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Perspective on First Quarter 2022 Economic & Market Events

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The first quarter of 2022 served up a quadruple whammy: Omicron, Russia's invasion of Ukraine, persistently high inflation and increasing interest rates. Omicron hit the U.S. hard in January but fortunately receded quickly, only to be replaced by concerns of Russia's invasion of Ukraine in late February. Meanwhile, high inflation, which the Federal Reserve had initially characterized as "transitory," proved to be rather sticky, reaching a 40-year high of 7.9% in February. The war in Ukraine fueled further price increases that were already at record levels due to labor and supply chain constraints. Then, the Fed increased the federal funds rate for the first time since 2018. There were few places to hide during the quarter as we witnessed the atypical occurrence of declines in both stocks and bonds. [1]

Though indications were strong that the U.S. economy would continue to grow, employment strengthen and multiple manufacturing and services indicators were pointed to expansion, the U.S. experienced its first decline in gross domestic product since the short and sharp pandemic recession nearly two years ago. The economy is still showing signs of resilience but inflation increased at a rate higher than wages over the past year and remains a primary concern for consumers. Not only have housing prices increased dramatically over the past year, jumping 19%, but the sharp rise in groceries and the price of gas at the pump have eroded consumers' household budgets. Inflation will likely continue to be a challenge as the year wears on, especially since the rise in housing costs is not yet fully reflected in inflation numbers. [2,3]

The much-anticipated rise in interest rates came in March, as the Federal Reserve raised the federal funds rate for the first time since 2018. The benchmark federal funds rate was increased by a quarter percent to between 0.25-0.50%. Also in March, the Fed released new projections for interest rate increases. This past December, projections suggested three quarter-percent increases in 2022. Now, officials are signaling there might be as many as 11 rate hikes through 2023, moving the fed funds rate closer to 3%.[4]

These new projections are a product of the larger-than-expected rise in inflation. Additionally, COVID-19 is still playing a role in supply chain disruptions which are contributing to a sharp rise in the cost of goods. Coupled with Russia's war on Ukraine and the sharp increase in the price of oil, the result is an unhealthy inflation environment. While U.S. oil prices have increased, the United States is currently one of the largest oil producers in the world and has been able to stave off drastic oil shock better than in previous disruptions. [5]

While higher rates may be effective for lowering inflation longer term, this improvement may come at a short-term cost to investors. Higher interest rates, along with any shrinking of the Fed's balance sheet, may reduce liquidity in the markets, which may put some downward pressure on stocks.

Though the Federal Reserve seems to have a strategy to manage inflation that the markets are absorbing, the wild card for investors seems to be what Russia does next, which could be as disparate as agreeing to a withdrawal from Ukraine with a promise to respect Ukraine's territorial integrity to invading additional countries and ratcheting up tensions with the West. A peaceful resolution to the Ukraine crisis may be met with deep relief by investors, potentially allowing markets to rally and return their focus to economic fundamentals, like GDP growth, inflation, and corporate profits. A widening of tensions may prove problematic to the financial markets and the economy, especially if Russia takes steps that violate the borders of NATO countries or if China pursues an invasion of Taiwan.

We've seen markets unsettled by war in the past. They tend to regain their balance in a relatively short period. However, the conflict in Ukraine is very different from other recent wars, thus, the market's near-term performance may first and foremost react to the outcome of events in Eastern Europe. A look back at history shows that despite all manner of challenges, financial markets have historically moved onward and upward, as has our nation as a whole.

As always, we appreciate the opportunity to work with you. It is our privilege to guide you through life changes, economic shifts and global uncertainties among so many other factors that may affect your financial future and to earn your trust through these seasons and cycles. Please contact your Investment Advisor Representative to assist or answer any questions you may have.

1. Bureau of Labor Statistics, March 15, 2022
2. Marketwatch.com,, March 14, 2022
3. https://www.reuters.com/business/us-economy-contracts-first-quarter-weekly-jobless-claims-fall-2022-04-28/
4. www.tradingeconomics.com
5. Reuters.com, 3.21.2022