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Amadeus Wealth Alternatives
Your Compass to Alternative Investments

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In this week's recap: Vaccinations and declining case numbers result in economic optimism; Fed Chair says no change for now.

Weekly Economic Update

Presented by Ed Papier, February 15, 2021

THE WEEK ON WALL STREET

Stock prices inched higher last week amid declining COVID-19 cases, a pick-up in vaccinations, and progress on a fiscal relief bill.

The Dow Jones Industrial Average gained 1.00%, while the Standard & Poor's 500 rose 1.23%. The Nasdaq Composite index climbed 1.73% for the week. The MSCI EAFE index, which tracks developed overseas stock markets, added 1.80%.[1,2,3]

STOCKS POST GAINS

Stocks powered higher to begin the week, buoyed by rising confidence in economic recovery and the potential for another round of fiscal stimulus. Small cap stocks continued their 2021 rally as investors looked for out-of-favor names that might benefit from an economic rebound.

Stocks traded in a tight range through the remainder of the week. Investors appeared to digest current stock price valuations, wondering if the market had already "priced in" the optimism of a rebounding economy.

On Wednesday, Fed Chair Powell gave assurances that the Fed's rate policy would remain unchanged for the foreseeable future. Some fear that inflation may pick up with broader reopenings and additional fiscal stimulus.[4]

On Thursday and Friday, stocks drifted mostly higher in quiet trading, managing to set some new all-time highs.[5]

ECONOMIC EXPECTATIONS RISING

A survey by The Wall Street Journal showed increasing optimism among economists about economic growth for this year.[6]

Among the survey's findings, economists, on average, now expect the economy to expand by 4.9%, an increase from their average estimate of 4.3% last month. They are, however, somewhat less sanguine about employment as they now expect 4.8 million jobs to be added this year, versus an earlier expectation of 5.0 million.[6]

Economists are forecasting accelerating inflation as a consequence of economic growth and fiscal stimulus, but believe that there is only a 17.5% probability of an economic downturn in the next 12 months, an improvement from its 21.2% risk estimate in January.[6]

THE WEEK AHEAD: KEY ECONOMIC DATA

Wednesday: Retail Sales. Industrial Production. Federal Open Market Committee (FOMC) Minutes.

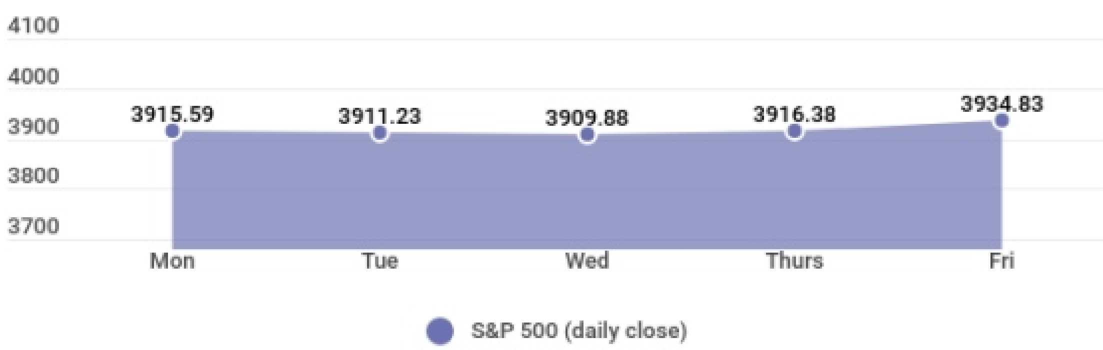
Thursday: Jobless Claims. Housing Starts.

Friday: Existing Homes Sales. Purchasing Managers Index (PMI) Composite Flash.

