Rochester Financial Services

Fee-Only® Financial Management Services

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Dow Jones	S&P 500	NASDAQ	Russell 2000	10 yr Treas	Earnings Yield (S&P)	Gold	Crude Oil
34,133	4,165	13,634	2,248	1.59%	4.52%	$1,778	$66.26

Investment Strategy Report

With The Economy Roaring Back, Will Inflation Derail the Stock Market?

April was another strong month for stocks, as the S&P 500 and the Nasdaq both advanced 5.4%, while the Dow finished 2.7% higher. With more of the country getting vaccinated and Covid cases on the decline, and stimulus payments boosting consumer spending, the recipe for a strong economic recovery is set. And the economic numbers thus far reported have not disappointed.

With over 60% of companies in the S&P 500 having reported first quarter earnings results, the average earnings surprise has been 23.3% higher than expected, with revenue coming in 3.9% higher, as stated by Louis Navellier in today's podcast. He added that with soaring global demand, US exports and imports have been extraordinary. He can not remember an earnings season this strong. He also said that the Atlanta Fed is forecasting that 2nd quarter GDP will be at an annualized rate of 13.3%, and this after a greater than 8% growth rate in the 1st quarter.

On April 16th, Fed Governor Christopher Waller said that "the Economy is ready to rip. Unemployment is seen falling to the low 5% level by the end of the year". It appears that the country is not waiting until July 1st to get back to normal. Economic activity is getting back to normal now, and then some. Retail sales were up 10% in March. Industrial production was up 1.4% and manufacturing up 2.7%. Weekly jobless claims are now at their lowest level since last March.

With economic activity in the midst of an historic surge, can anything prevent stock prices from pushing higher? We got a possible answer to that question today, as Treasury Secretary Janet Yellen warned that the Fed might have to begin raising interest rates sooner rather than later in order to stem a possible rise in inflation. While the former Fed chief might have forgotten that she no longer is in charge of the Fed, the markets didn't like the mention of either higher rates or possible inflation. The S&P experienced a moderate sell-off while the Nasdaq dropped almost 2%. Inflation and rising interest rates have historically been one of the major causes of bear markets, so investors are understandably taking notice. It is true that commodity prices have been rising, as the global recovery gains momentum. However, it was just last week that the actual Fed Chairman, Jay Powell, reaffirmed that the Fed still had no immediate plans to begin to raise rates. And with the 10 year Treasury yield still at a low 1.6%, and the 10 year German Bund yield still in negative territory, it is not evident that inflation will be a concern anytime soon.

The stock market has been going sideways for a few weeks now. On April 16th, the S&P 500 finished at 4,185. It hit 4,187 on April 26th and 27th, hit a high of 4,193 yesterday, before falling back to 4,165 today. It is interesting that on April 13th, Sentimentrader.com summed up the market environment this way: "This is just more evidence of the tension we're facing now: a mostly pristine market environment with almost no internal risk signals triggering, versus stretched sentiment and lopsided positioning. It would be rare to see an immediate, large, and protracted decline from these conditions, just as it would be rare to see a large, sustained advance". As is typically the case during these situations, the bull has to scare investors off its back first, before resuming its ride higher.

During the same time that the S&P 500 has been treading water, the Nasdaq has pulled back about 3% from its April 16th high. The issue of which sector will lead the market higher seems to be one that will be with us for a while. Last week we saw blowout earnings from tech giants Apple, Google, Amazon, and Microsoft, yet that was not enough to propel their prices higher. If tremendous earnings reports don't result in price gains, maybe the market is looking for the reopening stocks to assume the leadership role. However, Steve Sjuggerud (StansberryResearch.com) reported in his 4/13 Review of Market Extremes, that the strong start to April for growth stocks that saw them rally for nine consecutive days points to more gains in the year ahead for them. He still feels that we are in a melt up environment for stocks, similar to 1999, when we saw technology stocks lead the way until the final top. *Jeff Feldman*

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