Market Review and Outlook

2Q2021

Risk assets continued their positive momentum during the second quarter as reopening progressed. The successful distribution of the COVID-19 vaccine coupled with sizable fiscal stimulus led to a bounce in economic activity as evidenced by the historically high level of the Purchasing Managers Index (PMI). Corporate earnings growth was overwhelmingly positive with most companies beating their earnings estimates for the first quarter. The Federal Reserve (Fed) maintained its accommodative policy stance but concerns over rising inflation led the Fed to pull forward its timeline for policy tightening by projecting at least two interest rate increases by the end 2023. We expect strong economic growth to continue through the back half of the year, but weaker seasonality and the threat of higher taxes could lead to more muted returns over the near term.

The S&P 500 Index gained 8.6% for the second quarter and 15.3% year-to-date. Real estate (+13.3%) and information technology (+11.6%) led returns for the quarter. Energy (+11.3%) continued its rebound as favorable supply/demand dynamics supported the sector. Utilities (-0.4%) and consumer staples (+3.8%) faced headwinds during the quarter due to their more defensive characteristics. Growth outperformed value but lags by a meaningful margin year-to-date. From a market capitalization perspective, large cap equities outpaced small and mid-cap equities for the quarter, but small cap equities lead year-to-date.

Developed international equities, as measured by the MSCI EAFE Index, gained 5.4% during the second quarter and 9.2% year-to-date. International equities have lagged the US year-to-date, facing headwinds from a slower start to the distribution of the COVID-19 vaccine. However, vaccination rates picked up during the second quarter which helped boost consumer and business confidence and increases the probability for a strong economic rebound during the second half of the year. Emerging markets, as measured by the MSCI Emerging Markets Index, gained 5.1% for the second quarter. Year-to-date, the Index is up 7.6%. The increasing threat of tightening monetary policy within China, a large driver of emerging market performance, served as a headwind for the region but strong performance within Latin America was a positive.

Investment-grade fixed income, as measured by the Bloomberg Barclays US Aggregate Index, gained +1.8% for the second quarter and year-to-date is down -1.6%. The 10-year Treasury yield trended down for the majority of the quarter, falling 29 basis points to end the quarter at 1.45%. Credit spreads continued to contract with high-yield spreads moving to the lowest levels last seen since 2007. Municipals finished in-line with taxable bonds for the quarter but lead year to date.

Growth has picked up as the economy continues to reopen. Fiscal policy remains supportive and there is a good chance of another fiscal spending package later this year; however, it will require tax increases as an offset. The Fed is committed to accommodative monetary policy until we see full employment and sustained higher inflation, neither of which we are close to achieving yet. The recovery in jobs has been meaningful, but we still have a long way to go to a full recovery. We expect an increase in inflation in the coming months, but the pickup should be more transitory in nature. Consumer and business confidence have improved markedly this year. Treasury yields have normalized in response to the improved economic outlook, but the pace has slowed, and yields remain at low absolute levels. Corporate earnings growth has been very strong, reflecting the strength in nominal GDP. Given these factors, our overall outlook tilts positive which argues for a continued bias toward risk assets over the near term.

Brinker Capital Market Barometer

SHORT-TERM FACTORS (< 6 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Momentum				●	Market momentum remains solid
Trend				●	US markets remain above 50-day and 200-day moving averages
Investor sentiment		●			Bullish sentiment has retreated in recent weeks but remains above its LT average
Seasonality	←	●			Entering more seasonally weak period historically

INTERMEDIATE-TERM FACTORS (6-36 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Fiscal policy				●	Additional fiscal stimulus likely in '21; concern over potential higher taxes
Monetary policy				●	Fed and global central banks remain very supportive
Inflation			●		Inflation has picked up recently; expect to be transitory but watching closely
Interest rate environment				●	Treasury yields fell throughout the second quarter
Macroeconomic				●	Expect strong economic growth in 2021 driven by the vaccine/reopening
Business sentiment				●	CEO confidence increased again in 2Q to a record high level
Consumer sentiment				●	Consumer confidence surveys improved further in June
Corporate earnings				●	Expect continued strong earnings growth in 2Q
Credit environment				●	Credit spreads continue to tighten

LONG-TERM FACTORS (36+ months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Valuation		●			Equity valuations well above long-term averages but not a near-term driver
Business cycle				●	We've entered a new expansion period with positive GDP growth since 3Q20
Demographics			●		Mixed - US and emerging markets positive but developed international negative

Source: Brinker Capital. Information accurate as of July 15, 2021.

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