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MARKET COMMENTARY November 28, 2021

Dow Jones Industrial Avg.		33843.92	Standard and Poor's 500		4307.54
2021 (YTD) +10.6%	3rd	Qtr. -1.91%	2021 (YTD) +14.7%	3rd	Qtr. + 10.64 %

Potential Headwind – "There is a perfect inverse correlation between inflation and price/earnings ratios … When inflation has been very high … P/E has been [low].. - Liz Ann Sonders (Chief Investment Strategist, Charles Schwab)

Real or a Mirage? – The stock market's strong start to the year took a pause in the third quarter. The major averages were basically flat, which reflected decelerating economic growth. This adverse trend drew much media attention as there were great hopes the recovery that began last year would continue under the leadership of the Biden administration. Instead, the Delta variant of the COVID virus arrived and quickly spread across the country, and the administration felt compelled to re-emphasize controls. These restrictions served to dampen the enthusiasm of consumers and slowed the pace at which employees were returning to the workplace, which retarded economic growth in the third quarter.

However, all the concerns quickly evaporated when third quarter corporate earnings began to be released in early October. It was a complete surprise to most investors that 80 percent of companies exceeded profit expectations. This encouraged investors to resume buying, which reignited the year's market rally because stocks remain the most appealing alternative for most investors.

Big Election Promises –President Biden made the focus of his presidential run on two ambitious legislative efforts aimed at providing additional stimulus to the economy to assure the recovery from COVID continued and to address important Democrat priorities. The purpose of the first legislative effort was to address the perennial problem of underfunding maintenance of the nation's infrastructure. Politicians boast about their support for infrastructure spending, but their willingness to provide the needed funding is weak. As a result, the nation's road, bridge, water, sewer, and airports projects have not received the funding needed to be properly maintained for decades. Modernizing the nation's electric grid and providing high-speed internet coverage throughout the country, especially rural areas, were also added as priorities.

At the insistence of the progressive wing of the Democrat party, the bill included major funding for the country's move toward more green energy and provisions to reduce reliance on carbon sources (i.e., oil, natural gas, and coal). When combined with the President's early initiatives to block pipeline construction and discourage oil and gas exploration, it follows domestic oil and natural gas production have been constrained. The combination of these divergent policies has contributed to the sudden spike in energy prices evident throughout the economy.

Cost/Benefit Justified? - Does that mean there is a clear road ahead for investors? Far from it. In fact, challenges abound. The arrival of the Biden Administration brought with it some drastic changes in key policies. In addition to the introduction of vaccine mandates, significant alterations to energy and immigration policies also were early initiatives. The flood of money being pumped out of Washington ostensibly to provide economic relief has been broadened to cover infrastructure, a concerted effort to promote green energy, and a laundry list of potential entitlements disguised as new social programs. The President's reputation suffered another blow as a result of major disruptions to the country's supply chain. Much of it was traced to our heavy reliance on China as a trading partner, but it spilled over into trade with other Asian countries, particularly Korea and Taiwan, which are intimately tied to our high tech and semiconductor industries. All these factors have contributed to the sudden emergence of a serious increase in inflation. Last year the Federal Reserve had an inflation target of two percent because there was concern deflation was a risk. Now inflation is raging. In October, the rate of inflation hit 6.2 percent - a 31 year high!

Green Energy Conundrum - Shortly after President Biden took office he terminated the Keystone Pipeline project, which would have brought oil from Canada. Moreover, it was recently announced another Canadian pipeline is also on his “hit” list. The President is willing to request additional oil production oil from OPEC and Russia, but he doesn’t want us to pump our own or allow some to flow from our friendly neighbor to the north. Next, he prohibited energy companies from drilling on federal lands and he has openly declared his desire to eliminate coal as a power source. The result of the administration’s poorly planned energy programs has become crystal clear. The price of energy in all its forms has skyrocketed. The President has decided the nation should have inadequate, undependable green energy rather than the affordable energy independence that existed a year ago. This leads to the question “Will requiring the country to become reliant on intermittent green power (i.e., solar and wind) be capable of meeting the current requirements of commercial, industrial, and household usage?” The added demand stemming from the massive conversion of the nation’s transportation industry including the nationwide network of recharging stations required to charge the millions of electric cars and trucks envisioned will only magnify the problem. Not enough forethought or planning has occurred given the scope of this vision. A successful transition will require much more time and treasure.

FED Chair - No Change – The Federal Reserve (i.e., FED) deserves much of the credit (or blame) for the prolonged period of low interest rates. Professionals refer to this policy as Quantitative Easing (i.e., Q.E..). This policy was devised to help the country recover from the previous recession, but it has endured for more than a decade because of a tacit agreement between politicians and the FED to protect the economy and the markets. They were fearful if they allowed the normalization of interest rates a recession might ensue, instead the politicians continued to spend, and the FED allowed the money supply to mushroom. The outcome has yielded an asset bubble as evidenced by record stock market prices and soaring real estate values coupled with a sudden surge in inflation. It is not unreasonable to conclude an adjustment, a reversion to the mean, looms ahead, and it may prove to be much more painful than if it had all been addressed earlier.

Although there are reasons to be cautious, the investment environment remains favorable. The economy is growing and businesses are profitable. Liquidity is plentiful. In spite of the churning market activity, the holiday season has traditionally been favorable for stocks. Another variable appears ready to rejoin the investment scene after a protracted absence – interest rates. If interest rates begin to show strong upward momentum realize they will ultimately exert a negative impact on stock prices. Although the market averages remain close to all-time highs, a significant number of “high flyers” have suffered major corrections. To repeat a common caution, valuations remain very rich or to state it more plainly, stocks remain expensive. Be selective. Finally, given the strength of the stock market this year, rebalancing one’s portfolio is worthy of consideration.

Year-End Suggestions – If securities or real estate gains have been realized during the year, check to see if there are any losses that can be used to offset the gains. In addition, for any losses exceeding realized gains, up to $3,000 can be used to reduce your taxable income. Those who are working should seek to build their retirement accounts to the extent possible. Different plans have different limitations as defined in IRS regulations. Check with your accountant or tax provider to assure your actions are consistent with IRS regulations. In addition to gifts to family or friends, also give thought to making gifts to local charities. One on my list I can recommend is the Cape Cod Times Needy Fund. Enjoy the holidays and make 2022 the best year yet! - JML