Stocks head lower as Delta variant concerns grow

On the day
Growing concerns the Delta coronavirus variant could slow the global economic recovery have been percolating for weeks. Today, that concern seemed to be the “go-to” excuse for stock prices to head lower. Cyclical value areas tied to travel, leisure, hospitality, and reopening trends sold off more aggressively on the day. These areas have also turned into market laggards over the last month, as investors start to contemplate a market environment after the likely peak in U.S. economic and corporate profit growth during the second quarter.

Notably, the S&P 500 Index hasn’t seen a significant drawdown all year, despite weakening technical factors over a number of weeks. Yet, even following today’s decline, most major U.S. stock averages sit less than 4% away from their all-time highs. Bottom line: Although the Delta variant could delay or slow the return to normal across major economies (including the U.S.), its impact on growth should be minimal over time. While the risk for unvaccinated individuals is more significant, we do not believe consumer/business behaviors will change much based on the Delta variant and effective/available vaccines. This should help limit the negative impact on economic growth, in our view.

Committee View
Turning to the fundamentals, second quarter earnings season kicks into high gear this week. Expectations for corporate earnings increased leading into the reporting season, which leaves companies with a more challenging environment to “wow” analysts and investors. And while there is still room for companies in aggregate to surpass analyst Q2’21 profit estimates, stock prices may already reflect they likely will do so. Also, market crosscurrents could pick up over the next few weeks, as company outlooks for the second half are analyzed and digested by investors. Yes, the pace of growth in the U.S. is likely to slow across a range of areas in the back half of the year. However, growth should remain above longer-term trends over the next few quarters. And against a backdrop of very easy monetary conditions, we believe any short-term dislocations across stock prices should be considered a buying opportunity.

Though we continue to believe the U.S. economy is in the early stages of a recovery, it’s not exactly at the starting line anymore. We believe the recovery phase in the U.S. likely started in earnest in the late spring/early summer of 2020. Importantly, business cycles do not ring alarm bells when there is a shift from one phase to another. In our view, investors should focus on quality companies across cyclical industries that can demonstrate more predictable revenue streams, particularly in an environment where growth is above trend but slowing. Also, if market pullbacks develop across high-growth industries, like Technology, we believe investors should use the opportunity to acquire quality companies that can grow revenue in a changing economic environment.

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Chief Market Strategist

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Fixed Income Strategy

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Equity Research

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Asset Allocation

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Senior Director
Manager Research

Dan Garofalo
Director
Equity Research

Mark S. Phelps, CFA
Director
Manager Research

Frederick M. Schultz
Director
Equity Research

Cedric Buermann Jr., CFA
Quantitative Analyst
Asset Allocation

Ameriprise Financial
1441 West Long Lake Road, Suite 250, Troy, MI 48098
For additional information or to locate your nearest branch office, visit ameriprise.com

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