October 15, 2021 The Regan Group, Inc. Volume 24.3
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Regans' Notes

Flat Quarter for Stocks & Bonds

The third quarter of 2021 began with optimism around strong corporate earnings, positive economic momentum, and consumers with cash to spend and places to go. Negative headlines received scant attention.

By mid-August, however, the Delta variant had changed the sentiment. Negative headlines garnered more attention from anxious investors. Some Wall Street strategists grew cautious and lowered growth forecasts, and some companies lowered future earnings guidance owing to higher costs associated with supply chain disruptions and labor shortages.

A review of the trailing twelve-month data reveals that all equity asset classes have risen since the reopening of the global economy. Unusually high returns for investors without a normal correction for an extended period of time resulted in a correction, in our opinion.

However, the quarter ended with the S&P 500 Index falling almost 5% in September, eliminating most of the earlier gains from July and August. As stories of supply chain disruptions and labor shortages dominated the news, investors began to fear that growth was slowing. Headlines of the Chinese government's regulatory crackdown on multiple industries also appeared to us to weigh on the markets.

Despite these short-term issues, we believe the recovery from the pandemic remains on track, acknowledging the road ahead could be bumpy as headline headwinds persist.

Capitalism Vs. Socialism

We think it is not possible to analyze the economy these days without focusing heavily on what government is doing. Between the Federal Reserve, fiscal policy, and COVID-related restrictions, little in our lives avoid governmental influences.

Economic and financial markets forecasting has become much tougher as government has grown, in sheer size, and also in power.

The history of the world as been a battle between two competing ideologies of how resources should be distributed: Capitalism and Socialism.

Capitalism distributes resources to the most productive use through markets and competition, while at the same time putting brakes on greed and selfishness. In order to accumulate resources in a capitalist system, you must provide goods or services for which someone else is willing to pay. If your cost of production is greater than what the market is willing to pay, you will not create much wealth. Or, if a competitor can provide the equivalent or better for a lower price, you will lose market share and therefore your wealth.

As a result, while it may be true that some people in a capitalist system become extremely wealthy, they do it by creating goods or services that people want and in a way that competitors have a difficult time copying.

Under Socialism, on the other hand, politicians of both parties distribute resources. They tax individuals who have been able to create income and wealth and then transfer those resources to their personal or politically favored causes or group, often while shutting down competition. Governments do not create wealth, they spend it.

Capitalism does not mean zero government and it does not mean anarchy. There are things that government can do that benefit all citizens without redistributing wealth or income. Public safety (police and fire), electrical grids, courts, sanitation, and national defense, for example. This government spending can generate huge benefits.

Unlike in the U.S., no one has built a $1 billion paper mill in Afghanistan. Why? It wouldn't last very long under the rule of the Taliban. The rule of law is necessary to encourage investment and create jobs.

It would be good if government could do these things as efficiently as the private sector, and we could make a case that many of these things should be competitively bid out, but government creates monopolies in order to defend power, sometimes for better, sometimes for worse.

In the end, because the government doesn't create wealth, it only redistributes it, the bigger it gets relative to the private sector, the harder it is to create more wealth in an economy.

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Government Spending Went Up, Real Growth Went Down

Source: First Trust Advisors, L.P.:

	20 Years Ended 12/31/00	20 Years Ended 12/31/20
U.S. Non-defense, non-interest government spending grew an average % per year % of GDP	**13.2%**	**15.9%**
U.S. Real GDP grew an average of % per year	**3.4%**	**1.8%**

The bigger the government gets, the slower the economy grows.

So far, the U.S. private sector has been able to grow, increase profits, and continue to lift wealth, although at a slower pace. We believe that's because of the power of entrepreneurs and the new technologies they create. Eventually, this may not be the case. Smothering capitalism has a cost. The open question right now is how much government and how much political allocation of resources Washington agrees on.

Leading Economic Indicators (LEI)

While the broad economy and the U.S. corporate earnings are not perfectly correlated, we believe there are strong linkages between the two. The LEI is comprised of 10 economic components whose changes are believed to lead changes in the broader economy, including manufacturing new orders and interest rate spreads, as well as data related to consumer expectations, credit, homebuilding, and employment.

The strength in trend of the LEI today, with all 10 indicators in positive territory, is a rare occurrence. It suggests to us these strong earnings trends we are experiencing will remain in place.

Our Mission

Achieve superior results for our clients by providing institutional level investment management and consulting services.

What We Do

We help clients realize their vision of the future with personalized investment planning.

Our client specific strategies use independent, full-time professionals to research and manage portfolios for long-term growth of assets.

Our services include:

- **Over 50 years of experience** in both up and down markets.
- Independent, objective advice from professionals with the expertise you need to help you achieve your goals.
- Investment strategies appropriate for **long-term, serious, core money.**
- Asset allocation strategies customized to fit clients' unique needs, risk tolerance, and time horizons.
- A disciplined investment process.
- Portfolios that attempt to provide **more consistent returns with reduced volatility** over time.
- **Seek out, screen, and hire** high-quality money managers to run portfolios of individual securities.
- **Ongoing review** of the chosen managers' process, personnel, and investment decisions and report their performance quarterly.
- Replace managers when necessary.

Clients have trusted us for decades to provide their investment services.

We continue to grow and appreciate your introductions to friends and family. Our target markets are clients just like you – individuals, foundations, endowments, retirement plans, and corporations.