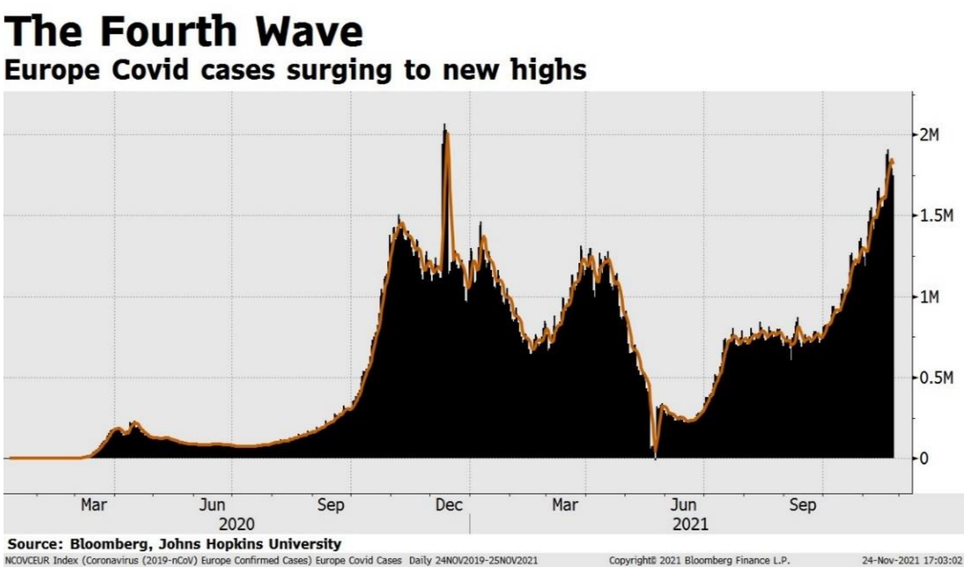
Courier Capital, LLC
Registered Investment Adviser
An affiliate of Five Star Bank

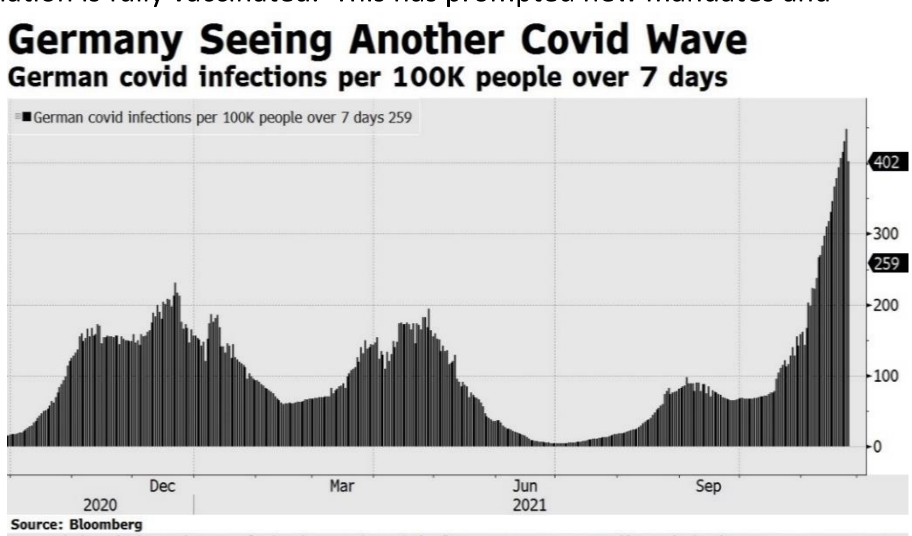
Economic and Market Update – DÉJÀ VU HOLIDAYS (11/30/2021)

