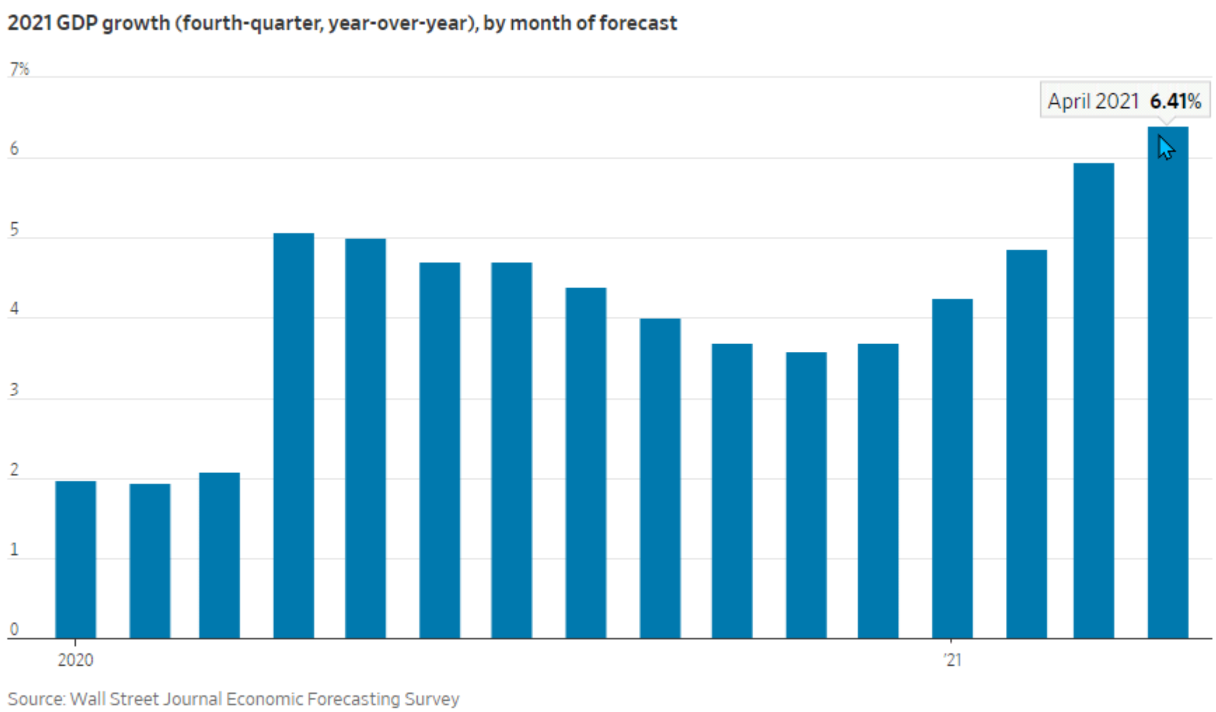
2021 June Market Outlook

We are in a bull market and most sectors are participating. There is a strong economic backdrop for the bull market that is explained below in the Bullish Case section. There are some concerns and headwinds that are discussed in the Bearish Case section below.

A new earning's season will be starting soon and earnings growth is expected to be about 60%. Part of the reason why earnings will be so good is the comparisons to last year's earnings were bad. Currently, the markets are rallying because of the anticipated good earnings reports and progress on an infrastructure bill.

