CONWAY• JARVIS LLC
Investment Outlook

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Update

The Market Pendulum Swings on Conflicting Narratives

Just as the first half of the year marked a significant shift of investor capital away from the Growth stocks and into the Cyclicals, Q3 is shaping up as a potential unwinding of that shift. For months, the inflation narrative dampened traders' enthusiasm for the big-cap Growth favorites of the past year. That narrative has faded under the weight of an abrupt decline in treasury bond rates and a flattening of the yield curve. That's inspired *traders* to return to those stocks that traditionally enjoy expansive valuations during extended periods of low interest rates and flourished during the pandemic. The NASDAQ and S&P 500 are benefitting from this swing of the pendulum at the expense of the Cyclicals and small-caps. As you might expect, those indices were pushed to new record highs earlier this week courtesy of record advances by Amazon, Apple, Google, and other Tech favorites.

Wednesday's scheduled release of minutes from the Fed's June meeting hinted at the possibility of persistent inflation readings prompting a tapering of bond purchases earlier than predicted. That was first on our list of things to watch in our previous Update and could account for Thursday's sharp market selloff on the opening. Looking beyond this week, we're seeing anecdotal evidence of an increase in cases of the Delta Variant virus in under-vaccinated locales. If that becomes a trend as summer comes to an end, we could see headline risk weigh on the market. It's too soon to tell but fear of a seasonal surge in the virus could account for the return of traders to the stocks that performed so well during 2020.

At this time, we're seeing the Reopening continue to gain momentum and expect the recovery to continue to run hot through at least the next several quarters. As investors, we're happy to see capital move *within* the market rather than to the sidelines. That should produce respectable returns for portfolios *diversified* across both Growth and Cyclical sectors. There's a caveat. The recent sharp decline of the 10-year treasury yield that we've seen *usually* suggests that a lengthy period of monetary support is required in the form of low interest rates. That's at odds with the outlook for a continued robust recovery that raised fears of inflation and a policy shift from the Fed. It may be that the bond market has got it wrong or we're seeing the stock market trade focused only on the near-term prospects while ignoring the possibility of a seasonal virus surge and a pause in the Reopening down the road. We should soon have an indication as to which market is pointing in the right direction. Stay tuned.

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