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All good things must come to an end. After seven consecutive months of gains for the broader equity markets, September–living up to its historical reputation as the lowest returning month–delivered losses. While the S&P 500 managed a small gain for the quarter, the September slide sent most other indices into the red for the third quarter.

A confluence of worries gripped the markets. Supply chain bottlenecks and stubborn inflationary pressures were the primary culprits, though consternation over Fed policy and budgetary decisions in Washington, D.C., compounded investor concerns. The silver lining of the quarter was impressive earnings reports from corporate America. Should this fundamental strength continue, the markets will be in good shape as the year ends and investors begin to ponder the prospects for 2022.

Immediate solutions to supply chain bottlenecks are proving elusive. As we opined last summer, it is highly difficult to restart supply chains after halting global economies. Supply chains are intricate and highly interconnected, vulnerable to any single weakness along the chain. In addition to the act of manufacturing, transporting both the raw materials necessary for production and the completed product are highly complex. Any disruption along the way, such as a regional economic shutdown, has the potential to derail the entire chain. Following the pandemic and the economic reopening, businesses are experiencing high demand for their goods and services. However, the supply of these products and services, including labor, has proven insufficient to meet this renewed demand. Should this imbalance continue, growth may decelerate. The globally integrated supply chain will eventually achieve equilibrium, but based on conversations with our portfolio companies, Riverbridge continues to assert that this process will take time.

Investors also continue to grapple with inflationary pressures. Many, including Fed Chairman Jerome Powell, initially felt that the inflationary uptick following the economic reopening would be temporary or transitory. As more data are reported, it appears likely that these inflationary pressures will persist. The labor market is extraordinarily tight as companies are struggling to find workers. In many cases, businesses are being forced to pay higher wages, which results in increased prices for the goods and services that they produce.

The Federal Reserve has indicated that it will begin to remove some of the stimulative pandemic-era policies in November. Furthermore, the Fed hinted that they may begin raising interest rates as early as next year should inflation remain persistent. A modest amount of inflation is healthy for the economy and the equity markets. The risk is that inflation rates rise to levels that threaten to derail economic growth and decrease corporate profit margins.

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From a fundamental standpoint, the Riverbridge portfolio companies continue to perform well. Most of our companies are less impacted by inflation and the supply chain disruption relative to the broader market. Furthermore, our portfolio companies are positioned to thrive in the new, post-pandemic economic normal. Thanks to their strategic market positions and internally financed growth, our portfolio companies have the flexibility and resilience necessary to adapt to the changing global markets.

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