PWM Weekly Observations

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Searching for Goldilocks

- **While we are currently at peak growth, there is no consensus about where we go from here. The bulls are getting bearish and vice versa.**
- **There is fear of growing too fast and incurring the wrath of the Fed with higher interest rates, which would pressure stocks. Likewise, there is fear of growing too slow due to Delta. Rates would stay low, but again, stocks would likely be pressured.**
- **The Goldilocks scenario is enough growth to keep the Fed from being too aggressive, but also enough to keep earnings on a solidly upward track.**

As independent advisors, we are able to access economic research from a wide variety of sources and this week really highlighted the confusion of the market seers. There is a massive tug of war between the growth we have been experiencing and the prospect of growing downward pressure on that growth due to tougher comparisons from last year, not to mention the spread of the Delta variant.

Morgan Stanley, in their report titled “Something has to Give”, Chief U.S. Equity Strategist Michael Wilson lays out a very concise summary of the peak growth/mid-cycle transition narrative and advises caution.

- The COVID-19 recession was deep, but it was swift, ending only two months after it started, according to the National Bureau of Economic Research. Massive monetary stimulus (from the Fed) and fiscal stimulus (from Congress) largely offset the economic loss and rapid vaccine development enabled a rapid return to growth. Likewise, the stock market also rebounded in record time. An economic cycle that normally takes years was compressed into a few months.

- The second quarter delivered peak growth because the economy sunk so low in Q2 last year. From here, growth will slow down due to tougher comparisons with a year ago. Economists call this the ‘midcycle transition’ and it is usually characterized by:

1. Economic and earnings growth peaks with slower growth going forward.
2. Equity markets narrow, meaning the broad indexes rely on fewer and fewer stocks to maintain momentum.
3. Leadership moves away from early cycle companies, like homebuilders, semiconductors, retailers and transports.

- The last step, which we have yet to reach, is the Federal Reserve tightening monetary policy, implying that interest rates rise and equity valuations fall.

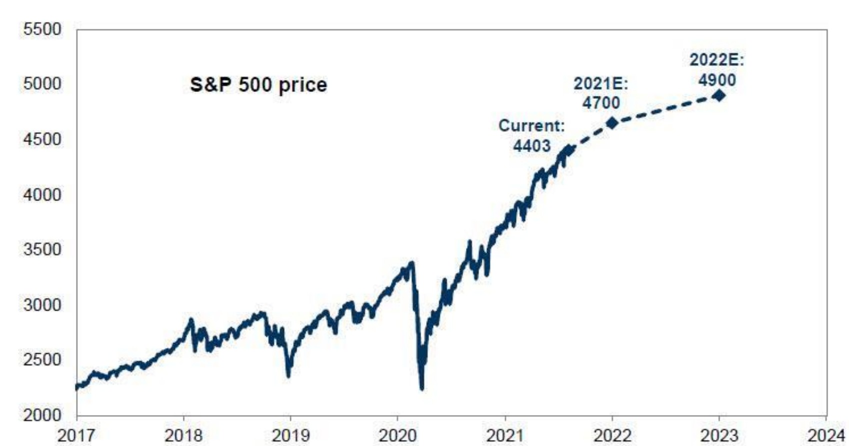
- Wilson's conclusion is that interest rates at current levels are not compatible with a booming economy and earnings growth. Something has to give, and the equity market is likely to discount it soon via lower valuations and he recommends a more conservative approach.

By contrast, the previously cautious David Kostin of Goldman Sachs turned more bullish and upgraded his year-end price target for the S&P 500 index from 4400 to 4700, one of the highest estimates on the Street.

Kostin has previously been a bear on interest rates (i.e., expected rates to move higher) but the recent decline in rates has changed his mind with a base assumption that the 10-year treasury rate gradually increases to 1.6% at year-end (vs. 1.29% as this is written and his prior 1.9% forecast).

Kostin also raised his 2021 and 2022 earnings forecasts for the S&P 500. The 2021 estimate increased 7% to $207 from $193 and the 2022 estimate climbed 5% from $202 to $212. The implication is that he now believes in continued earnings momentum and therefore higher stock prices. He is clearly in the 'growth continues' camp.

Exhibit 1: GS S&P 500 year-end price targets



Source: Goldman Sachs Global Investment Research

Exhibit 2: Summary of our top-down S&P 500 forecasts

	ex. Financials and Utilities		Adjusted EPS		Valuation			
	Sales growth	Profit margin	Level	Growth	P/E (NTM)	Dividend yield	Year-end price	Total return
2019	4.7 %	10.7 %	$165	1 %	22.7x	2.3%	3231	31 %
2020	(3.1)	9.7	142	(13)	18.1	1.8	3756	18
2021E	15.7	12.1	207	45	22.1	1.6	4700	27
2022E	7.8	11.9	212	2	21.7	1.4	4900	6
2023E	4.9	12.1	226	6				

Source: FactSet, Goldman Sachs Global Investment Research

From our point of view, we think President Biden got it right when he said this is a pandemic of the unvaccinated. The problem is that the bulk of our supply chains are in Asia and unvaccinated. China has recently initiated the most stringent lockdowns since the start of the COVID crisis and initial anecdotal evidence of a slowing Chinese economy is appearing. Thailand, Vietnam and Japan are also experiencing upticks in infections. The risk is that these infection trends hold and create additional supply chain disruptions. That could not only put a crimp on economic growth, it could also push inflation higher, despite the infection progress we have made in the U.S.