Latest Developments and Economics

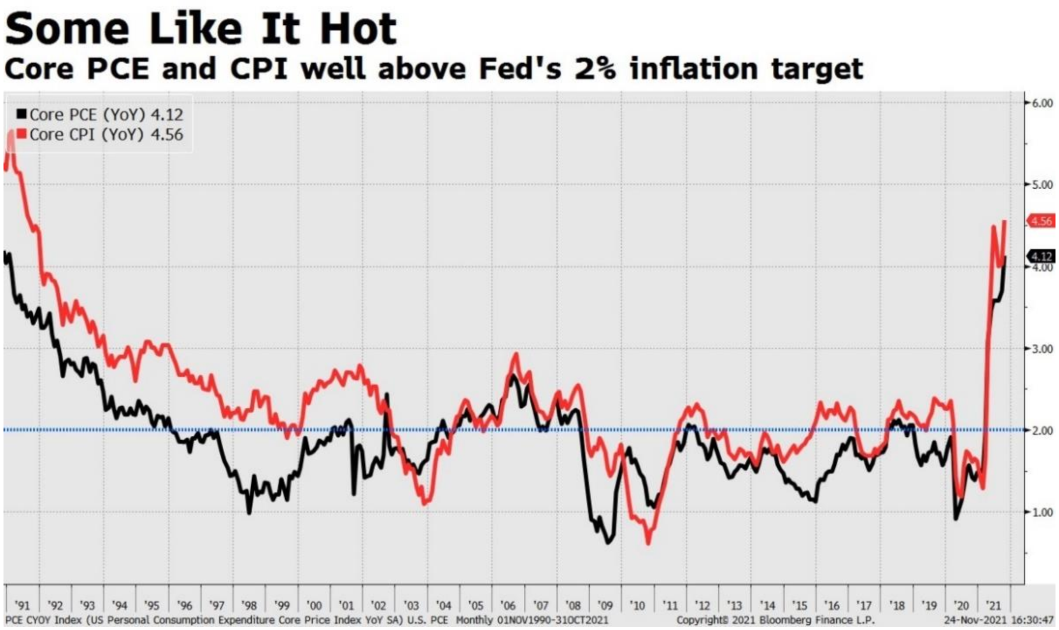
After more than 20 months talking almost exclusively about COVID and then the Delta variant, the virus is once again reminding us that it still controls the narrative. A new strain of the virus, labeled B.1.1.529, has been confirmed in South Africa and the reaction has been swift. This variant contains more than 30 mutations of the spike protein, which is the most significant part of it invading human cells. It will take several weeks for scientists to compare its transmission, morbidity and resistance to vaccines and treatment to previous strains. It is sufficiently different from Delta that it received its own Greek letter identity – Omicron – from the World Health Organization (WHO) which held an emergency meeting last Friday to determine the appropriate response. About 90% of the cases in the Gauteng province (which includes Johannesburg) are from the new strain and the U.K., U.S., Singapore and the European Union have restricted or halted travel to and from southern Africa. The good news is that it has been detected early and Pfizer and Moderna are already working on vaccines which could be available in three months. That did not stop a quick reaction in financial markets globally as most have responded with a quick 2% drop in most equity markets on Friday with reopening stocks taking the brunt of the decline.



