Summary

Economic data for the week included a pullback in existing home sales, while new home sales, the index of leading economic indicators, and jobless claims all improved.

U.S. equity markets were mixed to lower last week, but outperformed developed markets, while emerging markets ended with a small gain. Bonds were little changed, in keeping with minimal changes in interest rates. Commodities continued a string of gains, with agricultural commodities leading the way, as oil fell.

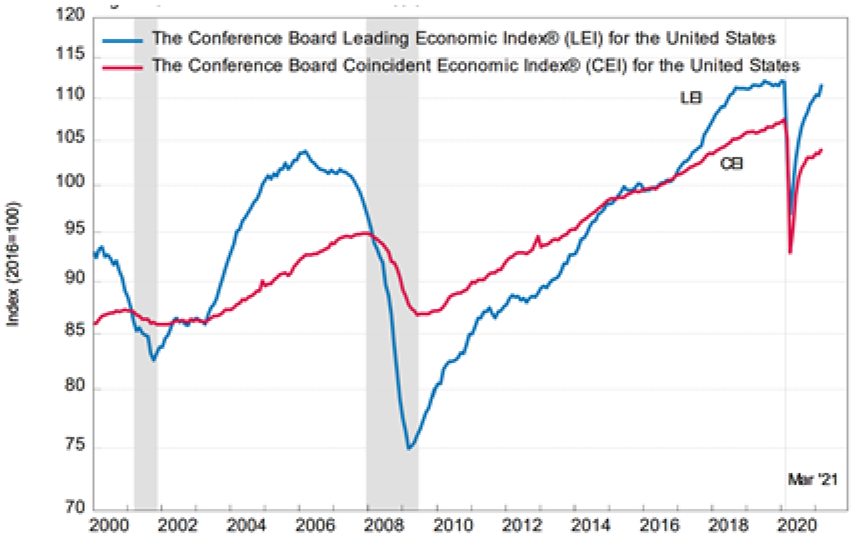
Economic Notes

(-) **Existing home sales** for March fell by -3.7% in March to a seasonally-adjusted rate of 6.01 mil., a deeper decline than the -1.8% forecast. This was the lowest level since last summer, and continued a string of monthly declines. During the month, single-family led the index downward, by falling -4%, which was slightly offset by a 1% increase in condos/co-ops. Overall sales fell in every region, led by the West, down -8%, while the Northeast only declined by a percent.

Single-family home sales are still up 10% on a year-over-year basis, though, and up 5% from the period right before Covid hit. Mainly, it appears that lack of inventory is weighing on transaction activity (inventories are down nearly -30% from a year ago). Additionally, demand is down from the rush to move last summer, during the pandemic's peak period of movers seeking more space and distance from cities, higher housing prices, and recent higher rates and still-not-loose lending standards. The inventory problem is seen by the 2.1 months supply number, as well as an average listing period of now under 20 days. The median existing home price rose 17% over the past year to $329,100.

(+) **New home sales** in March, on the other hand, rebounded by 20.7% to a seasonally-adjusted rate of 1.021 mil. units, and included a positive revision for the prior month. This surpassed expectations calling for a 14.2% gain, and reached the highest level since 2006, near the peak of the mid-2000's housing bubble. A recovery from February's winter storm slowdowns appeared to be the primary catalyst behind the move. The South achieved the strongest monthly gains, up 200k, while the West was the only region experiencing a decline in sales for the month. Months supply of new homes fell nearly a month to 3.6, while the median price of new homes was up 0.8% from a year ago at $330,800.

(+) The Conference Board Index of **Leading Economic Indicators** rose 1.3% in March, which was a continuation but also an acceleration in growth compared to the prior two months. All ten indicators showed gains for the month, led by jobless claims, new manufacturing orders, and a steeper yield curve. The coincident indicator rose by 0.6%, while the lagging indicator fell by -0.5% (the latter mostly due to weaker credit growth). For the trailing six months ended in March, the leading index rose at an annualized rate of 7.8%, which was a bit slower than the 8.1% annualized rate of the prior six months, which had started in the trough of March 2020. Overall, to no surprise, a variety of economic indicators continue to show robustness as the overall economy regains its footing.