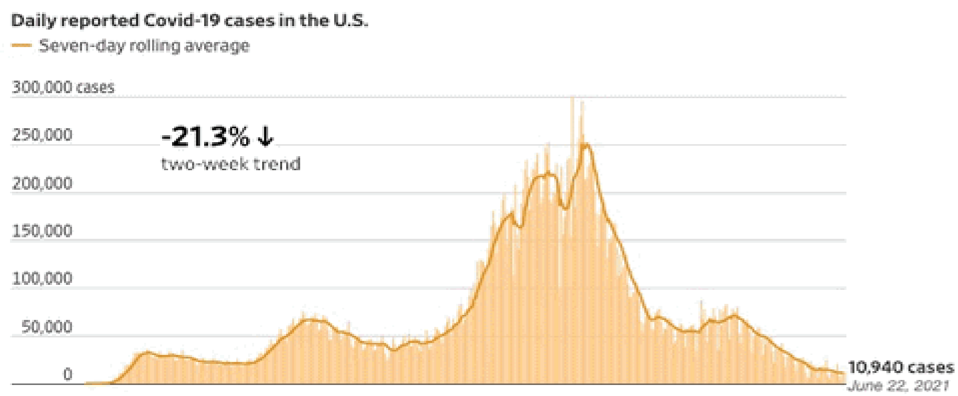
Bullish Case

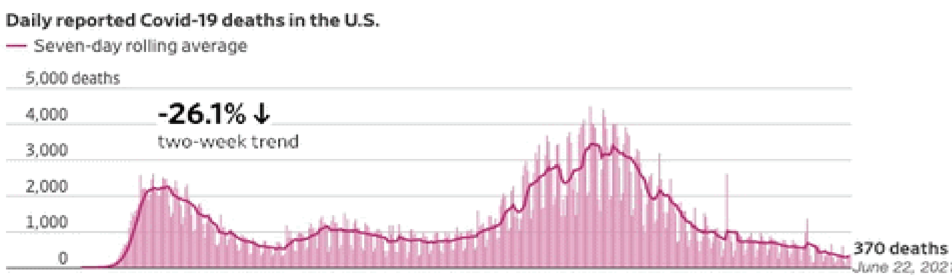
- Thanks to trillions of dollars of aid, support, stimulus, and liquidity from the Fed and lawmakers we are having a strong economic start to our new economic cycle. All the cash citizens and businesses have is leading to strong spending.



For the last 10 years, economic growth was slightly above 2%. Growth is now above 6% and is expected to stay strong this year and next. Admittedly this type of growth is not sustainable for a $20 trillion economy. Most economists forecasted that the economy would start to recover this summer, but the recovery has started and is strong. Progress with the health crisis is another reason for the strong recovery.

- Strong vaccination plans and efforts in the U.S. are helping the economy open up and are helping with a strong recovery.

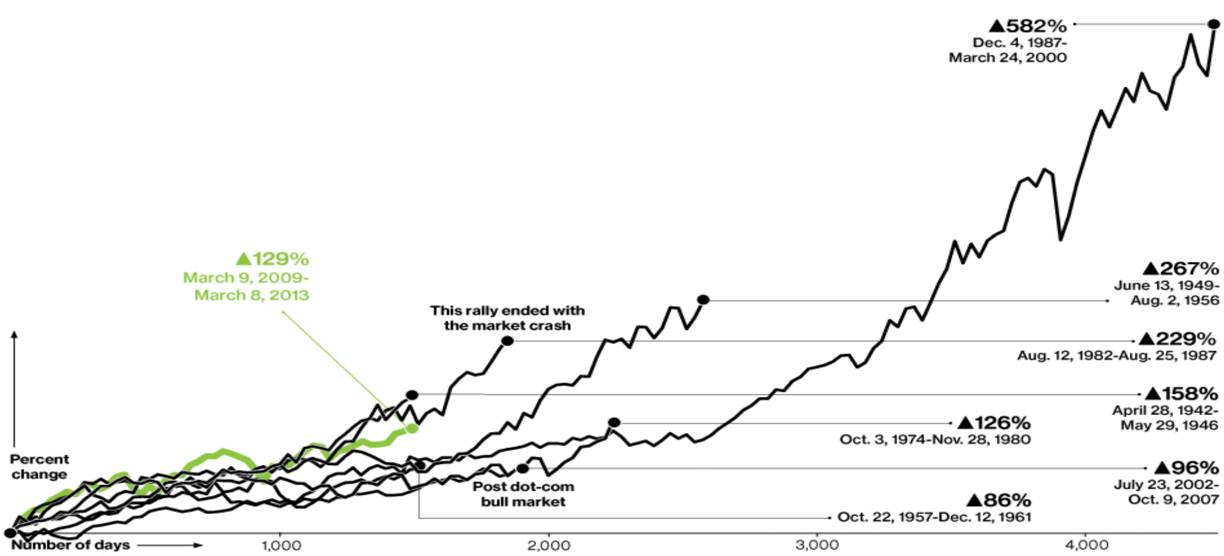




Source: John Hopkins, Center for Disease Control and Prevention

Infections and deaths have come down dramatically. The much improved covid trend is helping open up the economy.

