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We saw another positive month for markets in May, although gains were more modest than in recent months. Large cap stocks in the S&P 500 index were up 0.7% in the month, bringing their year-to-date gains to 12.6%. Small cap stocks in the Russell 2000 were up 0.2% in May and 15.3% so far in 2021. International stocks in the MSCI EAFE index were up 3.6% for the month and 10.4% year-to-date. Emerging market stocks were also up 1.2% for the month and 6.0% year-to-date. Yields fell slightly this month, so the Barclays US Aggregate Bond Index was up 0.3% in May but still down -2.3% so far this year. The 10-year treasury yield was at 1.58% at the end of May compared to 1.63% at the end of April.

As pandemic related restrictions wind down, we are seeing a significant return of normal activity and a major boost in demand for products and services. Many companies are experiencing shortages due to pandemic related supply chain breakdowns. Shortages include everything from raw materials to microchips. The combination of higher demand and shortages is leading to meaningful inflation. The Fed has stated that it believes the inflation we are currently experiencing is transitory and will subside once we have returned to full capacity. Many economists have expressed skepticism and expect inflation to have a greater impact and be much more difficult to bring under control than the Fed has stated.

The second estimate of GDP growth in the first quarter remained at 6.4%. That growth occurred when much of the economy was still shutdown. Now that restrictions are being lifted and people are returning to work in large numbers, we expect second quarter economic growth to come in even stronger. Some large school districts are still not allowing students in the classroom, but this situation is changing as well. Most school districts have now indicated that they will be teaching in person beginning next fall. That will allow parents who have been staying home with their school age children to return to work as well.

The combination of a reopening economy and massive amounts of government stimulus are super-charging the recovery right now and probably through the end of this year. After that, stimulus will likely start to subside, and comparable data will become more challenging when comparing new data to the prior year (2022 compared to 2021). Also, government policy changes will begin to be implemented which will most likely include tax increases and a more restrictive regulatory environment, both of which create an economic drag. Since the market is a forward-looking mechanism, it is likely the market will begin to price in these expectations late this year.

Globally, the US is ahead of many other countries in terms of vaccinations and reopening. However, we are beginning to see improvements world-wide, including a lifting of international travel restrictions under certain circumstances. International stocks have underperformed for several years, and we may well be at the beginning of a period of outperformance for international stocks.

As always, we are available to discuss any questions or concerns you may have. Please do not hesitate to contact us.

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