Source: The Conference Board. Shaded areas indicated recessions as defined by the NBER.

(+) **Initial jobless claims** for the Apr. 17 ending week fell by another -39k to 547k, below the median forecast calling for 610k. **Continuing claims** for the Apr. 10 week fell by -34k to 3.674 mil., which was still above the 3.650 mil. expected. Initial claims numbers were mixed by state, with TX and NY showing the largest declines, while claims ticked higher in VA, IN, and MI—the latter where the recent Covid upsurge remains a problem. Combining the regular programs and extended benefits showed a net increase in claims, which remained under 10 mil., showing some progress in the reduction of the overall count from peak levels.

Question of the Week

Are cryptocurrencies the place to be, especially if we see more inflation?

We've covered some of the characteristics of cryptos before, but with the ongoing spike in investor interest, the topic is worth revisiting.

With any newer and harder-to-understand product, it's important to take a step back and not lose sight of the forest for the trees. From that vantage point, a buyer of any asset considered 'investable' should believe that it makes basic economic sense, is durable to some degree, and/or fulfills a special need. For crypto, the jury might still be out. It goes without saying that when speculation in hard-to-value assets are involved, any invested funds should be considered within an investor's overall risk budget.

From a conceptual standpoint, it's probably helpful to separate 'cryptocurrency' from the 'blockchain' technology upon which it's based. Aside from one's views on crypto, blockchain appears to be useful in some capacity as a modernized and transparent digital ledger for contracts and other records, where having a documented permanent chain of ownership is useful. It's not hard to see how such records could replace the legacy use of paper contracts, which are cumbersome in a world demanding speed.

Cryptos are considered by most to be alternative currency. One classic definition is as a medium of exchange. Bitcoin might meet that hurdle to some extent now that it's being more accepted as a payment mechanism, and is listed as an option for some online funds transfer options (similar to PayPal). This is potentially also true for ethereum and maybe a few other cryptocurrencies, but that's about the extent of it. Are these mediums of exchange liquid and easy to convert to other assets? Again, perhaps true of bitcoin and a handful of other brands, but it's not as obvious for the other few thousand cryptos with lower name recognition and usage. Prices for all are volatile, and can result in large gains or large losses for investors (and transactions are deemed taxable by the IRS). Does these pass the test as an effective medium of exchange? For the large cryptos, perhaps, but it's less clear about the rest.

What backs a particular currency as a store of value? Again, it's helpful to take a step back from the enthusiasm to see what's really present. Well-accepted currencies like the U.S. dollar are backed by the economic, taxing, and military powers of the U.S. government, and its immense asset holdings (federal land, precious metals, etc.). Less tangible but important backing comes from accepted cultural conventions, such as political stability and rule of law, that have created an environment of trust surrounding the dollar globally. The U.K. pound, euro, Japanese yen, and Swiss franc are also well-accepted as globally-desired currencies, due to the underlying trust holders have in the assets and policies of these nations. Both tangible and intangible factors have resulted in their relative price stability over time. Cryptocurrencies, on the other hand, have experienced the type of volatility more in line with the stock market. This instability tends to run counter to the desired predictability for a major currency, especially one used as a global medium of exchange. (Would a buyer feel comfortable seeing the price of a new car change from $20,000 one month to $60,000 the next?) An advertised trait of cryptos is that they aren't reliant on any single government or economic bloc for support, nor can they be subject to central bank monetary policies. The independence has been seen as a strong benefit, especially with the opinion of some that major governments are spending too much money, threatening long-term currency values. However, if something bad happens, it also means there is no authority with deep pockets to step in and provide support, either.

It's helpful to have that backdrop to compare cryptocurrencies with conventional ones. Bitcoin has developed a crowd following, and seems to have the benefits of a network effect. This is due to it being an early mover in the space, and stated limitation of total 'coins' that will be produced. Unfortunately, some crypto investors may have a harder time understanding what they own, with only a 'hope' that it rises in price, and intention to sell to others at a higher price. In that sense, it could be more appropriate to consider these more speculative in nature as opposed to mainstream currency alternatives, at least at this point in time. This makes them more akin to an emerging market currency, or even a penny stock or stock option. (Again, the most durable currencies have tended to not be speculated in for hopes of big gains—aside from leveraged futures markets, that is. The currencies used in most global trade have been more stable than volatile, which is the reason why they're used in the 'medium of exchange' capacity.)

