higher, beware the leveraged. As you may have heard, there is a large property developer in China that has started to falter and is unable to make its debt payments. This may be the first signal of serious problems in China's overbuilt, over-leveraged, under-occupied, property development industry. We think it foolish to assume that only ONE property developer is in trouble. The news may be the first shot across the bow…and if rates rise, more may weaken under the strain of making debt payments. As far as we know, it's hard to make debt payments with rent from empty apartments.

Everything is linked. Shortages lead to supply woes…Supply woes lead to higher prices…higher prices lead to higher interest rates…higher rates lead to problems for those that are laden with debt.

Generally speaking, stock and bond markets can deal with periods of being overvalued – they justify "themselves" by saying profits will catch up to valuations. However, what markets DON'T like is uncertainty thrust upon them. The above listed issues are leading to uncertainty, and while we are confident that the market will adjust to most of the above in short order, it is concerning *IF* any become a protracted problem.

In the meantime, we have increased our defensive cash position to protect capital should more surprises be pushed to the front page. *Perhaps* new leadership will emerge in the market, and that is what we are focused on identifying. We don't feel we have to catch the bottom of the market, knowing that if we pick the right investments that there will be plenty of profits to be made with lower risk.

As always, we would be happy to discuss this with you over the phone or by zoom. We look forward to the day when we can meet face to face!


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