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## CHANGE IS SPECULATIVE

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Market Review    **JUNE 2021**

In little time, the temporary and deflationary change that COVID-19 brought reversed into another leg up for the business cycle and inflation. Trillions of dollars went into the economy to keep expenditures upright through the pandemic. Without the increase in money supply, government loans, and transfer payments, the economy may have gone into a depression. Giving economic support was seemingly necessary, but it also changed the systemic risks that investors face moving forward.

Today's low return and rising price environment are accomplishing their intended effects in the economy, but the same monetary climate has likely altered the path of future financial returns. For the economy, a consumption rebound just took place on methods that effectually borrow from future consumption. Therefore, all of the debt accumulation that went into supporting consumption during the COVID-19 crisis has probably come with the chance of less consumption once the economy enters the payback period. The payback period could take shape in the form of higher taxes. It may also require a higher percentage of business profits to pay back old debts if balance sheet deleveraging becomes a requirement. Higher taxes and future debt service could subtract from future shareholder distributions and produce a different path for financial returns.

However, being in a low-return environment is helping to support risky ventures in the hopes that these investments will realize a long life of usefulness. Doing things to drive the cost of capital to zero may result in an innovative breakthrough. For example, a significant amount of money has gone into financing companies linked to clean energy projects, social finance, and software development. Some of these investment projects could have huge societal payoffs, assuming that they can improve the quality of life or even raise productivity standards. Low returns and low borrowing costs are opposite sides of the same thing and act as agents for the next investment boom.

Still, overly optimistic and wasteful investment expenditures could produce excesses in capital pricing and lead to a net overall economic loss. Moreover, paybacks on unproven investment projects may never come. If the investment required to enter a venture is so high compared to its future return of capital, the internal returns that define the project might already measure out to nearly zero. Going public in today's market with a suitable business model can mean an immediate multi-billion-dollar valuation. In many instances, these business models have not established a track record. They may currently lack merit

**"Congress seems close to passing another trillion-dollar bill that would invest in the infrastructure of the economy."**

based on fundamentals and derive all of their present value from expectations for the future.

The present SPAC (Special Purpose Acquisition Company) situation is helping to rapidly expand investment before investors can obtain all of the facts. Companies turning public in a SPAC can avoid the traditional underwriting channels and obtain public market financing more efficiently. However, the awards given to ventures and the people who help raise SPAC money could come at the detriment of public investors. Still, investment vehicles like SPACs are usually a sign of a lot of excess liquidity in markets. Today's compressed yield spreads on high-yield debt is another picture of excess liquidity pushing down yield premiums to take on risk. The federal government plays a part in encouraging investment. Congress seems close to passing another trillion-dollar bill that would invest in the infrastructure of the economy. Fortunately, a good chunk of money is for road and bridge repair. Still, speculative investment in new technology like electric vehicles and battery refuel stations are other fiscal objectives. More government spending will further expand the financial economy. Hopefully, such an expansion will result in productive growth; otherwise, price and valuation uncertainty could be what is in store.

It's not that present market conditions are wrong. For example, if new technologies experience a massive breakthrough moment, then present valuations might be set too low, and inflation expectations could verge on being too high. But investors should still have a level of awareness for what is happening between the exchange of risk and return. Then they can be in a better place to plan and make appropriate and controlled investment decisions. The practice of planning has many components that include decisions made around asset allocation, investment concentrations, tax planning, retirement income planning, and estate planning. Therefore, it is essential to understand the changes occurring in capital markets and the global economy and implement comprehensive financial planning decisions accordingly.

Asset Categories	US STOCKS	FOREIGN STOCKS	US BONDS	FOREIGN BONDS	HARD ASSETS	HYBRIDS
Monthly	0.54%	-0.18%	0.67%	-0.18%	-1.00%	1.60%
Year to Date	17.36%	9.99%	1.28%	-1.22%	17.00%	4.85%

\*DATA USED IS SOURCED FROM MORNINGSTAR®, DATE ENDING JUNE 30, 2021.

## US STOCKS

US Stock returns showed strength in large caps in June but experienced nearly no change in mid-and small-caps. Growth assets fueled the large-cap rally as the interest rate climate began to soften again. As a result, large-caps posted a 1.7% return in the month, which raised their year-to-date return to 14.9%. Year-to-date returns held in mid-and small-caps currently stand around 17.0% and 20.2%, respectively. Growth investments have started to outperform as low interest rates are seemingly keeping innovation active.

## FOREIGN STOCKS

Foreign Stocks slipped mildly in the month to record losses of around -0.18% for the broad category. However, the foreign asset category has provided a near 10.0% return since the beginning of the year. In June, foreign large-caps were disappointing by finishing down -1.1% and bringing the year-to-date return to 9.1%. On the other hand, emerging markets received inflows in June to post a monthly return of 1.2%. That category has been a laggard, but its 8.7% year-to-date return is within the broader foreign stock category range.

## US BONDS

US Bond returns were positive for a second consecutive month. In addition, interest rates retreated last month, which helped to earn a 0.7% monthly return in the broad asset category. As a result, the entire category has captured 1.3% in the first half of this year. High-yield bonds and bank loans possess the highest investment returns to date. Their performance figures would confirm that there is a demand to own risk-based capital this year.

## FOREIGN BONDS

Foreign Bonds slid modestly in June to a loss of -0.18%, and the asset category is now down -1.2% for the year. World bonds are responsible for dragging the asset category down. The year-to-date loss in the world bond category currently resides around -2.3%. There is increasing pressure on global interest rate hikes since trillions of national value already sat below zero percent, which is a risk for this particular asset class. Conversely, emerging market bonds have been making a comeback and have managed to claw themselves back to breakeven this year.

## HARD ASSETS

Hard Assets experienced the most profound losses in June. The entire group lost -1.0% last month due to a -11.8% contraction in the precious metals price. The year-to-date loss in precious metals currently stands at -4.7%. Other hard assets, however, are performing well. For example, energy partnerships are up 37.9% this year, but their present valuations still come up short compared to pre-covid price levels. In addition, domestic real estate has returned 20.4% in the last six months, which also helped support the broader asset category.

## HYBRIDS

Hybrids were vigorous on both counts in June. Preferred stock and convertible debt posted attractive monthly returns of 1.3% and 1.9%, respectively. The category groups have also given modest but meaningful returns during the first half of 2021. Preferred stocks currently stand with a year-to-date return of 5.1%, while convertible debt is at 4.6% over the same period. The low return environment seems to be conducive to bringing demand to these assets.

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