Stegent Equity Advisors, Inc. Investment Letter

Market Review

July 2021

First, the good news. Returns have been pretty rosy across global markets mostly due to the perceived end of the pandemic. Equities were up big with the S&P 500 posting 8 new highs in June alone. The best performing sectors were energy, financials and real estate. Commodities were also up. President Biden's new infrastructure deal could mean a lot of additional stimulus to the US economy. Improvements to our transportation, power and internet infrastructure are long overdue.

Now for the bad news. One word: Inflation. Industrial metals were up significantly. Agricultural components such as coffee, wheat and corn spiked upwards while beef and pork trended downward. Inflation is making itself known in the US. In May, the core consumer price index (CPI) for inflation rose from 3% to 3.8% year-on-year marking the largest increase since June of 1992! In June it rose again, putting the current rate at 5%.

Another market negative is the incursion of MEME stocks (stocks that regularly make headlines and trade contrary to their company fundamentals). Lured by the social media hype, individuals are tying their hand at investing on apps like Robinhood. While the euphoria has resulted in life changing gains for some, we suspect investors will incur a lot of painful losses in the end.

So where do we go from here? It's no secret that a great many investors believe a stock market correction lurks just around the corner. However, it's also no secret that trying to time the market's ups and downs is mostly fruitless.

We try to incorporate thought leadership from many sources into our investing philosophy. One of our favorites, the economists at First Trust Advisors, L.P., tend to focus on the fundamentals such as profits and interest rates. They believe the S&P 500 is still undervalued and has a lot more room to run in 2021. Their model takes the government's measure of economy-wide profits from the GDP reports, discounted by the 10-year US Treasury note yield, to calculate fair value. Using a 10-year Treasury yield of 1.36% to discount profits (from the first quarter, the most recent available), their model suggests the S&P 500 is 45% undervalued. And with profits likely to grow 20% or more this year, fair value will rise more as the year unfolds.

First Trust also understands that current monetary policy is inflationary and that the US Federal debt has now risen above 100% of GDP due to past and current government spending. While these policies could shift their estimates in the future, they maintain their bullish position towards the market, citing the re-opening, easy money and deficit spending. With the Fed keeping interest rates down and profits trending upward, it appears that this bull market isn't quite done yet.

As always, we are grateful for the opportunity to continue to serve as your trusted advisor. Please reach out with any questions or concerns.

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