- We are in a new economic and market cycle that will probably last at least five years (the average length of bull markets). Investors need to be invested at the start of an economic and market cycle. Below is a chart that shows the length and returns of each bull market going back to 1942.



Source: BusinessWeek

The horizontal axis shows the period of each bull market and the vertical axis shows the return of each bull market. Briefly, most bull markets last about 5 years, and most economic cycles last about the same.

The average gain for a bull market cycle is about 160%. From the market trough of last year, the market is up about 95%, so there is probably more upside in this new bull market. Most of the gains in a bull market are made in the first few years.

Last year we began investing and by the start of this year, we were close to 90% invested. We plan to stay invested the rest of this bull market cycle.

- Earnings estimates keep rising. Last year we were in a deep recession and earnings fell. Earnings comparison for this year compared to last year will show strong improvement. Earnings for the 2^{nd} quarter of 2021 are expected to increase about 60% over the 2020 2^{nd} quarter. See valuation section.

- The Fed has stated several times that they will do all they can to help the economy, especially those being left behind in terms of employment. The Fed has the economy and investors' back.

- Low-interest rates have allowed some homeowners to refinance their homes and the extra cash is spurring spending helping the economy. Keeping interest rates low also helps businesses finance long-term and big-ticket projects.

- TINA – **T**here **I**s **N**o **A**lternative to stocks. Bond yields are low and there is capital loss risk if rates continue to rise. See the Bearish section below and the bullet points about interest rates and inflation.

- Financial Planners, 401ks are not selling. I've written many times about these two participants of the market and both control trillions of dollars and they normally don't sell but rebalance. This is a fairly new phenomenon that I've monitored for about the last five years.

- Another behavior of market participants has been that they consistently buy on pullbacks.

  Both phenomenons (key participants don't sell and participants buy on pullbacks) have kept the markets resilient compared to past market cycles. This is true despite the many headwinds (health and financial crisis, trade wars, conflicts with China, fears of rising inflation, and interest rates) the markets have faced.

  If these trends continue, we should feel relatively comfortable at the start of this economic and market cycle.

  See Technical, Price Analysis section.

- Markets have been making new highs, this can continue. I’ve written about the new highs phenomenon several times. If you would like explanations of new highs and why they can continue, email me.

- The market believes there will be an infrastructure bill helping the economy, earnings growth, and labor markets.

Bearish Case

- Progress with the pandemic, global health crisis is a key to a global economic recovery. The “delta” variant is new and is expected to be the dominant virus in the world and U.S. Unfortunately the “delta” variant is highly contagious and could prolong the global health and economic crisis, especially for poorer countries. The U.S. has made excellent progress, but the rest of the world is way behind in vaccinations and opening up their economies.

- Most markets are overvalued. See valuation section.

- Rising inflation and interest rates are a major concern for investors and analysts. High inflation and interest rates are bad for the economy and markets. Most economists, analysts believe the current inflation trend is transitory. I wrote about inflation in last month’s Economic Update. In the report, I make the case for both sustained and transitory inflation. I tend to agree with the transitory case. If you would like to receive this report, email me.

