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Amadeus Wealth Alternatives
Your Compass to Alternative Investments

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In this week's recap: Markets react positively to infrastructure proposals; S&P 500 rises above 4,000 for the first time.

Weekly Economic Update

Presented by Ed Papier, April 5, 2021

THE WEEK ON WALL STREET

Overcoming a rocky start, stocks rallied into the close of a holiday-shortened week of trading as technology shares staged a powerful recovery and investors reacted positively to President Biden's infrastructure spending proposal.

The Dow Jones Industrial Average gained 0.24%, while the Standard & Poor's 500 picked up 1.14%. The tech-heavy Nasdaq Composite index rose 2.60%. The MSCI EAFE index, which tracks developed overseas stock markets, slipped 0.43%. [1,2,3]

S&P 500 HITS 4,000

Monday opened with two banks reporting they face losses due to the default of a small U.S. hedge fund. That news, combined with rising yields, higher new cases of COVID-19, and a public warning of new virus variants, started the week off on an unsettled note. [4]

Despite the shaky start, upbeat economic reports helped spark a rally that was paced by gains in the technology sector. The market also reacted positively on Wednesday to the introduction of a $1.9 trillion infrastructure proposal.

Stocks closed out the week with an exclamation mark, with the S&P 500 Index closing above 4,000 for the first time. [5]

HEDGE FUND WOES

Last week's trading opened on news that a U.S.-based investor was forced to unwind positions in multiple Chinese technology companies and American media holdings.

A number of large banks saw their share prices fall early in the week, reflecting concerns about their exposure to the hedge fund losses. Meanwhile, investors grappled with whether this was a one-off event or the opening act for additional hedge fund issues. As the week wore on, it appeared the hedge-fund issues were an isolated event. [4]

THE WEEK AHEAD: KEY ECONOMIC DATA

Monday: Factory Orders.
Tuesday: Job Openings and Labor Turnover Survey (JOLTS).
Wednesday: Federal Open Market Committee (FOMC) Minutes.
Thursday: Jobless Claims.

QUOTE OF THE WEEK

"Politics: A strife of interests masquerading as a contest of principles: The conduct of public affairs for private advantage"

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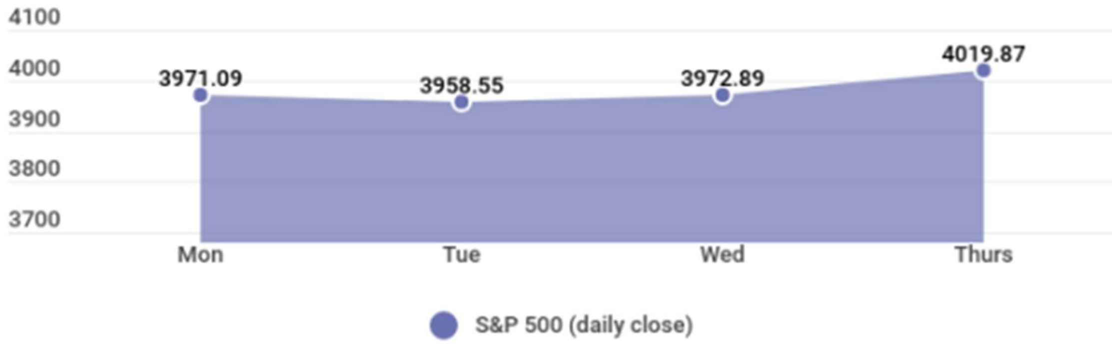
Market Index	Close	Week	Y-T-D
DJIA	33,153.21	+0.24%	+8.32%
NASDAQ	13,480.11	+2.60%	+4.59%
MSCI-EAFE	2,208.32	-0.43%	+2.83%
S&P 500	4,019.87	+1.14%	+7.02%



	Treasury	Close	Week	Y-T-D
	10-Year Note	1.69%	+0.02%	+0.76%

Sources: The Wall Street Journal, April 1 2021; Treasury.gov, April 1, 2021
Weekly performance for the Dow Jones Industrial Average, Standard & Poor's 500 Index, and NASDAQ Composite Index is measured from the close of trading on Friday, March 26, to Thursday, April 1, close. Weekly performance for the MSCI-EAFE is measured from Friday, March 26, open to Wednesday, March 31, close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