Moving away from the most liquid and recognized cryptocurrencies, where name recognition and network user effect has created a market, the next tier of digital currencies could potentially be in the thousands. If a cryptocurrency is that easy to create and introduce to the world, with so little information about their backing and liquidity, risk rises tremendously. This is not only price risk, but risks of operational problems, and fraud. In a sense, some appear more like rewards programs, to the same degree that airline miles or grocery store coupon points are 'currencies.' As in many emerging industries, dilution between all of these cryptocurrency products could create a handful of winners and many losers. The fact that only 180 national/regional physical currencies exist today (according to the United Nations), some with fairly little liquidity, shows that the marketplace is not unlimited. In one example, it's our understanding that at least one well-known cryptocurrency was set up as a joke by its founders, and has since taken off due to the novelty, with help from online message boards to 'pump up' the value. What makes one coin better than a dozen or thousand others one could pick from? Another risk is technological. If new processes are invented, which reduce transaction times, fraud/theft risk, electricity use, or other hurdles, it's easy to see new winners emerging. Of course, this was said about bitcoin a decade ago, with many predicting its immediate downfall—yet, it lasts.

There is also the increasing risk of individual governments creating their own cryptocurrencies (most G10 currency transactions are electronic to a large degree anyway), which could change supply/demand dynamics for the current privately-issued coins. Originally, the most attractive feature of bitcoin and cryptocurrencies generally was their anonymity and lack of affiliation with a government central bank. This was seen as a benefit for privacy reasons (a criticism is that these can be used in illicit transactions, but so can paper cash), and as a potential safe haven from inflation or devaluation of major country currencies. All else equal, these features remain selling points, but seem to have taken a back seat to price speculation lately.

Of course, there are more risks. What happens in the event of widespread hack and crypto theft? (These have already occurred.) What authority is really in charge to help restore confidence and asset values? Secure storage is an important issue for all digital assets, as online sources haven't always been foolproof. The Coinbase IPO this month (with a market cap of over $85 billion) has elevated visibility on the liquidity/trading side, but security problems haven't been solved. There is also the possibility of governments regulating or even outlawing the use of crypto, outside of their own perhaps, which could threaten the value of existing products (meaning the chance of a current coin becoming worthless isn't zero). For instance, China has tried to circumvent the use of crypto, to prevent capital flight and evasion of surveillance. What if the power goes out? This is a problem for all digital assets, with digital money being adversely affected at an inopportune time. Speaking of energy, cryptocurrencies like bitcoin that require 'mining' (coins are given as rewards for solving math puzzles) require immense amounts of electricity, which hasn't been earth-friendly.

Opinions in the economic and institutional investment communities remain split, between those thinking crypto is a viable investment alternative and those skeptical about durability, compared to classic tangible assets like precious metals. Firms that have moved into the crypto business tend to have a much more bullish view on the industry's prospects, unsurprisingly. Interestingly, few fund firms or brokerages generally have been outright bearish on the space, despite the risks, perhaps in order to preserve their option of providing crypto-based products or services in the future. A few exchange-traded funds that own crypto have opened abroad, with the U.S. SEC still under pressure to make a definitive call on domestic products. The prices of current strategies have diverged from their underlying net asset values, due to a liquidity premium—investors have placed a value on the ease in 'one button' crypto exposure, as opposed to vetting custodians and exchanges, needing to open a digital wallet, etc.

In short, for investors in crypto, it's probably a prudent approach to focus on the more-accepted brands, which also tend to be the most heavily traded. Inflation opinions are mixed, with as many arguments against a sharp rise than for it; the newness of crypto makes the potential reaction to inflation unclear. In all fairness, traditional currencies and cash-like instruments haven't fared that well on an inflation-adjusted basis over longer time frames, either. Better traditional hedges against inflation include equities (unless it becomes extreme), real assets like commodities and real estate, possibly TIPs, and foreign assets (if the dollar weakens relative to history or other currencies).