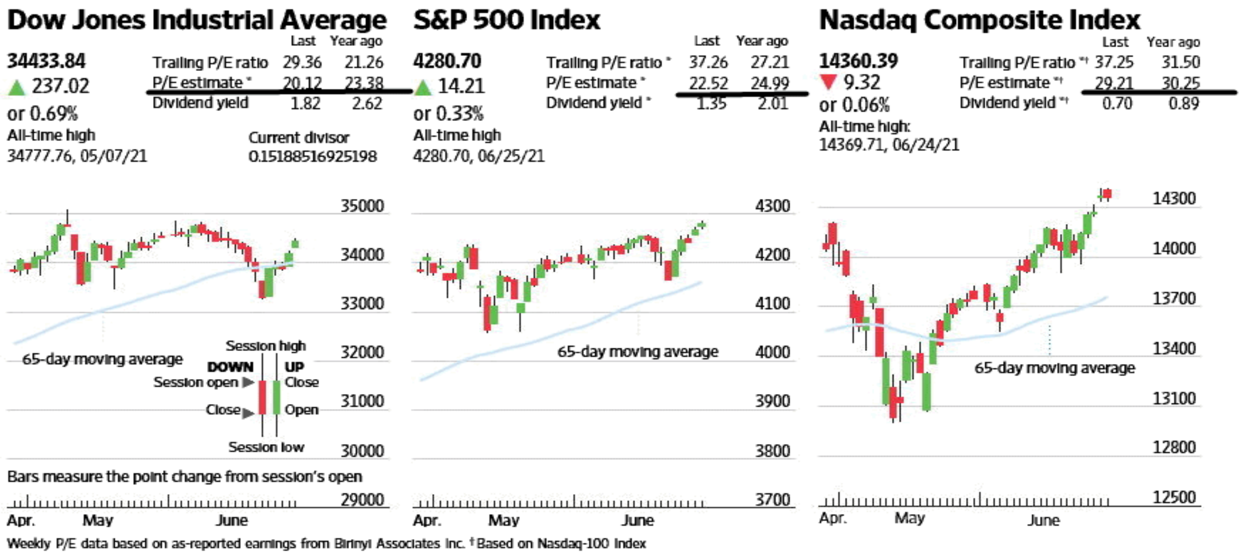
- In the last market cycle, the supply of stock was falling helping stock prices. This trend is reversing because of the many IPOs that have been issued last and this year. The tailwind of a shrinking supply of stock will be behind us.

- This year there has been a rotation between growth and value, and this is making the markets volatile and uncertain. I’m working on a special report on growth versus value

- High debt at national, local, state levels, with corporations and many families could be headwinds later in this economic cycle.

Valuations

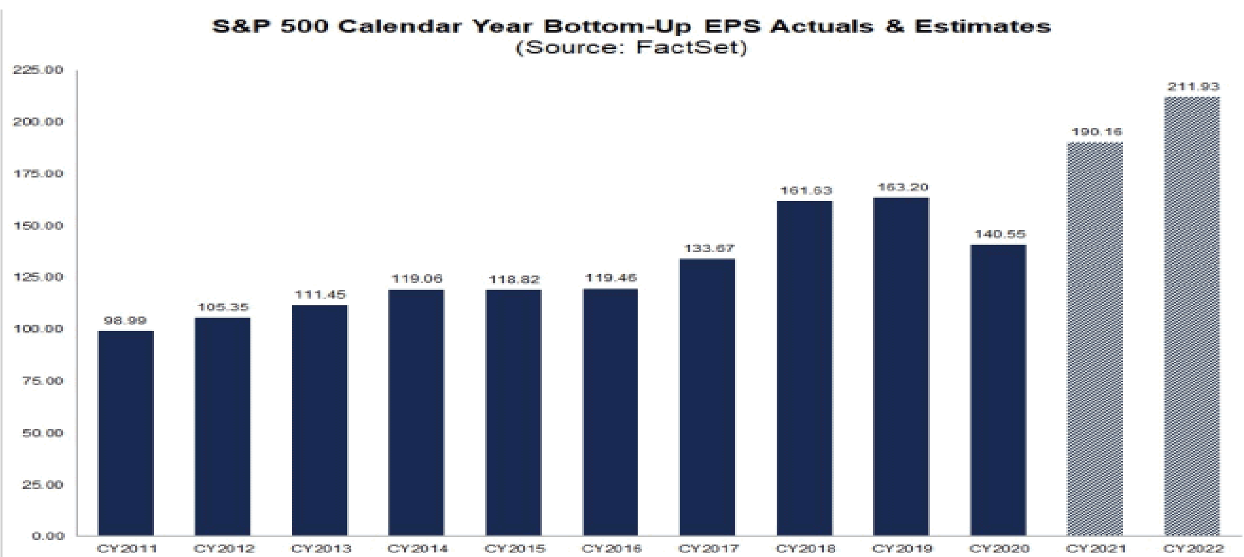
In past updates, I’ve shown long-term charts that show the average P/E ratio for the markets is about 16. Below is an image that shows the current P/Es for the major markets:



