The Shobe Financial Group

Market Perspectives

3rd Quarter 2021

Market Outlook

There has been a lot of activity this quarter as the recovery from COVID-19 continues and Biden roles out more of his agenda. With that, digital currency is gaining more attention as it attempts to make its way into our market.

The Proposed Tax Changes

When Biden laid out his infrastructure priorities, proposed tax changes became a topic of conversation as a potential source of revenue for the initiative. While adjustments to state and local tax and personal taxes on the wealthy have been discussed, the most political support has been for a higher corporate tax rate around 25% (down from the proposed 28%). Still, the political dynamic is going to be the thing to watch as a higher corporate tax rate would mean a bigger blow to higher tax states.

Even though the uses for the money have bipartisan support, the scope of funding is still yet to be determined.

Inflation: The Common Questions and How it is Determined

Q: Why are prices going up if the Fed has said there is no inflation?

The Fed has agreed that inflation has risen. However, it is vital to note that the Fed's target for monetary policy may be different from your personal inflation rate.

The Fed makes changes to policy off inflation metrics. Their benchmarks are not affected by rising assets, housing, or energy either. The goal is to keep sustained changes in the level of prices and not so much on the price of single items or services. These prices are raised periodically all at one time rather than over time.

The consumer price index is over 2% now on a year-over-year basis and the Fed says transitory factors are the reason for the increase. These transitory factors include "base effects" due to low inflation last year during the height of the pandemic and "restart pressures" like supply chain and material shortages.

With these benchmarks, it is unlikely that the recent surge will change the Fed's stance on increasing interests rates.

Q: Why are food and energy not included ?

Food and energy prices are more volaille, so while the Fed does watch them they focus more on a core measure to read the inflation trend.

Q: What if inflation rises on a sustained basis?

If this were to happen, the Fed can constrict policy by raising short-term interest rates sooner than expected or through a reduction in the pace of monthly asset purchases. These moves can cause economic growth to slow.

What is Digital Currency?

Cryptocurrencies like Bitcoin, Ethereum, and Dogecoin are considered digital assets but their use as mediums of exchange are limited. They can be used to purchase a small portion of goods and services but have two big considerations: high associated transaction fees and possible dramatic changes in daily value. Some prefer using these as they improve efficiency and prevent user costs, but they do not offer protections like a bank account would.

Over the past several years, the Fed has been weighing the risks and benefits of digital currencies. They are expected to publish a paper this summer with their findings. That being said, cryptocurrencies are not going to replace the dollar but do expect them to stick around.

.Questions

If you have any questions about the proposed tax changes, inflation, or digital currency please reach out to our team.

Economic Snapshot

The US economic recovery should remain strong as the pandemic recedes, with a shift in consumer spending (from goods to services). Job growth should be robust, but the usual labor market frictions will be amplified by the speed of recovery. Higher inflation should be transitory, moderating as supply bottlenecks clear up, but pressures could be more severe and last longer, possibly leading to a sustained increase in inflation expectations. The Fed is not expected to raise short-term interest rates for sometime, but is likely to taper the monthly pace of asset purchases later this year or in early 2022.

	ECONOMIC INDICATOR	COMMENTARY
FAVORABLE	GROWTH	Led by a recovery in consumer services and supported by further vaccination progress, GDP growth is expected to be strong in the near term. Labor market frictions may be a constraint.
FAVORABLE	EMPLOYMENT	Nonfarm payrolls are still down about 9.5 million from the pre-pandemic trend, but we should see strong gains near term. Matching millions of unemployed workers to millions of available jobs will likely be challenging.
FAVORABLE	CONSUMER SPENDING	Consumer spending on services should continue to improve, while spending on consumer goods (which had been unexpectedly strong thorough the pandemic) is likely to moderate.
FAVORABLE	BUSINESS INVESTMENT	Capital goods orders and shipments exhibited a strong trend in early 2Q21, supported by business optimism. Business structures are expected to remain relatively soft, but should improve.
FAVORABLE	MANUFACTURING	Growth in new orders has remained strong. Supply chain constraints should continue to ease, helping to improve supplier deliveries.
FAVORABLE	HOUSING AND RESIDENTIAL CONSTRUCTION	Work-from-home has led to strong demand. Supply constraints have limited new construction and the pace of home sales. Higher prices have reduced affordability, so a pause may be in order.
FAVORABLE	MONETARY POLICY	Short-term interest rates may be raised a little earlier than previously expected, but not anytime soon. The pace of monthly asset purchases is likely to be tapered later this year or in early 2022.
FAVORABLE	FISCAL POLICY	Fiscal support will continue, but the impact on growth will fade over time. Lawmakers should eventually work to put the budget on a long-term sustainable trajectory, but not anytime soon.
FAVORABLE	REST OF THE WORLD	Still a mixed bag. The spread of the virus and the distribution of vaccines will vary widely.
NEUTRAL	INFLATION	Inflation has picked up, reflecting base effects (a rebound in prices that were depressed a year ago), restart pressures (supply chain bottlenecks and materials shortages), and higher prices of used vehicles. However, these pressures are expected to be transitory.
NEUTRAL	LONG-TERM INTEREST RATES	Bond yields normally rise in an economic recovery; however, Fed asset purchases should prevent long-term interest rates from rising too much.
NEUTRAL	THE DOLLAR	The trade deficit widened during the pandemic and in the initial recovery, putting some downward pressure on the dollar. While Fed tightening is far off, we may see an increase sooner, a positive for the dollar.

Raymond James, "The Evolution of Money" *Investment Strategy Quarterly*. Pg. 4-6, Web.

Raymond James, "The Road Ahead for Biden's Infrastructure Agenda: Impact on Spending, Deficits, and Taxes" *Investment Strategy Quarterly*. Pg. 7-9, Web.

Raymond James, "Q&A: Inflation" *Investment Strategy Quarterly* Pg. 14-16, Web.

Raymond James. "Economic Snapshot" *Investment Strategy Quarterly*. Pg. 17, Web.