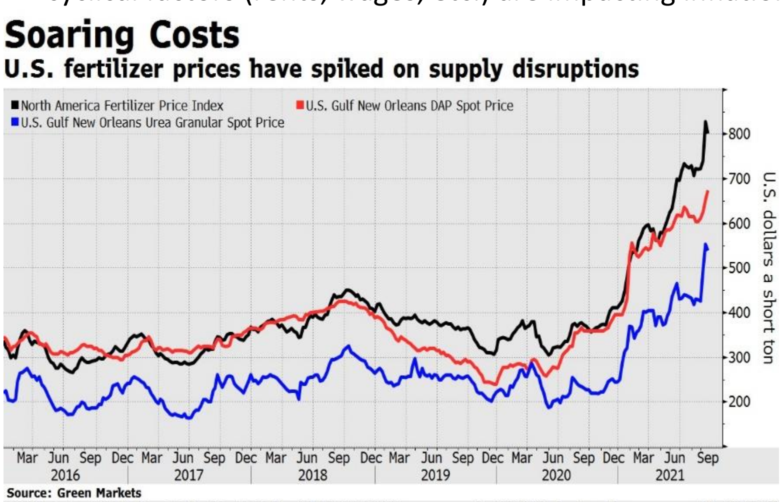
This comes on top of a fourth wave of Delta around the world. Europe is struggling with this new wave despite a significant percentage of the population vaccinated and moving on to booster shots. This is not the case in Africa where only about 35% of South Africans are fully vaccinated and less than 7% of the African continent vaccinated (which makes the new strain potentially more dangerous). One of the exceptions is Germany where only 68% of population is fully vaccinated. This has prompted new mandates and restrictions. Germany has already shut down their Christmas markets and are considering tougher restrictions and potentially lockdowns given the record daily infections. This prompted a strong reaction from Jens Sohn, Germany's health minister, to say that soon "pretty much everyone in Germany will be vaccinated, recovered or dead." Neighboring Austria had already entered their fourth national lockdown with all activity shut down until December 12. They are also the first European country to make vaccination a

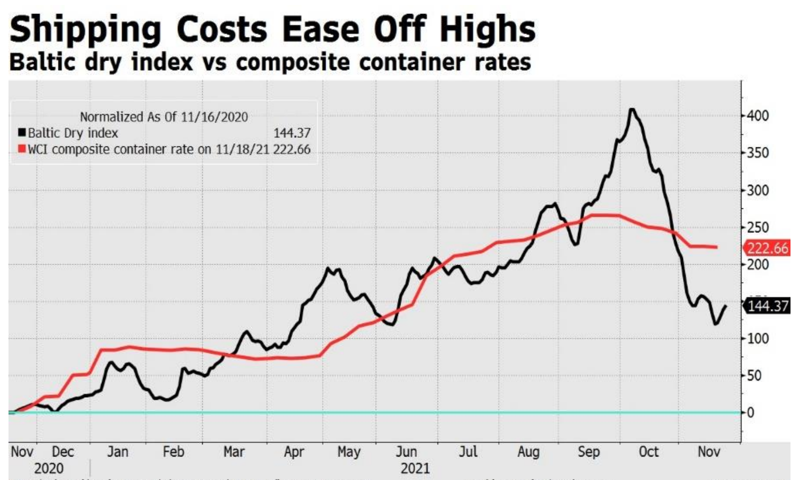


legal requirement starting February 1, 2022 (something that Germany is also considering). The new restrictions and vaccine mandates have been met with resistance across Europe. There were protests in Austria, Belgium, Denmark, Italy, Switzerland, Croatia and the Netherlands. The new wave of coronavirus cases has not escaped the United States though the impact is uneven. Currently, the Northeast and Midwest, which are entering the colder months, have seen the greatest increase in new cases. The U.S. is closing in on 49 million confirmed cases resulting in nearly 800,000 deaths. Mandates are restrictions are also restarting in parts of the U.S. as Erie County in Western New York has reinstituted mask mandates in public spaces with the potential for restrictions to go even further. This has the potential of significantly slowing down the global recovery.