Source: WSJ

P/Es for the major markets are substantially higher than the historical average. If you do your homework, stock bargains can be found

Below are actual and forecasted earnings for the S & P:



Last year earnings for the S&P were down about 14%, but the index was up about 16%. Earnings for 2021 are expected to be up around 35%, and next year's earnings are forecasted to increase by about 11.4%. These estimates change all the time. I will provide updates if I see major changes.

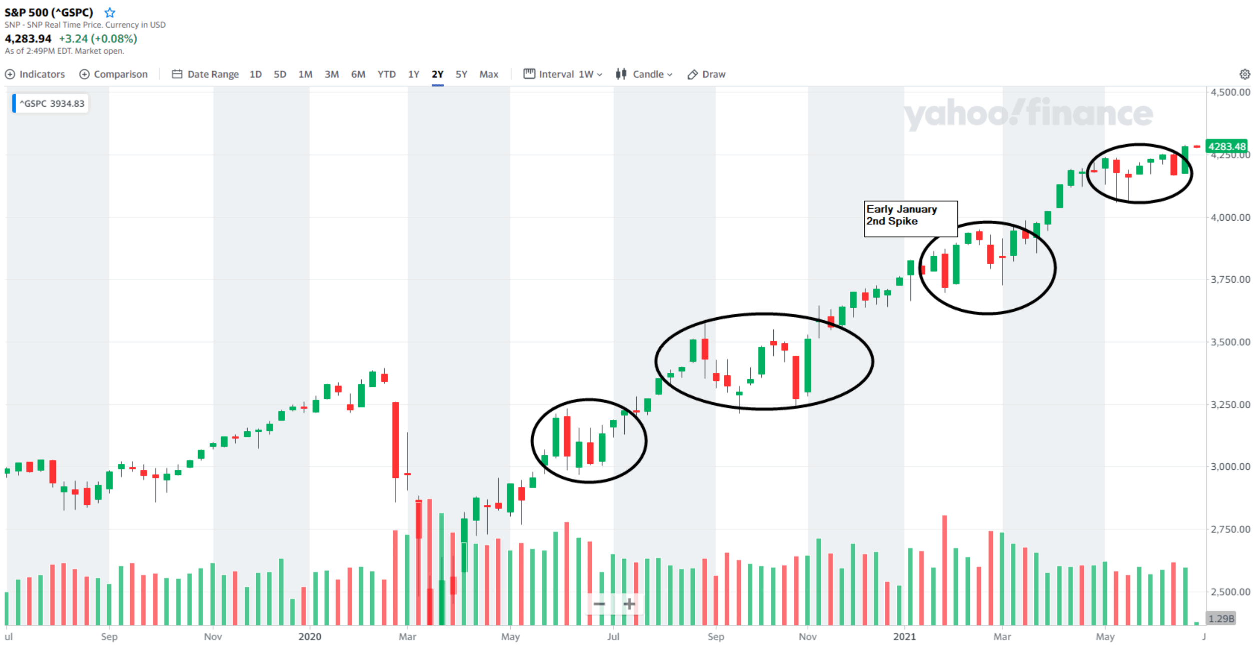
If we use the P/E historical average the S & P should be about 3,376 (212 earnings estimate times 16 P/E). If we use a 20 multiple then the S & P could be worth about 4,240. Currently, the S & P is around 4,280.

Because we're at the start of a new market cycle, companies/stocks can grow into their valuations.

