THE ECONOMIC MONTH IN REVIEW AND OUTLOOK – APRIL 2021

U.S. Markets and Economy

U.S. stocks set more records in April as the young bull market, led by a resurgent NASDAQ index, made strong gains for the month. The NASDAQ gained 1,000 points and again surmounted the 14,000 level, while the Dow Jones broke through 34,000. The broad-based S&P 500 index was also strong, cracking 4,200 and gaining 5% for April. The S&P is up above 11% for the year already, which is an above-average *annual* return in recent decades.

The good news has poured in from all sides: many companies have reported first-quarter earnings that beat Wall Street estimates. Compared to last year's first quarter (already dented by the beginning of the pandemic), corporate earnings should be up an astonishing 50% year over year. The second quarter should be even better, because the comparison quarter (April–June 2020) was an economic disaster as the pandemic and lockdowns spread across the country. In addition, the rate of growth of the U.S. economy is surging, with the first estimate of first-quarter real growth coming in at a very strong 6.4% annualized. Most forecasters expect the current quarter to be even stronger as the economy continues to open and the virus continues to recede, with U.S. daily vaccinations still exceeding two million. More than 100 million Americans are now fully vaccinated against the virus. Employment growth is still fairly rapid, although April's unemployment rate was steady at 6.1% (according to data released in early May).

The economy is powering ahead, with a strong dose of expansionary fiscal policy already administered by the Biden administration. Previous rounds of stimulus payments have not all been spent by American consumers, so the "dry powder" in American checking accounts will drive consumption spending even higher. The Biden administration has proposed another $4 trillion in spending, and even if only a fraction of that amount is eventually approved by Congress, there will be even more forward thrust from fiscal policy (the markets have shrugged off the possibility that some of this spending will be paid for with a higher corporate tax rate and higher taxes on high-income individuals).

The Federal Reserve has done its part to keep the party going. The Federal Open Market Committee (FOMC) statement issued at the end of its latest meeting stated clearly that the Fed was going to maintain its zero short-term interest policy for some time, and, in addition, Jerome

Powell stated that there were no plans to cut back on "QE4," which means continued monthly buying of $120 billion of longer-term securities. Even the bond market showed some signs of life, with the 10-year Treasury yield retreating from the 1.75% level. This decline in yield suggests that the bond market is not worried about a substantial pickup in inflation. The Fed knows that measured annual inflation will exceed 2% for some months, as comparisons are against weak prices a year ago. Because the FOMC has declared that its 2% target is now only an average, a moderate (and temporary) increase in inflation above 2% is acceptable (one member of the FOMC reminded everyone that if inflation did pick up "too much," the Fed certainly knows how to contain it). The Fed is also determined to get the economy back to "full employment" before hitting the monetary brakes. Because that level of unemployment may be around 3.5% (the level reached before the pandemic), there is still plenty of room for additional economic growth.

World Markets and Economy

Europe is still down in the dumps. The virus is not under control, vaccinations are lagging, and an expansionary monetary policy by the European Central Bank (ECB) has not been matched with sufficiently expansionary fiscal policy, as the members of the eurozone have only just begun to have a common fiscal policy for all members—and, of course, there is still the adjustment to Brexit. Much about Brexit has yet to be settled, with the latest example being fishing rights: in early May, British and French patrol boats were headed for a confrontation near the isle of Jersey. For April, the broad-based STOXX Europe 600 index gained less than 2%, losing more ground relative to booming U.S. indices. British stocks led the way higher, while German stocks lagged with a gain of only 1%. UK economic activity should surge in coming months, according to the Bank of England, while German economic activity sank in the first quarter of 2021.

In Asia, China has continued its strong post-pandemic growth, while also continuing to flex its military muscles in all directions. An economic cold war between China and the U.S. could slow growth in all of Asia. The Biden administration will have to find a way to both compete and cooperate with China. Not surprisingly, Chinese stocks lost ground in April. Japan's stock market also was lower.

In India—soon to be the world's most populous country—the COVID-19 epidemic is still spreading almost unchecked. Aside from the massive human misery inflicted on India, there is also the risk that new variants and new infections could spread to other countries. India's stock market also fell.

Outlook

The economic recovery is now in high gear, supported by reopenings, pent-up consumer demand, and expansionary fiscal and monetary policy. As in any bull market, there are minibubbles of speculative euphoria driven by short-term (usually naive) public speculators. Even Jerome Powell has used the F-word (froth) to describe this phenomenon. The inevitable popping of these bubbles could lead to short-term selloffs, which would be a healthy corrective. As we said last month, long-term investors will avoid all fads and bubbles and stick with the tried-and-true: a diversified, well-managed portfolio of good-quality stocks of companies with real earnings, dividends, and growth potential.

Please remember that past performance may not be indicative of future results. Different types of investments involve varying degrees of risk, and there can be no assurance that the future performance of any specific investment, investment strategy, or product, including the investments and/or investment strategies recommended or undertaken by Reilly Financial Advisors (RFA), or any non-investment related content made reference to directly or indirectly in this commentary will be profitable, equal any corresponding indicated historical performance level(s), be suitable for your portfolio or individual situation, or prove successful. PLEASE SEE ADDITIONAL IMPORTANT DISCLOSURE INFORMATION at www.rfadvisors.com/disclosures.