Marketline June 2021

Stocks:

The market shifted in June. From a stance of anticipating the reopening and higher growth as the economy recovers, attention turned to expiration dates for various government programs and Congress' lack of progress on proposed infrastructure bills. Sentiment shifted rapidly from worries over fast growth, inflation, and higher rates – to the creeping belief that fiscal stimulus will wane while we must still contend with promised increases in interest rates and new Covid variants resulting in scattered lockdowns. Never mind that the brakes on growth won't show up for several months: the stock market's job is to look forward. These factors caused the Dow to close flat for the month and reined in the S&P at a 2.2% return. But growth and technology stocks surged, making up for lost time earlier this year. The Nasdaq rose 5.5%. Generally, when investors believe that economic growth is waning, stocks that offer substantial future promise even if they don't earn much today catch a strong bid.

Overseas was a reflection of the concern registered in the US: Canadian stocks and the Mexican Bolsa posted just 1.6% and 0.6%. In Europe, where the Delta virus variant is spreading rampantly and stock indices lack heavy tech exposure, the return was basically nil. Meanwhile the US dollar is surging, depressing performance from overseas investments even more.

All in all, the June shift in sentiment presages a more volatile time for stocks, as investors work out whether growth will continue or moderate. Upcoming earnings reports are critical. We have seen a preponderance of good numbers coming out in prior quarters, but now companies are struggling with higher labor costs, higher materials costs, and supply chains that simply cannot deliver. If earnings reports disappoint, expect investors to take stocks to the woodshed.

Bonds:

Remember the old dance song with the phrase, "do the twist"? That's what the bond market did last month. Short maturity interest rates – a few months to seven or so years – rose. But longer bonds fell in yield, a process we call "flattening". The fulcrum was right around the seven year area.

As we write this, the same process has brought longer interest rates down even more. If you are shopping for a mortgage, that is a good thing. If you need to reinvest bond money, that is a bad thing.

The current thirty year rate is just under 2%, down dramatically from the 2.35% of March. Since bond prices rise when rates fall, this has propelled bond portfolio values upward, particularly their corporate and municipal bond segments. As readers know, we become somewhat depressed when rates sink so far, and talk in this column turns to "bleak landscape" and "scraping the bottom of the barrel" as we search, often fruitlessly, for a decent bond. But this month despite the decline in rates, we found several interesting new names. These include Scott's Miracle Gro, Central Garden & Pet, Asbury Automotive, Denton TX, and several pieces in Illinois which is experiencing some ratings upgrades. Some of these involve taking a calculated credit risk. But Denton and a couple of the Illinois pieces offered great yields at a strong quality level. These bonds will arrive in select portfolios over the next few weeks.