When markets/stocks are overvalued, price analysis can be more helpful.

Technical/Price Analysis

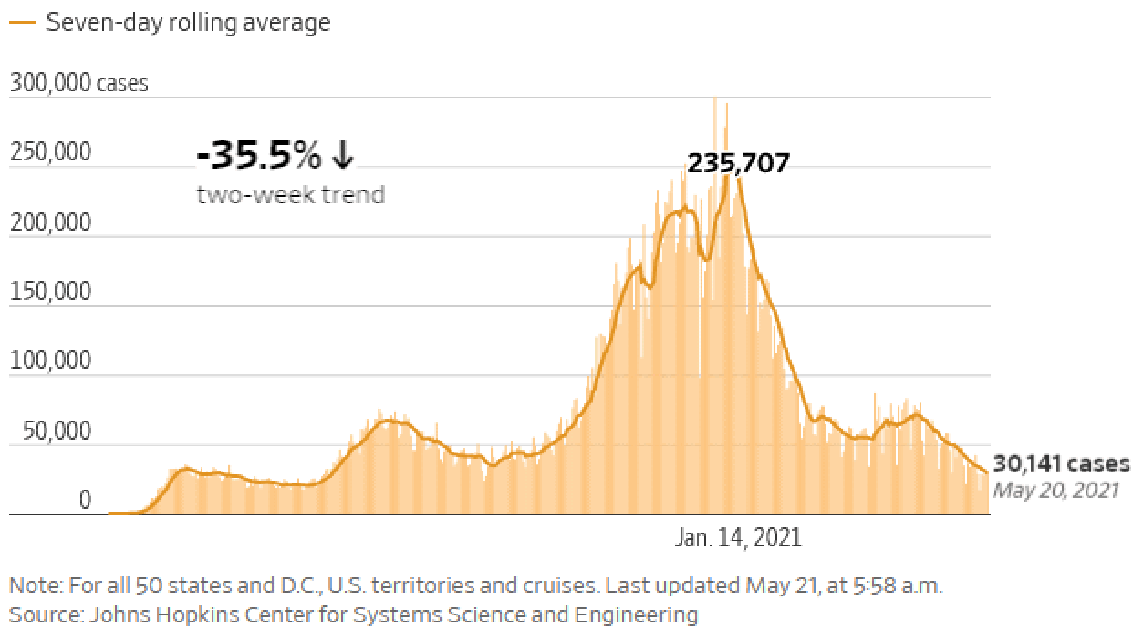
One of the factors for my bullishness is that bad news is met with little selling and participants buy these dips:



The pandemic has brought lots of bad news. Even though the markets collapsed and entered a bear market all the relief and support from the government helped the markets recover quickly. Also, some participants did not sell.

The current pattern is bullish. In a bull market, it is normal for prices to advance, then prices consolidate. After the consolidation, prices resume the bullish trend. Since the bottom, the market is on its fourth consolidation.

