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INVESTMENT COUNSEL

Coming Back

The global economy and financial markets are coming back from the impact of the coronavirus pandemic. For some key measures, the comeback is complete. With a big second-quarter advance, the level of real U.S. economic activity now has surpassed its pre-pandemic high. Many U.S. stock market indexes have posted all-time highs as well. Perhaps less welcome, inflation has reached rates not seen in many years. The rates of recovery for many economic and financial indicators are quite varied. As a result, confidence in outcomes from here remains a bit guarded. A review of some important factors can provide perspective for investing yet ahead.

PERSPECTIVE

U.S. industrial capacity never is fully utilized with a long-term average of 80%. The rate of utilization, however, provides indications of the potential for business to invest and hire and for subsequent levels of production. Chart I shows the pattern of capacity utilization over time. The notable secular decline reflects the much reported adverse impact of globalization on U.S. production. A decided improvement was under way until the pandemic drove utilization to a 53-year low. A substantial recovery has resulted, but a significant gap remains versus trend. Closing this gap could come with more jobs and moderate inflation. At the same time, globalization remains, even if altered by the pandemic in ways known or yet to be determined. How supply chain disruptions are addressed likely will determine in part the utilization ahead of the U.S. industrial capacity.

The pandemic's impact on employment and incomes has been notable, and changes in labor force dynamics continue to evolve. The shift to remote work remains while expectations for return to offices have risen. Some jobs likely have been lost permanently and many workers have weighed career options including early retirement. The growth of the overall economy depends on the participation of a greater force of productive workers. Chart II shows the rate of labor force participation over time relative to a long-term average of 64%. The secular rise up to 2000 is as clear as the subsequent decline thereafter. A new uptrend appeared at hand, only to be truncated by the pandemic. A rebound has occurred, but it will take the hiring of many more workers to renew the uptrend let alone come back to trend.

Higher inflation has come back and it is explainable by basic economics as shown in Chart III. Will this uptrend be relatively short-lived, i.e., "transitory" or will it be sustained? The direction from here will influence business, consumer, investor and policy decisions. Disruptions to the global supply chain have emerged as an important factor, reducing available goods even as a stimulus-induced recovery has lifted demand. While the impact of disruptions may abate, longer term adjustments likely are still in early considerations.

INVESTMENT IMPLICATIONS

Portfolio values are coming back from pandemic lows to the relief of investors generally. The comeback for individual markets and sectors has ranged widely. Nevertheless, if a portfolio was aligned properly with individual investor goals, horizons and risk tolerance pre-pandemic, perhaps only fine-tuning adjustments have been necessary. If not properly aligned earlier, misalignments likely have grown and should be addressed. Coming back is good; moving forward is better.

CHART I

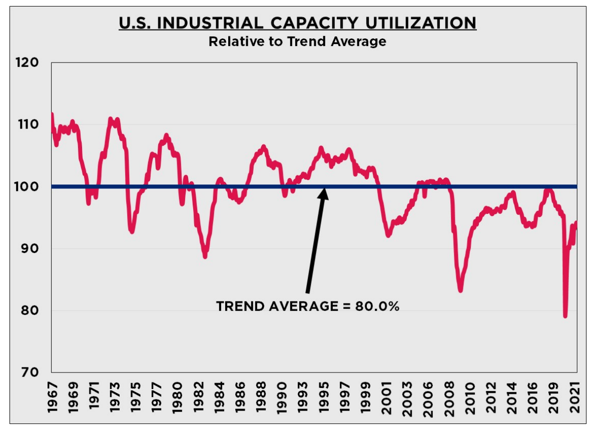

CHART II

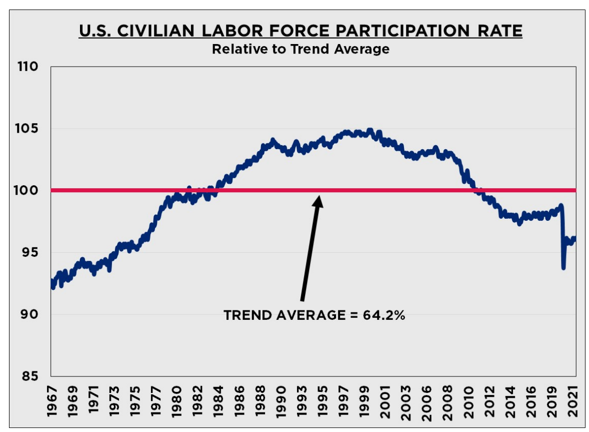

CHART III