Market Commentary

Greetings!

MARKET COMMENTARY

Asset class returns during the month of January were very consistent with our broad economic views that the U.S. is in the midst of reflationary dynamics which suggests the year-on-year rates of change in growth AND inflation are accelerating from March-2020 lows.

Most of the month was generally positive for those long equities as positive economic data and falling volatility (as measured by the CBOE Volatility Index ("VIX") resulted in moderate gains across most equity exposure. The last two weeks in January reversed course due to a) weaker economic data b) Johnson and Johnson's (Ticker JNJs vaccine difficulties c) the rampant speculation occurring in GameStop ($GME) equity and options. These events drove the VIX from "green light zone" to "red" in one week as the index increased 45% from 22.75 to 33.06.

In the near term, there are concerns that re-opening related growth and resulting inflation could propel longer term interest rates to levels incongruent with an economy suffering from high unemployment, poor demographics, and alarming debt levels (125% National Debt/GDP). Reported earnings from U.S. corporations will be extremely robust on a year-over-year growth basis for 1HCY21 due to a very low base level created by COVID-19. The "true" picture of the U.S. economy will be revealed in the summer of 2021.

At this point, leading economic indicators are beginning to show decelerating growth and inflation which could signify volatility for U.S. stocks already trading at record high valuation multiples and extremely exuberant retail and institutional sentiment.

WHAT'S NEXT?

Without doubt, the current market excesses, irrational exuberance, and market bubbles are a legitimate source of concern. The primary question seems to be: How will the Federal Reserve balance rising growth and inflation with structural economic problems in the country? Janet Yellen (now Treasury Secretary) began raising interest rates in late-2018 to cool-off a strong economy which resulted in a massive sell-off in December of that year. Jay Powell (current Fed Chair) has indicated that the U.S. economy is not ready to sustain reductions in Quantitative Easing (Fed is printing $120B/mo), nor increasing interest rates. However, if current inflation accelerates to a higher threshold; the Fed may be forced to raise rates before the economy has fully healed.

Perhaps, the key market metric to focus on is the ten-year Treasury rate. Given the probability of a large $Trillion fiscal package, vaccine distribution picking up steam and, post-holiday COVID hospitalizations and deaths in retreat, the rise in the ten-year treasury yield now appears to be the market's barometer for Fed action.

The Federal Reserve continues to label current inflationary dynamics as "transitory" which allows easy monetary policy to continue. This appears to be the most likely policy for the next 6-12 months as the U.S. recovers from COV-19 despite inflationary pressures. Easy monetary policy as historically been a boon for U.S. growth stocks as lower interest rates enable higher stock valuations. That said, how long will investor's faith remain in the Fed's ability to support stock prices during the next leg down of the U.S. profit cycle? We are not convinced of either side of the argument right now, but the mantra "Don't Fight the Fed" has traditionally been a prudent investment strategy.

As always, if you have any questions or would like to discuss your accounts or financial situation further, please call your advisor directly or email us at clientservices@benchmarkfinancial.info. Please visit our website at www.benchmarkfinancial.info for more information on our planning services.