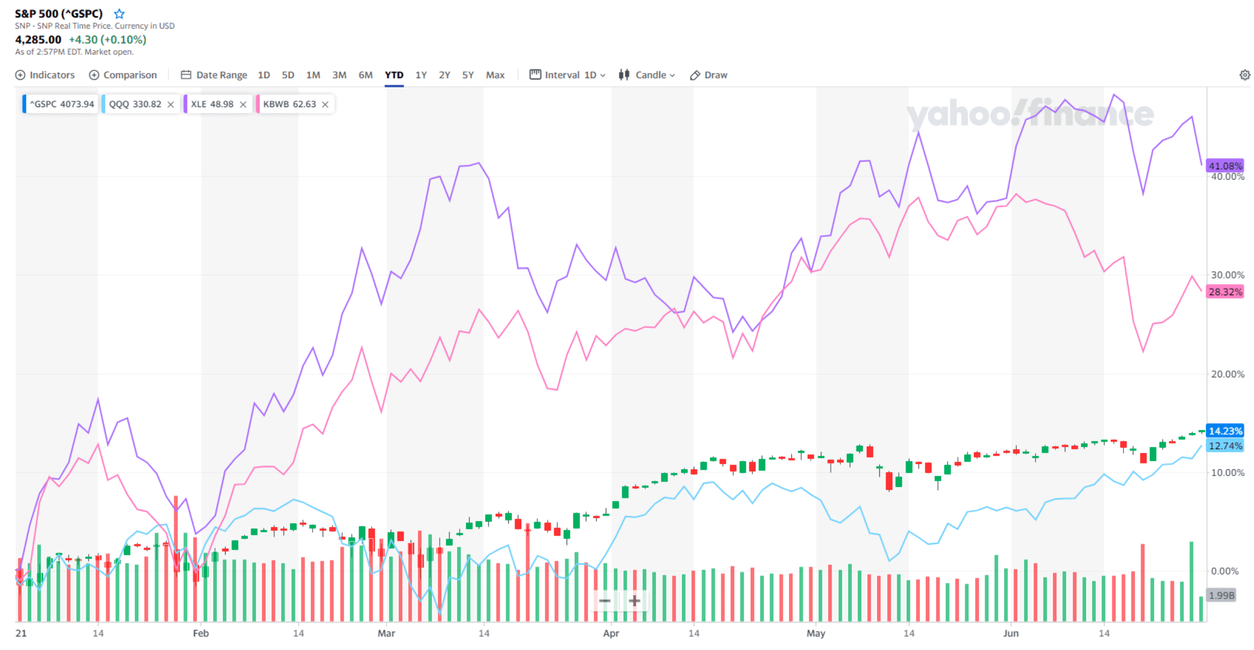
The second wave of infections early this year was very bad news as infections and deaths spiked:



During the spike, the S & P only declined 4.5%, and participants bought the decline, pullback. The particular period is the third circled period with text in the S & P chart above.

Last year we were in a recession and a bear market for many stocks. Technology growth stocks did very well last year as it was one of the few places that were growing and stock prices more than reflected the growth. Because growth was so rare last year, investors piled into technology growth stocks. I'm working on a special report on the overvalued, over-owned technology stocks.

This year value stocks like energy (purple trendline) and financial stocks (pink trendlines) have the best returns:



For the last few months, value stocks lost their momentum and have essentially traded sideways, but their gains remain substantial. The S & P and QQQ's key stocks are heavily weighted toward technology growth stocks. These two indexes struggled at the start of the year but starting rallying in mid-May. We can see in the chart that as the value stocks stalled, the S & P and QQQs have rallied.

Psychology of the Market

The market and many consumers are acting like the health crisis is close to the end.

Even though last year the economic and pandemic news was awful, the markets rallied strongly. This year the U.S. pandemic and economic news are much better, but the market is obsessed with inflation and interest rates. I analyzed the prospects for inflation in last month's Economic Update, and I basically agree with the Fed that inflation will probably be transitory.

The other focus of the markets is the question, should investors invest in growth or value? Again, I will issue a special report on the growth stock leaders. My answer, we are at the start of a new economic and cycle, and investors should invest in both. Your age and risk temperament will help determine the weightings for your portfolio.

Summary and Conclusion

- Most investors and consumers in the U.S. are acting like the health crisis is over. But, the delta variant could prolong the global economic and health crisis.

- We are in a new economic and market cycle and investors should be close to fully invested.

- We are having some inflation. Will it be persistent or transitory? No one can predict the future, so we must keep an eye on the Fed, inflation and, the credit markets/interest rates.

- Last year the markets were able to overlook the health and economic crisis. This year the markets are focused on inflation, interest rates, and value versus growth.

  To me, value versus growth is a silly argument. Growth investors and value investors are very different and they will stick to what they need from their investments and what they know and feel comfortable with. Most investors should have both in their portfolios.

- Analysts and investors are expecting strong economic and earnings growth for 2021, 2022.

- Because the markets have been overvalued for several years, technical/price analysis could be more helpful in making investment, trading decisions. The markets are seeing new highs. I have written about new highs many times- once new highs are made, new highs can continue to be made because sellers/supply diminish.