Despite the seemingly inexorable move upward in markets, it's a confusing time for investors. Valuations are high, there is plenty that can 'go wrong' and plenty that can 'go right'. Rather than bet as traders would, we suggest that sticking with the plan is the right approach.

What We're Reading

U.S. plans to give extra COVID-19 shots to at-risk Americans

Senate to try to finish $1 trillion infrastructure bill on Saturday

Jobs report will cause big shift in stock market leaders

Big Tech stocks lag following Friday's strong jobs report - Here's why ***(3 Min Video)***

Just-in-Time Manufacturing? Not With Rickety U.S. Infrastructure

Yesterday's Wars Didn't Prepare the Pentagon for Tomorrow's China

Israeli scientist says COVID-19 could be treated for under $1/day

Visualizing the 4,000 Year History of Global Power

Biden seeks to make half of new U.S. auto fleet electric by 2030

Toyota warns rivals' gasoline engine phase-out goals must overcome challenges

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Markets This Week

The stock market continued to climb a wall of worry with broad indexes all sharply higher. Along sectors, only Consumer Staples was the loser. A strong jobs report Friday supported the belief that corporate earnings will remain strong. Bonds reacted in the opposite way. After a recent rally, interest rates began to head north again, especially on Friday, as the strong jobs report was interpreted as an indication that the Fed's hand could be getting forced to raise rates sooner rather than later. Gold and commodities declined on a stronger dollar.

US Equities	1 week	YTD	Fixed Income	1 week	YTD	Sector Breakdown	1 week	YTD
S&P 500 (SPY)	0.91%	18.74%	20+ Yr. Treasuries (TLT)	-1.04%	-5.56%	Consumer Disc. (XLY)	0.32%	12.93%
Dow (DIA)	0.75%	15.92%	Barclays US Aggregate (AGG)	-0.43%	-1.14%	Info. Technology (XLK)	0.95%	19.66%
NASDAQ (QQQ)	0.95%	17.60%	Intermediate Municipal (MUB)	0.02%	1.13%	Financials (XLF)	3.67%	29.52%
Russell 1000 Growth (IWF)	0.91%	17.75%	US Corporate Bonds (LQD)	-0.82%	-1.36%	Health Care (XLV)	0.60%	18.05%
Russell 1000 Value (IWD)	0.86%	18.92%	Barclays US High Yield (HYG)	-0.21%	2.17%	Utilities (XLU)	2.24%	9.21%
Vanguard Mid-Cap (VO)	0.92%	18.06%				Industrials (XLI)	0.17%	17.66%
Vanguard Small-Cap (VB)	0.73%	15.44%				Energy (XLE)	0.24%	33.38%
						Materials (XLB)	0.14%	17.24%
International Equities	1 week	YTD	Commodities	1 week	YTD	Consumer Staples (XLP)	-0.80%	6.44%
MSCI EAFE (EFA)	1.03%	11.57%	Commodities (PDBC)	-2.45%	30.21%	Comm. Services (XLC)	0.51%	23.17%
MSCI Emerging (EEM)	0.66%	0.97%	Gold (GLD)	-3.05%	-7.69%	REITS (VNQ)	0.58%	27.52%
						Homebuilders (XHB)	0.49%	31.85%

The table above is an analysis of the weekly and year to date returns of various markets/sectors that we follow (More RED = worse performing markets/sectors; More GREEN = best performing markets/sectors). Source: IEX Trading & PWM Research.

Retirement Planning:

Deciding between a traditional or a Roth 401(k)? Here's what to consider

The main, and most well-known, difference between a traditional 401(k) and a Roth 401(k) is the time at which your money is taxed, but there are other factors to consider as well.

Estate Planning:

Estate planning for rising interest rates

In a rising interest rate environment, you may want to lock in lower interest rates now while preparing to capitalize on higher interest rates in the future.

Tax Planning:

12 Ways to Save on Taxes Through Life's Transitions

There are ways to save on your taxes through life's transitions. Here are 12 tax tips to help you save through major life events.

Health:

[Erectile Dysfunction Risk 6 Times Higher in Men With COVID]

The preliminary numbers also indicated that having ED also increased men's susceptibility to SARS-CoV-2 infection.

Entrepreneur:

[Want to Create a Great Employee Environment?]

Organizations need to think about how they're going to make the new office attractive, engaging and a place where their employees want to return.