Summary

The Federal Reserve meeting last week resulted in no changes in policy, per expectations. Economic data included strong advance GDP results for Q1, as anticipated; and durable goods orders, housing prices, and consumer confidence all experienced growth.

U.S. equity markets were mixed to lower for the week, outperforming foreign stocks that lost ground in line with a stronger dollar. Bonds fell back as interest rates ticked higher. Commodities gained across the board along with stronger goods demand coupled with some supply concerns.

Economic Notes

(0) Following the **FOMC** non-decision mid-week, and subsequent press conference by Fed Chair Powell, economists focused on the word 'transitory'—used to describe the recent uptick in inflation. Some watchers are skeptical, bringing up the lack of historical precedent for the unusual past year, and immense fiscal stimulus, which is feared to be a potential inflation trigger for years to come. A good deal of debate remains about Covid's aftermath on the economy, and the Fed is waiting until 'substantial' further progress has been achieved before acting. However, there is a more optimistic reality as well. Rapid vaccine development and a fairly efficient distribution process may cap the overall pandemic impact to perhaps just a year or year or and a half, in the best case. This compares to historic pandemics of the past that have lasted years, with unpredictable geopolitical repercussions, and few medically-based resolutions. The economy has bounced back sharply, and continues to—perhaps at a better rate than expectations. Labor markets, heavily tied to shutdowns and social distancing behavior, have also improved, although they still have room to go. Powell himself noted the initial worries of the Feb about labor market 'scarring' (in which worker job skills, networks, etc. can erode the longer a recession persists), but this largely seems to have been avoided. Recent quotes from Powell include the 'thinking about thinking about tapering,' referencing the caution about communication which is an odd contrast to the more secretive Fed actions of the past. In theory, this gives financial markets time to absorb the concept well in advance of any official action.

(+) The advance report of **U.S. GDP** for the first quarter came in at an annualized 6.4%, an improvement on Q4's 4.3%, but a bit below the 6.7% consensus expectation. Interestingly, as GDP growth is quoted in real/inflation-adjusted terms, the number would have been a bit higher had the pickup in inflation been less (nominal GDP growth was up an annualized 10.7%—one of the of the strongest results in the last 40 years). Personal consumption rose nearly 11% in the quarter, which reflected the strong surge in business reopenings and general spending activity (particularly of the in-person type). Goods consumption was up 24%, despite its smaller size in the economy, while services rose a still-solid 5%. Government spending rose by over 6%, with gains in business loan programs and Covid vaccines in particular. Inventories fell by -3%, which may serve to adjust Q2 growth higher, as that segment tends to borrow from or add to subsequent quarterly growth. The GDP price index grew at an annualized rate of 4.1%, while the core PCE price index rose an annualized 2.3% during the quarter, each of which were just a tick below expectations.

We're relatively early in Q2, but the Atlanta GDPNow model is predicting 10.4% growth, and New York Fed Nowcast is estimating 5.3%. These models use real-time, and predicted relationships based on history, such as correlations, and are subject to change. Following the Q1-Q2 bouncebacks, 2021 and 2022 as a whole could see above-average growth, before it tapers off toward more normal levels. Growth numbers are dependent on the pace of the mini-boom resulting from general restarts, as well as the result of any government infrastructure plan; however, consumers probably won't be getting multiple haircuts and other services for those lost in 2020.

(+) **Personal income** rose a dramatic 21.1% in March, about 0.8% higher than expectations, with stimulus payments representing the bulk of the total. In fact, this equated to the strongest single-month result in the series history, dating back to the 1950s. On a year-over-year basis, personal income was up nearly 30%, including a surprising 4% rise in salaries, although base effects from March 2020 are a large part. **Personal spending** in the month rose by a less-dramatic 4.2%, a tenth higher than expectations. The combination caused the personal saving rate to rise by a significant 13.7% to 27.6%. The savings rate is not only a theoretical byproduct of income minus spending in this case—this has reflected a 'hoarding' of cash by many Americans during the pandemic, or spending on items other than essentials. The March PCE price index rose 0.5% on a headline level and an upwardly-rounded 0.4% for core. This brought the year-over-year rate of change to 2.3% and 1.8% for headline and core, respectively—signs of the reacceleration of inflation that the Fed has been looking for. The base effects will be significant though, in the near term, as the potentially 'transitory' effects the Fed has mentioned as the economy reopens.

(0) **Durable goods orders** rose 0.5% in March, which lagged the median forecast calling for 2.3%. Core capital goods orders, removing the more volatile components like transportation (particularly commercial airplane orders), saw a 0.9% increase, but still below the 1.7% expected. Core capital goods shipments rose 1.3%, just short of expectations, and inventories rose by 1%. Monthly data tends to be sporadic for this index, but overall orders are up 25% from a year ago, which has also coincided with shortages for cars and household appliances.

(+) The **S&P/Case-Shiller home price index** gained 1.2% in February, beating expectations by a tenth of a percent. All twenty cities experienced gains, led by 2% increases alone in San Diego and Phoenix, followed by solid gains in Seattle and San Francisco as well. Year-over-year, the index continued to accelerate higher, by 0.8% to 11.9%. A combination of low interest rates, rising demand, and low inventory has continued the trifecta elevating housing values. Interestingly, on a real inflation-adjusted basis, prices are near where they were at the prior peak of March 2006.

(+) The **FHFA house price index**, which covers a broader swath of the country than just the largest cities, rose 0.9% for February, falling just short of the 1.0% increase expected. All of the nine regions saw gains, led by the Mountain and Pacific states, each up about 1.5%. Year-over-year, this also accelerated, by 0.2% to 12.3%—the highest one-year reading since the index was created in the early 1990s.