OF NOTE

We are currently witnessing a major disconnect between markets and the economy, and the greatest financial bubble ever. The disconnect originates from the relentless combination of monetary policies without limits feeding fiscal policies without limits, in what is known as Modern Monetary Theory (MMT), or Magic Money Tree, a major force distorting markets and valuations. MMT is just the latest expression of a dynamic that has dominated global macro markets over the last decade, which can better be described as "the transformation of risk-free interest into interest-free risk" that, amongst other implications, has resulted in artificially low - even negative - interest rates and artificially low credit spreads that have fueled Bubbles too Big to Fail.

The case of "pre-existent fragility" was exposed by Covid, a shock without precedents. The response from Central Banks and Governments via MMT is also another shock without precedents in terms of size, speed, and scope, that dwarfs the monetary and fiscal response to the Global Financial Crisis of 2008.

In addition to distorting valuations, MMT has reinforced the narrative and belief in the "Central Bank Put" which assumes that "don´t worry about risk, mummy will come to rescue us", which has been a self-fulfilling prophecy as central banks feed reckless behavior that becomes systemic and forces them to step in, which in turn trigger a "Buy the Dip" mentality, alongside "Fear Of Missing Out", which are very reminiscent of the 2001 mania and Dot Com bubble.

Unfortunately, MMT does not solve problems, rather simply, it:

Delays problems via more debt ("kicking the can down the road")
Transfers problems via "beggar thy neighbor" currency wars
Transforms problems from "bubbles too big to fail" into inflation, and
Enlarges problems, creating systemic risk, which ultimately brings us back to 1) as "mummy Fed and daddy US Government" are forced to come back to the rescue.

While there is a growing recognition of the problem of ballooning US debt, most participants are ignoring the problem. Higher yields in US Treasuries (which have now surpassed the spike during 1Q20) have not resulted in stress in either equity nor credit markets. Part of the reason is that, unlike in 1Q20, when equity valuations and fixed income were collapsing at the same time, the recent sell-off in US Treasuries has been more than cushioned by strong gains in equities, and thus 60/40 balanced portfolios remain balanced, at least for now…

Despite the recent increase in inflation and inflation expectations above the historical ceiling of 2%, the Fed is in Powell´s words, "not even thinking higher interest rates", confirmation we are in a new paradigm of higher inflation and lower interest rates, which can be summarized as "the transformation of Bubbles Too Big to Fail into Inflation, (or perhaps more worryingly, Stagflation)" which is the only way out of this mess that Central Banks have created.

The debate between inflation vs deflation is widely open. While there are many deflationary forces in the system (unemployment, weak economic activity, technology, demographics, overcapacity, malinvestment), there is one major force single-handedly offsetting them all: Money Printing. Don´t fool yourself. Inflation is here and rising. Inflation is not about asset prices going up, inflation is about the value of the money going down.

The Covid shock from 2020 is now entering its third wave and is not yet completely resolved. The pain is being patched by money printing and debt, but you cannot solve solvency problems with liquidity.

The current consensus and complacent expectation is that the Fed has everything under control ("the Central Bank Put"). Many disagree. The main problem is that the size of the problem is getting larger and larger with each iteration (current bubbles in 1Q21 are much greater than in 4Q18).

Should the Tesla and Crypto Emperor have no clothes, the collapse is not just a zero-sum-game between "early movers" and "greater fools", but also a major distortion to the markets as it was the case in 2001. Just look at the recent craze in "Penny Stocks", where "tick-tock financial influencers" are tipping retail investors how to spend the next Stimulus check to make 10x in 1 week. Yes, reality beats fiction.

Overall, we believe we're in for a bumpy ride and more printing and debt that will be very supportive for real assets in general. Similar to the collapse of the 2001 dot com bubble, the path ahead will be bumpy. The bubbles will be tested and exposed via higher levels of volatility, which will invariably result in more money printing, more debt, and eventually more inflation. [6]

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Know someone who could use information like this?
Please feel free to send us their contact information via phone or email. (Don't worry – we'll request their permission before adding them to our mailing list.)

CITATIONS:
1. The Wall Street Journal, April 1, 2021
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