Dreher Investment Services, Inc.
Economic Outlook: 2nd Quarter 2021 July 7, 2021

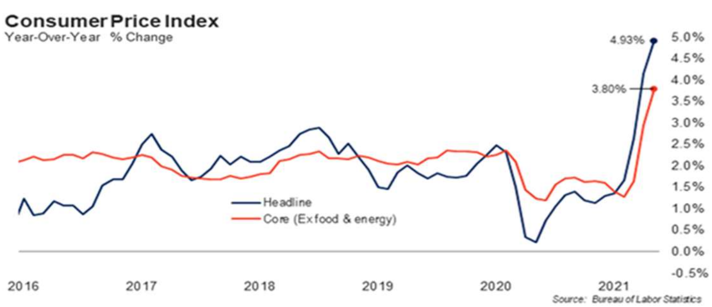
Market Review: 2Q-21

Equity markets in the 2nd quarter continued their rapid ascent, with the S&P 500 recording a **<u>+8.64%</u>** return. The index has now returned **<u>+14.41%</u>** YTD, **<u>+37.92%</u>** over the last year. This of course is coming off of the dismal 20% retraction we saw in March of 2020. It is fair to say that the markets have eliminated concern of a double dip recession and have priced in the start of the next expansion.

The 10-Year US Treasury Note decreased **<u>-0.30%</u>** in the 2nd quarter moving from **<u>1.74%</u>** to **<u>1.44%</u>**. Retail investors once again started buying bonds with a renewed acceptance that the Fed won't be raising rates for the foreseeable future.

Inflation

Driven by pent up demand and supply chain breakdowns, inflation has risen to levels not seen in some time. The month of May saw core inflation rise **<u>+0.7%</u>**, bringing the yearly increase to **<u>3.80%</u>**. Most analysts share the Fed's belief that the short-term inflation boost is in large part due to several sectors reflating to pre-pandemic levels coupled with global Covid-19 logistical issues. At this time analysts don't view inflation spikes as a problematic trend and expect a return to the sub 2% norm.



Market Indices

Index	2Q-21	1Q-21	1-Year
S&P 500	8.64%	5.77%	37.92%
Dow Jones Industrial	4.61%	7.76%	34.07%
Nasdaq Composite	9.49%	2.78%	42.83%

Economic Indicators

Indicator	2Q-21	1Q-21	1-Year
U.S. GDP	~7.8%	6.4%	~21.8%
Non-Farm Payrolls	1.70M	1.55M	7.92M
Unemployment Rate	5.9%	6.0%	11.1%
Headline Inflation	~1.9%	1.3%	~5.7%
Core Inflation	~2.0%	0.7%	~4.3%
Corporate Earnings Y/Y	~63.6%	52.5%	-
Corporate Revenues Y/Y	~19.6%	10.9%	-
Federal Funds Upper Limit	0.25%	0.25%	0.25%

~ Denotes Future Estimate

The Federal Reserve

As we transition out of the COVID-19 induced recession of 2020, the Federal Reserve will be under immense pressure from all sides. Throughout 2020, this Fed showed it is much more proactive than Feds in the past. Through quantitative easing measures, they were very instrumental in helping limit the economic damage caused by the pandemic. As we begin the next expansion, continued fiscal stimulus is not likely and monetary policy will become a pivotal element in the strength of this economic cycle.

With a surplus of stimulus cash and prolonged low interest rates, inflation and other key economic indicators have risen significantly over the past year. The Fed has calmed investors by confirming its current dovish stance, repeatedly stating its belief that current signals are "transitory," leaving the Federal Funds Rate near zero.

If inflation continues to be elevated and employment numbers start to return to what the Fed considers "full employment," we will see how committed the Fed truly is to their patient approach.

Strategic Market Outlook

The U.S. equity markets set all-time highs multiple times during the 2nd quarter, building on robust 1st quarter gains. Markets are now poised to leave the economic recovery stage and enter into the next expansion. Companies will now focus on transitioning to a post-pandemic environment. ***<u>Volatility can be expected in the short-term and will continue to be used as buying opportunities to establish long-term positions.</u>***

U.S. fixed income levels decreased by almost 20% during the quarter, with the <u>10-Year U.S. T-Note</u> finishing at **<u>1.44%</u>**. This decrease can be attributed to renewed demand after an acceptance that the Fed is not going to combat short-term inflation spikes by raising the Federal Funds Rate. ***<u>At current levels, duration will be limited on any fixed income purchases.</u>***

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