LaFleur & Godfrey
PRIVATE WEALTH MANAGEMENT

Fall 2021 Commentary

Dan Van Timmeren

John Koczara

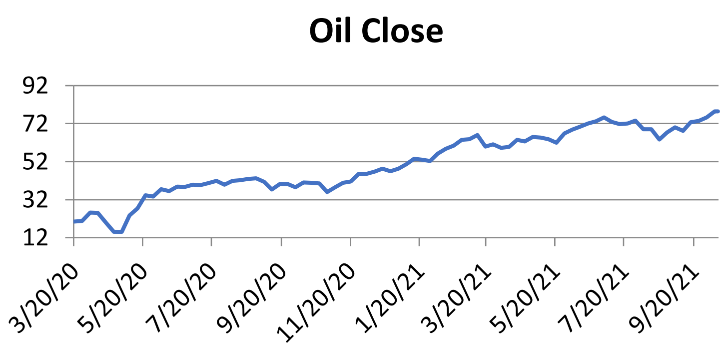
A Bumpy Ride To End The Year?

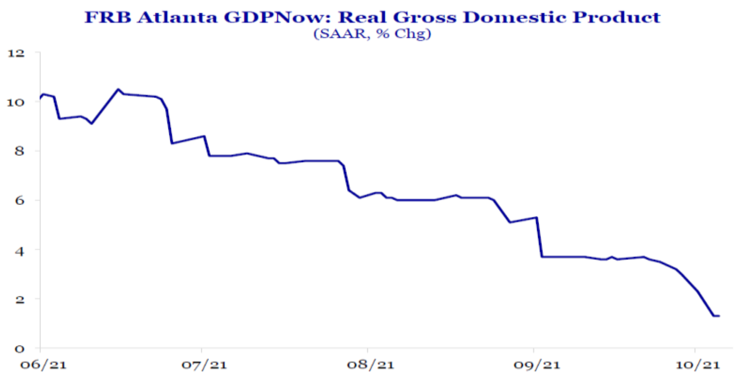
Economic Perspective: As our last quarterly commentary intimated, our economy has now reached the uneven and uncertain stage. Gone are the days of daily economic ‘beats’. Unfortunately, they have recently been replaced by ‘surprises’ & ‘misses’ to a large extent. This was to be expected with year-over-year comps becoming more challenging. However, beneath the surface, some of the recent weakness has caught our attention.

Supply chains around the world are an absolute mess. Pent-up demand, labor shortages and production issues related to the pandemic have resulted in huge supply chain delays and dramatic cost increases. The average cost to ship a 40-foot container has more than quadrupled compared to one year ago! Companies will struggle to pass these increased costs on to consumers. Our key concerns are a.) whether higher producer prices stick and b.) if unfilled demand is deferred into the future or lost for good. This will depend on how soon some of these issues are resolved.

The rise in energy prices is also worth noting. Oil has breached the $80 per barrel level and natural gas has been hovering around $6 per million BTU. Both prices are near highs last seen in 2014. It is likely that they remain range bound near current levels as OPEC has stood firm with its position to gradually increase production levels, much to the dismay of the United States and other countries.

With projections for moderating economic growth over the next six to twelve months, you would think all areas of the economy would be weak. That is hardly the case. The housing market, a beneficiary of our low interest rate environment, remains red hot. Our service economy, the largest in the United States, remains very strong. The recent ISM Services Index report came in at 61.9 – bolstering the case for strong, sustained growth. This marks the eighth month in the low to mid-sixties (any reading above 50 is expansionary). Even manufacturing improved in September with a reading of 61.1 – its highest level since May. We also need to remember that if GDP growth slows from 5-6% today to closer to 3%, that’s still good! It’s all a matter of perspective.





Market Perspective:

The stock market spent 227 calendar days before it finally corrected just over 5% in September. To say that we were due for a pullback would be an understatement. During that same time period, the market was up over 30% - rightfully so given the strong economy, improving earnings and significant valuation multiple expansion. Our friends at Strategas Research posit that market performance over the near-term will need to be led more by earnings & fundamentals over the P/E multiple expansion we have been experiencing. We wholeheartedly agree – especially if interest rates are rising coupled with higher inflation. It may prove challenging with several market headwinds that still need to be resolved.

Proposals out of Washington D.C. have investors on edge. The current 'human' infrastructure bill being negotiated includes higher taxes for businesses (corporate rates up), consumers (income taxes up for high earners) and investors (capital gains taxes up). Without clarity, we expect a range bound market.

Importantly, the Federal Reserve is pulling back its accommodation – as soon as the November 3rd Fed meeting. To his credit, Fed Chair Jerome Powell has done an admirable job communicating with investors and telegraphing his intentions. The market is currently pricing in a pullback in asset purchases (down from $120 billion per month) but no change in interest rate policy for the foreseeable future. This is very important. If interest rates SLOWLY grind higher over the coming months/quarters, we will remain constructive on equities. The real risk remains with inflation. We remain in the camp that argues that a normalization of supply chains is on the horizon and current issues will resolve themselves. As such, we expect the current inflationary pressures to subside. However, it is likely they will settle at a level higher than the Fed's preferred 2% target.

Looking Ahead:

Consumer economic activity led the way coming out of the depths of the pandemic. We are encouraged that economic leadership in the United States is becoming more balanced along with business activity. A key barometer of business activity is capital goods orders excluding aircraft and defense orders. This is widely known as a good proxy for business investment. It has been on the rise and recently rose 0.5% - accelerating from a 0.3% increase the month prior. Year-over-year, business investment rose an impressive 15.8%! This bodes well for sustained economic growth. When businesses feel confident enough to invest, there are oftentimes many positive ripples throughout the economy. While we are not yet out of the woods with this pandemic, there are indications that the worst is behind us. As our economy transitions from its fast pace to a more moderate pace, our investment team is confident the economic gains will be durable and it will therefore remain a favorable environment for investors.