(0) **Pending home sales** rose by 1.9% in March, which disappointed relative to the 4.4% increase expected. Regionally, the Northeast saw the strongest gains, at over 5%, followed by the South and West, while those in the Midwest fell by -4%. It appears, based on comments from the NAR that tight housing inventories remain a 'consistent' issue, which will weigh on existing sales as well. Year-over-year pending sales are up 25%; naturally the March 2020 trough in sales played an extreme role in the bounceback.

(+) The Conference Board **consumer confidence index** for April ticked up by a robust 12.7 points to 121.7, surpassing the 113.0 level expected. Consumer assessments of present economic conditions rallied by nearly 30 points, surpassing the far smaller improvement of the future expectations component. The labor differential, which measures the ease in finding employment, also rose 17 points. Overall, consumer confidence looks to be rebounding sharply as vaccinations become more widespread, and businesses reopen. Levels near 120 are more indicative of 'late cycle' dynamics, which reflects the extremely distorted timeline of the past year. The employment component will continue to take time, but optimism about job prospects is a welcome reflection of improvement there as well.

(+) The final **Univ. of Michigan consumer sentiment index** reading for April saw a rise of 1.8 points to 88.3, surpassing expectations of 87.5. Assessments of current conditions were unchanged from the prior reading, while expectations for the future rose by several points. Inflation expectations for the coming year fell back by -0.3% to a still-very high 3.4%; those for the next 5-10 years were flat at 2.7%.

(0) **Initial jobless claims** for the Apr. 24 ending week fell by -13k to 553k, a low point for the pandemic recovery periods, but a bit higher than the 540k expected. **Continuing claims** for the Apr. 17 week came in 9k higher at 3.660 mil., a bit further than the 3.590 mil. level expected. Initial claims rose sharply in VA and MI, while TX saw the highest decline. On the broader side, including special pandemic emergency programs, it appeared that roughly a half-million beneficiaries fell off the rolls last week, which is another positive development.

Market Notes

Period ending 4/30/2021	1 Week (%)	YTD (%)
DJIA	-0.50	11.30
S&P 500	0.04	11.84
NASDAQ	-0.38	8.55
Russell 2000	-0.23	15.07
MSCI-EAFE	-0.76	6.59
MSCI-EM	-0.37	4.83
BBgBarc U.S. Aggregate	-0.18	-2.61

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
4/23/2021	0.03	0.16	0.83	1.58	2.25
4/30/2021	0.01	0.16	0.86	1.65	2.30

U.S. stocks reached record highs yet again falling back somewhat by Friday. By sector, 'value' segments did well again, with energy up nearly 4% along with stronger crude oil prices, followed by financials and communications. The latter was helped by stronger than expected revenue/earnings news from large constituents Alphabet and Facebook. Real estate also fared positively, despite interest rates ticking higher, but helped by stronger economic data. Info technology and health care lagged, each down a few percent for the week, upon earnings reactions.

Earnings data has come in for roughly 60% of S&P 500 companies, with results the best year-over-year numbers in a decade at the current pace (according to FactSet data), and 86% of firms beating estimates—which itself would be a record if that pace continues. The strongest results are coming from consumer discretionary and financials, with both well over 100%, followed by materials and communications. Notably, revisions continue to be upward, which may explain the more enthusiastic large cap stock valuations, at least from a P/E standpoint. From a free cash flow metric, valuations appear lower.

Foreign stocks performed negatively last week, with still-lagging economic activity due to Covid lockdowns and a stronger U.S. dollar. Eurozone GDP was reported at a -0.6% decline in Q1, which was unsurprising due to the longer period of contained movement and activity compared to the U.S. While the U.K. gained slightly, Europe and especially Japan lost ground, due to earnings weakness in the latter. On the positive side, lockdown easing was announced in France for one, with a goal of the end of June for broader reopening. Emerging markets fared similarly to develop markets, highlighted by weakness in China due to continued crackdowns on fintech firms, and a bit of profit-taking from tech firms generally. There has been rising concern over certain Chinese bonds, especially those in the state-owned enterprise group, coinciding with the government's attempts to smooth over bad debt. The recent decline in bonds of Huarong AMC, the country's largest state-owned distressed debt manager, after some delayed reportings, highlights this risk.

U.S. bonds fell back last week, as interest rates ticked higher along with growth coming in stronger than anticipated, leading to higher inflation expectations and investor flows moving away from safety and toward risk. High yield and floating rate bank loans fared better than investment-grade debt, with flattish results for the week. Foreign bonds were down a percent in developed markets, due to the negative influence of a stronger dollar, while emerging market debt was down to a lesser degree.

Commodities rose across the board last week, led by gains up to 3% for agriculture and industrial metals, followed by smaller gains for energy. Precious metals was the sole declining group on the week, as investor risk-taking and higher interest rates outweighed other factors. The price of crude oil rose over 2% to around $63.50/barrel, largely due to shorter-term inventory issues. Generally, expectations for higher inflation tied to stronger economic growth have driven commodities to a recent mini-boom. Corn, for example, has experienced its strongest month in several years as bad weather has been coupled with labor shortages and spiking demand. This has resulted in commodities earning the strongest returns of any asset class over the past year, rewarding patient asset allocators.

Have a good week.

Ryan M. Long, CFA
Director of Investments
FocusPoint Solutions, Inc.

Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Axios, 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.