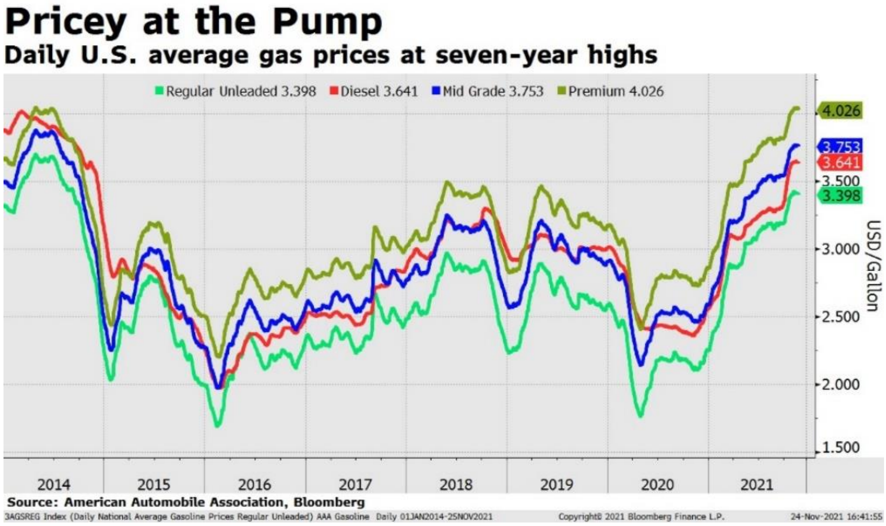


Before this latest news the U.S. was contending with issues beyond the virus. The most often discussed topic has been the continuing and accelerating inflation. The latest headline CPI data showed prices increased 6.2% from a year earlier – the highest since 1990. This was driven by items such as gasoline, car prices and travel but, after excluding volatile food and energy, core CPI and PCE (the Fed's preferred measure) still increased well beyond their target. In addition, the inflation sources were much more broadly based in this reading. While it is hard to predict how long the supply-driven transitory factors will continue to impact inflation the fact that the more cyclical factors (rents, wages, etc.) are impacting inflation could be a sign that it is going to last longer than

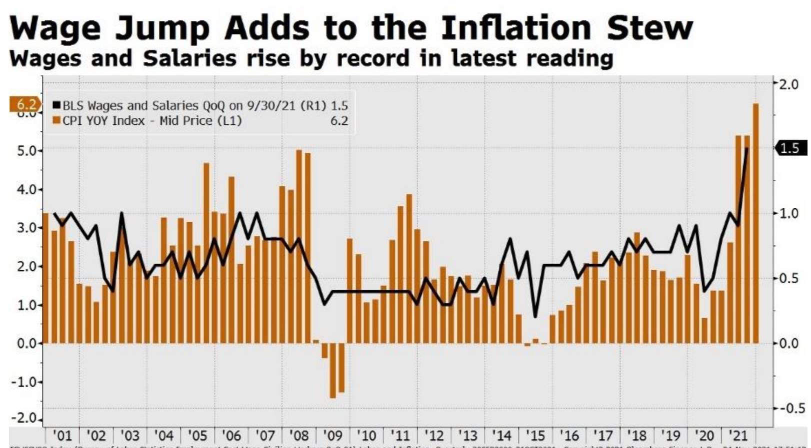




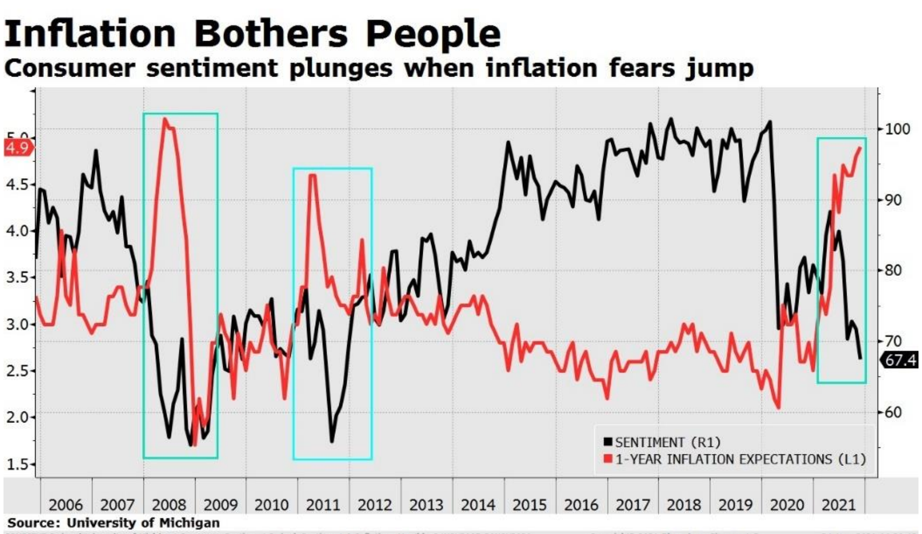
expected. Like a game of inflation "whack-a-mole" some inflationary pressures are subsiding (shipping costs) while others are picking up (fertilizer). These are elements of inflation that are generally behind the scenes for most consumers. Everyday items, such as gasoline, food and home energy costs are the ones that people experience directly.



