

Market Themes

In our last newsletter we gave our mid-year update. That newsletter reviewed several themes from the April newsletter that we thought would impact the markets this year. That newsletter and all our past newsletters can always be found on our website¹. Back in April we thought interest rate increases would create a tough environment for the bond market; and as of September 30th, we have seen the major bond indices negative for the year. We thought that the equity markets would have a good year and we had seven straight months with positive returns for the S&P 500 before a negative month in September. The S&P 500 hit an all-time high 50 times this year.

One of the biggest concerns for investors has been how to generate income in a near zero interest rate environment. If interest rates continue to rise like we anticipate, bond prices will do down further. With credit spreads near their lows, higher interest rates will most likely lead to flat or negative returns in fixed income in the future. Paragon has been utilizing callable yield notes to generate income. Please contact your wealth manager at Paragon to learn more about callable yield notes and how they may fit in your portfolio.

All nine of the major themes outlined in our mid-year review remain major factors for the markets going forward. Some new themes have popped up over the last quarter we will discuss in this newsletter.

¹ <https://www.paragoncap.com/about-us/>

- 1) Supply Chain – prior to this year, many consumers didn't think about how the items they bought got to the store shelf. We took for granted that if we needed a car, the lots would be full, if we need a couch then there are plenty of furniture stores to choose from. Disruption caused by COVID has created many problems in most industries. We could write pages of examples, but we will highlight three that we feel are relevant to your life and portfolios.
 - a. Auto industry – the semiconductor shortage is one of the most talked about stories of the year. Thousands of cars and trucks sit in parking lots ready to be sold, but missing semiconductor chips. The chips are primarily made in Taiwan and plants have been shut down, shipping containers delayed, and ports backed up. The government is discussing investments and incentives to build additional semiconductor capacity in the U.S. We believe holdings in Intel (INTC) will benefit from the additional funds and future capacity in the U.S.
 - b. Retail – one of Paragon's stock holdings, Nike (NKE), announced during their earnings call that they are having difficulty getting merchandise to sell. Over 80% of shoe factories in Vietnam are closed and so are over 50% of apparel factories. Nike makes over 50% of their shoes in Vietnam. We believe the market will look through any potential supply chain issues for Nike as investors focus on the benefits of the increase in direct-to-consumer business.
 - c. Labor – throughout the year, we have all seen "For Hire" signs everywhere we go. Starting wages have risen and signing bonuses are standard. In their recent call, Costco (COST) cited port delays, container shortages, covid disruptions, shortages of various components, raw materials and ingredients, labor cost pressures and truck driver shortages.
- 2) Space Travel – in the last 3 months we have seen the space race move from the US/Soviet Union to the race of billionaires. Both Richard Branson and Jeff Bezos both went to space with civilians. Currently this is a fun story to watch as we see the privatization of space travel. We are monitoring the advancement for future investment opportunities.

- 3) Crypto Currencies – crypto currencies like Bitcoin are not going away. However, China banned all crypto related transactions. This is not new, in 2017, China outlawed all crypto exchanges. China’s main grievance is that crypto is unregulated by a higher authority. Some argue that crypto helps facilitate illegal activities like money laundering and allows money to leak out of the country without documentation. Crypto can also be found as part of our next theme...
- 4) Ransomware – we have discussed ransomware in past newsletters. Since May 2020 there has been over 40 publicly reported attacks against food companies. The headliner was in early June when the largest meat producer was shut down due to a cyber-attack. Colonial Pipeline, the largest fuel pipeline on the east coast, carrying half of the east coast natural gas and was attacked with a \$4.4 billion bitcoin demand. Just in 2020 alone, 350,000 crypto currency payments to ransomware were made, three times the amount in 2019.
- 5) Debt Ceiling/ Infrastructure Bill – we saw congress come together in the 11th hour to kick the proverbial can down the road, approving a federal debt ceiling increase to keep the government open until at least early December. As of the end of the 3rd quarter, the two infrastructure bills remain a major topic in Washington. Both parties (Republicans & Democrats) agree on part 1 (\$1 trillion for traditional infrastructure like roads and bridges). The stumbling block is the attached part 2. Part 2 was originally proposed as a \$3.5 trillion bill focusing on what some consider non-traditional infrastructure, many believe this bill will be negotiated to levels closer to \$2 trillion. First the Democrats need to agree on the bill, then convince the Republicans. This affects the markets because to pass a bill, it needs to be paid for. We have heard many rumors of tax increases, both on the wealthy and on corporate America. We said in April and July that we thought it was doubtful that many of those would actually get passed and that continues to be our thought. While there will be impacts from tax increases, the market hates uncertainty so we believe markets will remain volatile. We believe once the impacts are known, there will not be a major impact on major index levels.