QUOTE OF THE WEEK

"When his aunt Louisa asked him in his last weeks if he had made his peace with God, Thoreau responded, "I did not know we had ever quarreled"

Market Index	Close	Week	Y-T-D
DJIA	31,458.40	+1.00%	+2.78%
NASDAQ	14,095.47	+1.73%	+9.37%
MSCI-EAFE	2,221.46	+1.80%	+3.44%
S&P 500	3,934.83	+1.23%	+4.76%



	Treasury	Close	Week	Y-T-D
	10-Year Note	1.21%	+0.04%	+0.28%

Sources: The Wall Street Journal, February 12, 2021; Treasury.gov, February 12, 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, February 5, to Friday, February 12, close. Weekly performance for the MSCI-EAFE is measured from Friday, February 5, open to Thursday, February 11, close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

OF NOTE

You know in your heart of hearts you have never taken this level of risk, and you never thought you would...Jeremy Grantham, January 22, 2021

To get a sense of how extreme valuations have become after a decade of deranged monetary activism, the ratio of U.S. total equity market capitalization to GDP is instructive. The present ratio is 2.63. The historical norm – not the low, the norm – is 0.78, about 70% below the current level.

The immediate problem is that the process of Fed-induced yield-seeking speculation and demand-driven issuance of low-grade securities has now been wholly reproduced, but in magnified form. The only difference is that the objects of speculation involve common stocks, leveraged loans, and corporate debt with "covenant lite" features. Investors and policy makers seem to have little grasp that all of this has happened before, and an even weaker grasp of what is likely to happen next.

Sadly, Federal Reserve policy makers remain blind to their own role in creating repeated bubbles, crashes, and financial crises, focusing instead on wildly activist monetary policies that have little correlation with actual subsequent economic outcomes, beyond what can be explained by pure mean-reversion. The Fed is like a mechanic that loosens the wheel bolts on people's cars because he thinks it will improve their mileage, then shrugs "we don't have the tools" to keep their cars from swerving into the ditch. Here's a tip. Maybe stop loosening those wheels. Stop putting everyone at risk from experimental fixes that aren't in the manual and produce consequences that you don't comprehend. The swerving and crashes are your own doing.

One of the charts at this link: https://www.hussmanfunds.com/comment/mc210201/ shows how investors were pricing the "good stocks" in the S&P 500 as of January 22. Each line represents a decile (10%) of the S&P 500, ranked by price/revenue ratios. Among the stocks in the top valuation decile at the 2000 market peak, the median drawdown loss by October 2002 was about 80%. Yet many stocks in the broad market were actually reasonably valued from a historical perspective even at the 2000 market peak. In recent weeks, that top valuation decile has eclipsed its 2000 peak. The difference from 2000 is that every other decile just hit the highest level in history as well.

Hussman's estimate of the likely average annual 12-year average nominal total return for a conventional passive investment mix invested 60% in the S&P 500, 30% in Treasury bonds, and 10% in Treasury bills is singularly the worst investment outlook in U.S. history: -2.15%.[7]

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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.)

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The forecasts or forward-looking statements are based on assumptions, may not materialize, and are subject to revision without notice.

The market indexes discussed are unmanaged, and generally, considered representative of their respective markets. Index performance is not indicative of the past performance of a particular investment. Indexes do not incur management fees, costs, and expenses. Individuals cannot directly invest in unmanaged indexes. Past performance does not guarantee future results.

The Dow Jones Industrial Average is an unmanaged index that is generally considered representative of large-capitalization companies on the U.S. stock market. Nasdaq Composite is an index of the common stocks and similar securities listed on the Nasdaq stock market and is considered a broad indicator of the performance of technology and growth companies. The MSCI EAFE Index was created by Morgan Stanley Capital International (MSCI) and serves as a benchmark of the performance of major international equity markets, as represented by 21 major MSCI indexes from Europe, Australia, and Southeast Asia. The S&P 500 Composite Index is an unmanaged group of securities that are considered to be representative of the stock market in general.

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CITATIONS:

1. The Wall Street Journal, February 12, 2021
2. The Wall Street Journal, February 12, 2021
3. The Wall Street Journal, February 12, 2021
4. Board of Governors of the Federal Reserve System, February 19, 2021
5. CNBC.com, February 12, 2021
6. The Wall Street Journal, February 11, 2021
7. www.hussmanfunds.com/comment/mc210201/