The national average for a gallon of gasoline rose to $3.40 (a seven-year high) from $2.11 one year ago and home heating could be up from 6% to 46% this season. The pressure on administration led to an announcement of 50-million-barrel release of oil from the Strategic Petroleum Reserve, the nation's 600-million-barrel emergency oil stockpile meant to lessen the impact of disruptions to the oil supply chain. This will be the first time it will be used to simply bring down prices. It is estimated that the move will have the temporary effect of bringing gasoline prices down about $0.05-$0.10 per gallon in late December. In the end this release is mainly symbolic as the U.S. uses about 20.7 million barrels of oil per day and the additional 32 million barrels (18 million barrels were previously announced) being released in the coming months will eventually be replaced. The Biden administration also requested that the FTC investigate "illegal conduct" in the pricing of gasoline by major oil companies. This tactic has been tried by prior administrations and the FTC often comes up empty as the industry generally has too many actors that transform oil (which accounts for about half the cost of retail gasoline) into gasoline to collude.



The stickier side of inflation includes elements such as wages. The low participation rate in economy and the need for workers is creating a large increase in employment costs – just about as high as CPI on a percentage basis.



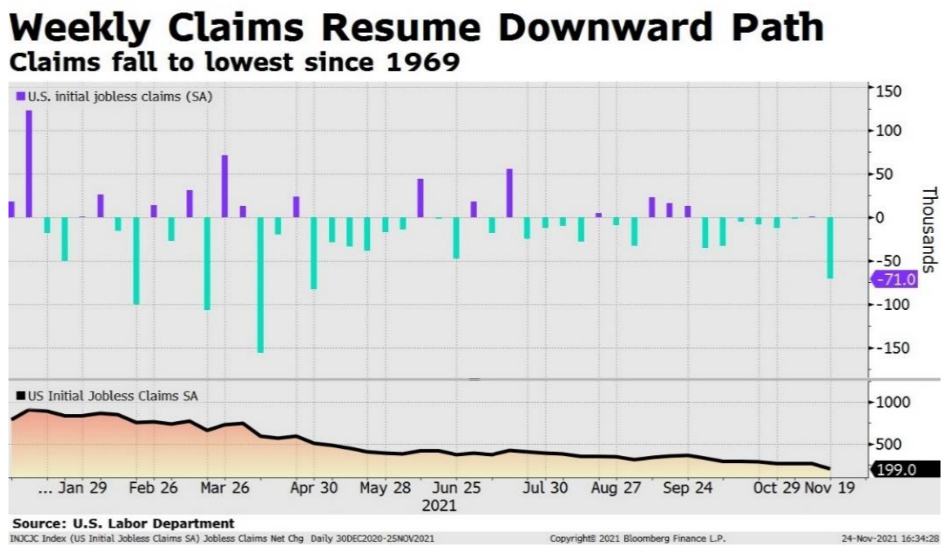
The result of this continued experience of inflation is that consumer sentiment begins to wane. The deleterious effect of inflation is that people begin to tighten their wallets and not spend as much since more of their income gets diverted to essentials and the price of other goods deters spending. In addition, renewed virus concerns, lock downs and mandates may have more negative psychological impact on consumers as well.