Are cryptos in a bubble? As with any historical bubble events, that's hard to answer in real time. However, the level of general excitement, the FOMO (fear of missing out) component, and lack of discussion about downside risks might point to something. Related assets, such as blockchain derivatives called NFTs (non-fungible tokens) have also become popular. Some NFT pieces in the art world like digital photos, videos of famous NBA dunks, etc., have been selling for astronomical prices. Perhaps this could either be the start of a new futuristic trend or an odd footnote in a history book at some point.

Market Notes

Period ending 4/23/2021	1 Week (%)	YTD (%)
DJIA	-0.42	11.86
S&P 500	-0.11	11.80
NASDAQ	-0.25	8.96
Russell 2000	0.41	15.33
MSCI-EAFE	-0.41	7.41
MSCI-EM	0.35	5.23
BBgBarc U.S. Aggregate	0.13	-2.43

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2020	0.09	0.13	0.36	0.93	1.65
4/16/2021	0.02	0.16	0.84	1.59	2.26
4/23/2021	0.03	0.16	0.83	1.58	2.25

U.S. stocks ended a bit lower on net, although small caps continued to outpace large caps. By sector, health care was one of the few gainers for the week, up nearly 2%, while energy, utilities, and consumer discretionary stocks all led on the downside. Real estate also gained several percent, as the recent tempering in interest rates and economic reopenings continued to help sentiment for the group.

Earnings continue to roll in for Q1, with a quarter of firms in the S&P in, and FactSet noting over 80% of companies reporting an earnings surprise, with blended already-reported and estimates calling for 34% year-over-year earnings growth—far stronger than the 24% growth expected. Net profit margins have also increased to one of the highest readings in the last decade. Company narratives have largely reflected the challenges of the past year, such as that of airlines, although comments contain tinges of optimism for quarters to come. For some digital winners, on the other hand, such as Netflix, that benefitted from the extended lockdowns, 'normal' hasn't looked as good.

A positive week for stocks took a negative turn on Thursday, falling -1% almost immediately after President Biden proposed higher capital gains taxes on wealthy Americans (likely those earning over $1 mil. a year) to the maximum ordinary income tax rate, or even higher into the 40-45% range. Then again, moods seem to improve by Friday. While the '1%' owns the vast majority of U.S. equities by overall assets, equity ownership is far more diffused than it was decades ago (through retirement accounts and cheap trading). However, the sheer talk of rising capital gains rates, even for the wealthiest sliver of society, can send a bit of a shockwave through markets, which fear higher taxes for lower brackets as well. Much remains to be determined on this front, but the massive government spending that's taken place will have to be paid for one way or another. While the more extreme higher-rate tax plans may not make it through a one-vote majority in the Senate, a variety of numbers may be floated out over the spring and summer as the administration looks to gauge sentiment for various 'pay for' options.

Foreign stocks underperformed U.S. equities, largely due to negative returns in the U.K. and Japan, not helped by even a weaker dollar. Emerging markets outperformed, with a small gain for the week. China, Brazil, and Mexico all fared positively, but were offset by weakness in India and Turkey—so a mixed week broadly. Rising Covid cases outside of the U.S., notably in Europe and India, dampened sentiment relative to the U.S. as lockdowns continue and vaccine supplies appear more problematic. The ECB kept policy unchanged, as expected.

U.S. bonds gained slightly, as interest rates fell by a basis point or two across the yield curve. Investment-grade corporates fared best, followed by bank loans, although most domestic segments saw little significant change.

The U.S. dollar fell by nearly a percent against developed market currencies, causing a sharp rise in developed market debt, while emerging market bonds were little changed on the week.

Commodities gained ground generally, along with a weaker dollar. Agricultural prices led the way, with corn and wheat up over 8% each, due to weather concerns in both the U.S. Midwest and Brazil. Industrial metals gained slightly, while energy declined. The price of crude oil fell by almost -2% to just over $62/barrel, with larger supplies and an assumption that a paring back of Iranian sanctions will add to global oil production, and further supply gains.

Have a good week.

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Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post. Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.