- 6) Weather – even though this did not affect the markets much, Paragon has clients in over 30 states and our thoughts are with anyone impacted by Hurricane Ida in Louisiana, wildfires in California and Lake Tahoe, flooding on the east coast and other weather-related incidents throughout the country.
- 7) Politics – we might have just scared you with that word! As always, we do not discuss politics unless directly affecting the markets. We will point out two major events that have occurred since our last newsletter. The first is the withdrawal from Afghanistan, ending a 20-year war, in which many soldiers gave their lives in the pursuit of defending our country and trying to keep terrorist attacks at a minimum. The other is the current House Select Committee investigation of the Jan 6th attack on the Capital. We are not sure if this will impact the 2022 elections and the markets, but we will be closely monitoring this and all events in our Capital.
- 8) COVID – one cannot write a newsletter without discussing COVID. Our take on this newsletter will be market related. Vaccinations are becoming mandatory for employees across the country. Pushback from employees will make the already difficult labor market worse, and backlogs and supply chain issues worse. This is expected to be a major theme for the 4th quarter.
- 9) China and international policy – our last theme is another one that looks forward. Evergrande, one of the largest real estate companies in China, is slowly collapsing under the weight of an over levered balance sheet. We will continue to monitor the situation, but we currently believe any impact will be contained by the Chinese government.

A variety of large U.S. based companies face increased scrutiny by regulators inside and outside of the U.S. Apple (AAPL) has recently been the subject of a variety of issues from limiting the profitability of in-app purchases in Korea to the EU mandating the use of a single charger for all cell phones (eliminating the lightning charger for Apple). As with all the concerns we highlighted above, we will continue to monitor the situation and make changes to portfolio holdings as appropriate.

This year has been interesting to say the least. We are extremely grateful for all the trust and support our clients have shown us over the past two years dealing with the current pandemic. We miss our in-person meetings, we have been having some meetings in our offices and it is great to see people face-to-face. We traveled a little earlier in the year before the Delta variant shut that down for the last several months. We look forward to seeing everyone in person soon, in the meantime we have enjoyed the benefits of technology with video conferencing and conference calls. We want to meet with all of you however you feel safe. We are happy to meet in person, video, phone, or emails.

Update to Paragon's Security Policy

We take your security very seriously. We have instituted new security protocols that will require verbal confirmation of all money movements. If you email or message us to move money from your account to your bank, we will be calling to verify. We understand this creates an additional step in the process and may be viewed as an inconvenience, but it is for your security!

How to stay informed

For up-to-date news and thoughts from Paragon, plus interesting articles on topics like saving and investing for children, taking care of elderly parents and their finances and other timely topics, we encourage you to follow us on LinkedIn and/or Facebook. We have company pages for both and appreciate your liking and/or following us.

- Paragon LinkedIn: <https://www.linkedin.com/company/paragon-capital-management-llc/?viewAsMember=true>
- Paragon Facebook <https://www.facebook.com/Paragon-Capital-Management-llc-352968418169300>
- Craig Novorr LinkedIn <https://www.linkedin.com/in/craig-novorr-1a8a822/www.paragoncap.com>

Also, please share your experiences with friends and family; we love the opportunity to help those you know with their financial success.

Even though Paragon's offices remain temporarily closed due to COVID-19, we are all working from home and staying in contact with each other daily. We are available to meet with clients at our office by appointment only and are also available to schedule account reviews via video or phone conference.

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