Inflation Expectations
Latin America has the highest inflation forecast for both 2021 and 2022

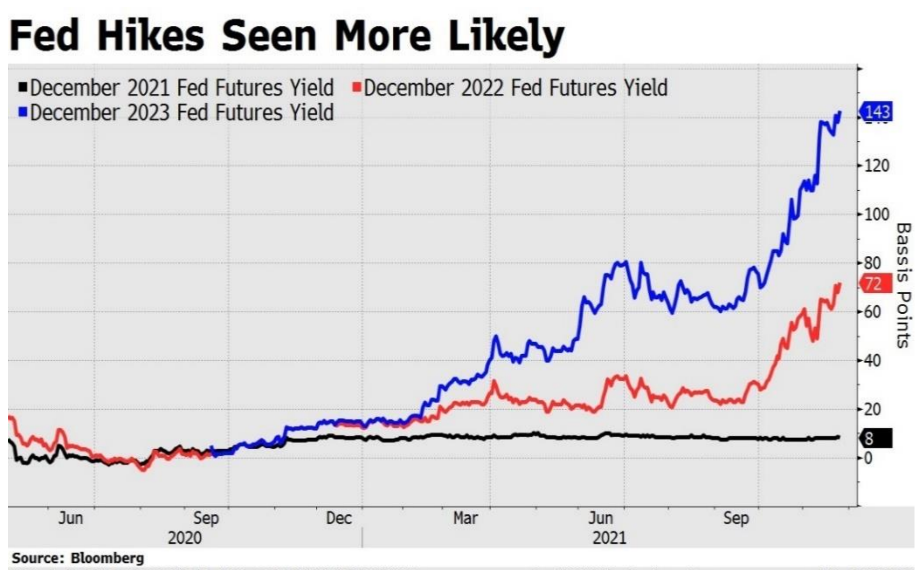
Region / Country	2021	2022
Latin America	**11.9%**	**10.4%**
Africa	10.6	9.5
EMEA	7.8	6.7
Asia Pacific	1.2	2.3
Eurozone	2.4	2.2
U.K.	2.4	3.5
U.S.	4.5	3.7
World	3.7	3.5

Source: Bloomberg
Note: Data based on Bloomberg surveys

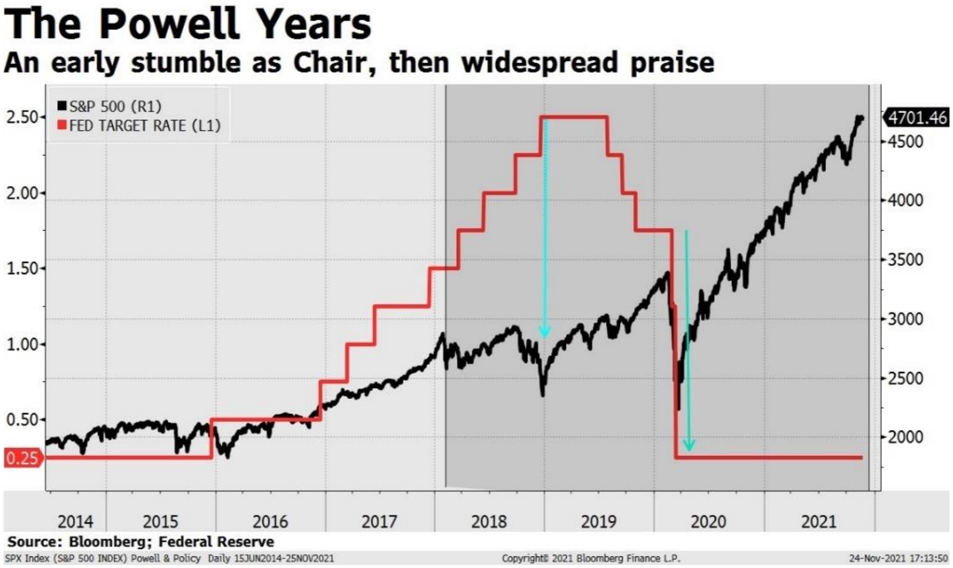
The table on the left shows that current and expected inflation is not just a U.S. phenomenon. Most of the world is expected to see inflation numbers in 2022 which will not be much different than 2021. The U.S. is expected to see some measure of relief, but inflation is expected to be lowest in the Eurozone at 2.2%. The world inflation expectation is 3.5% vs. 3.7% in 2021 and the emerging markets (Latin America, Africa and Asia) are expected to experience significant inflation.



The job situation in the U.S, has been a source of some good economic news recently. The latest data show that there were 531,000 jobs created last month and the initial jobless claims fell to 199,000 – the lowest reading since 1969. Unemployment has now fallen to 4.6% and it is attributable to more people taking jobs but, also the decline in number of people in the workforce which has dropped markedly.



The pressure that inflation is bringing, along with a recovering economy, is making it harder for the Federal Reserve to justify zero interest rates and the unusual accommodation in order to keep interest rates low. This prompted the Federal Reserve to announce the start of tapering in the month of November. The purchase of $120 billion of bonds each month to keep rates near zero will decrease $15 billion per month. This would bring an end to bond purchases in the middle of 2022 after which they would raise interest rates. Powell suggested the possibility that they could hasten the pace of tapering their purchases to $30 billion per month and the market, as well as Federal Reserve presidents, have been hinting at more rate increases in 2022. Markets are pricing in two rate hikes in 2022 and four by 2024 but, were still shocked by Powell's comments. Keep in mind that, as we have seen, the virus could change that course quickly.

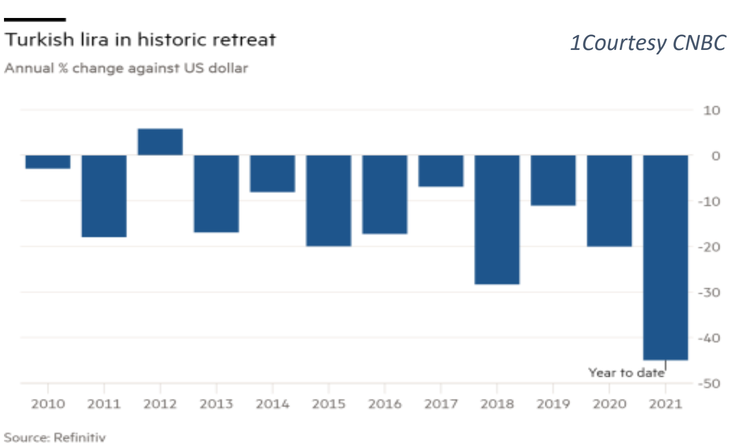


Speaking of the Federal Reserve, President Biden announced the reappointment of Jerome Powell as Fed Chairman for another term. This was a safe choice and his confirmation should be easy given that he was a Republican nominee and has so far successfully responded to the virus and steered the economy towards recovery. In addition, the consistency of the current Fed chair and direction creates more certainty and the markets reacted calmly as this removes a potential "unknown". This doesn't make everyone happy as some progressive legislators were not satisfied with Powell's bank regulation record and felt he was too soft. In order to appeal to both sides President Biden nominated Lael Brainard as Fed Vice-Chair (she was the other candidate for chair). This leaves Biden with three positions to appoint to the Federal Reserve Board of Governors, including Vice Chair of Supervision which has most direct authority over bank regulation.

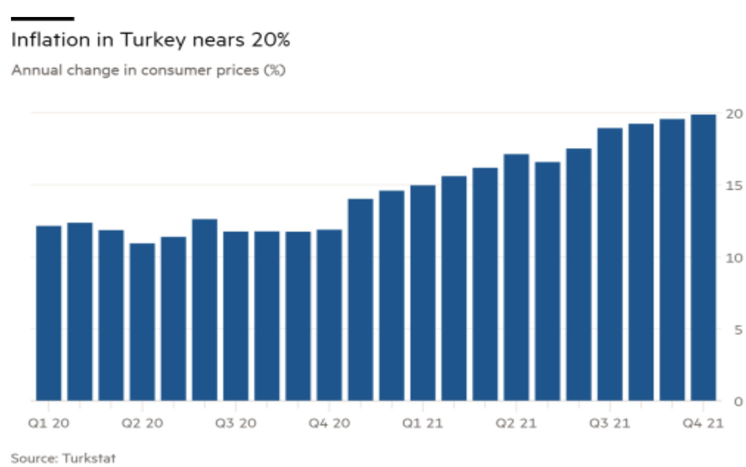
On the legislative front the bi-partisan Infrastructure bill made its way past the House and to President Biden where it was signed into law. The additional $517 billion of spending (on top of baseline spending) makes for almost $1.2 trillion dedicated to physical infrastructure over the next several years. Offsets amounted to about $183 billion so this may add about $350 billion to the deficit over the next several years. The House then turned its attention to the "Build Back Better" economic package. This will set up quite the scenario in the Senate as the House started with $1.64 trillion from the original $3.5 trillion proposal. The House added several new spending features before passing it and the CBO estimates that it will add about $367 billion to the deficit over 10 years. The Senate will debate it and changes are expected as moderate Democrats indicated they wanted no increase to the deficit. Any changes will require a revote in the House. While this is going on the Federal Debt Limit is back in the spotlight. In October there was a bi-partisan agreement to fund the government until December 3rd so there must be some agreement to fund the government before the U.S cannot pay its bills by mid-December.

Turning internationally, in addition to the virus, there are other developments worth watching. China is still defining the transition to "Common Prosperity" while wrestling with real estate development and debt issues.

In Turkey, President Recep Erdogan sparked a devaluation of the Lira to historic lows after he defended interest rate cuts in Turkey despite inflation of over 20% annually. This has the potential of economic crisis for the nation of 85 million people.

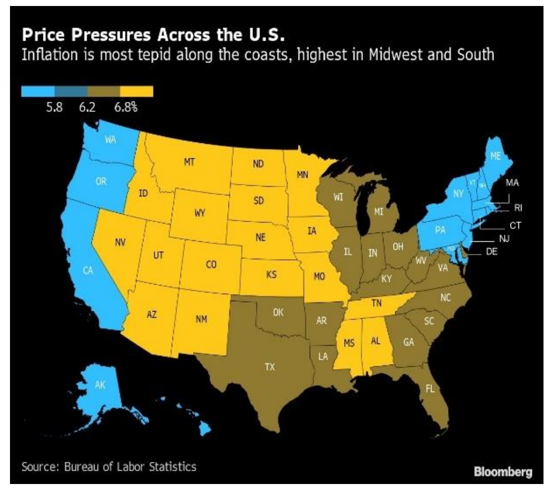


1Courtesy CNBC



Financial Markets

Financial markets went on quite the ride towards the end of the month. The developments with the Omicron variant and Powell's comments to Congress had the effect of whipsawing markets in the U.S. over the last few days. The yield curve reacted sharply by continuing to flatten. The flattening yield curve resulted from short maturity bond yields rising while longer-dated bond yields falling. This flattening can also be seen in the chart above which shows the difference between the 10-Year Treasury yield and the 2-Year Treasury yield and that difference is once again falling. Another significant influence on bond yields and rates is expected inflation. Currently, with inflation so high, bond yields are negative from a purchasing power standpoint. How negative depends a bit upon where you live in the U.S. as the inflation experience is quite different in separate parts of the country.



Equities also declined around the world in November. The S&P 500 ended down nearly 1% while midcap and small cap stocks were down 3.0% and 2.0% respectively. International equities fared worse with developed markets down almost 5.0% and emerging markets down about 3.5%. The virus makes the future even murkier with the potential for rising interest rates in the U.S coupled with the uncertain path of the virus caused by the new wave of Delta and the Omicron variant. One note in support of equities is that S&P 500 earnings are still expected to rise to $220 in 2022 and $235 in 2023 from an estimated $210 in 2021.

Should you have any questions please contact us.

Image sources: Bloomberg and CNBC unless otherwise noted

Buffalo Office

1114 Delaware Ave.

Buffalo, New York 14209

PHONE: 716-883-9595

Jamestown Office

214 West Fifth Street

Jamestown, New York 14701

PHONE: 716-484-2402