Market Update

January 11, 2021

Unprecedented….

- Unprecedented events rocked the U.S. Capitol last week. Ultimately, Congress certified Joe Biden as the next President and President Trump agreed to a peaceful transition of power.
- The Democrats took control of the Senate by prevailing in both Georgia runoff elections. With all three levels of government now in the hands of Democrats, President-elect Biden will have a better shot at implementing his agenda.
- Economic data was a mixed bag. Vehicle sales ended 2020 on a solid footing and ISM indexes remained well in expansionary territory. However, job creation came to a halt in December, with payrolls falling by 140k.

Along with personal resolutions, the New Year tends to usher in a sense of hope. But, as the last few days have demonstrated, simply flipping the calendar does not guarantee a fresh start. Many of the issues that made 2020 a challenging year linger on. The health crisis is (still) front and center, with positive cases and hospitalizations surging to all-time highs.

Meanwhile, the unprecedented events at the U.S. Capitol last Wednesday shocked the country and the world. Still, in terms of the economic outlook, the biggest development on the political front was that Democrats narrowly took control of the Senate by prevailing in both Georgia runoff elections. With all three levels of government now in the hands of Democrats, Joe Biden will have a better shot at implementing his agenda.

The Biden election platform promised an ambitious spending agenda, funded by higher taxes. A thin Senate majority will pose a challenge to several elements on the list, but increased spending to support the economy through the pandemic appears likely. Tax changes, such as the planned tax hikes on corporations and high-income individuals, appear less likely. While they can be rolled through in the budget reconciliation process with a simple majority, more conservative-leaning Democratic Senators would have to be on board, making it a harder sell than temporary supports to bridge the economy while vaccines continue to be rolled out.

The S&P 500 is near all time highs. Big Tech and Growth lead the way for 2020. Many on was street are looking to a change of the leadership to more Value oriented stocks with Big Tech as well for 2021. This anticipated rotation is due to Biden administration policies, COVID-19 vaccine rollout, and Federal Reserve policy. Gold seems to be starting a slight downward trend as bond prices seem to be trending down slightly.

Overall, the combination of vaccinations and increased spending, suggests that 2021 should be a much better year than the one we left behind. Markets certainly seem to be in tune with this view, with risk assets shrugging off this week's turmoil in the Capitol. That said, we are not out of the woods yet and there could be additional bumps along the road. New COVID-19 variants, which appear to spread more easily, pose an added downside risk. The new administration certainly has its work cut out for it.

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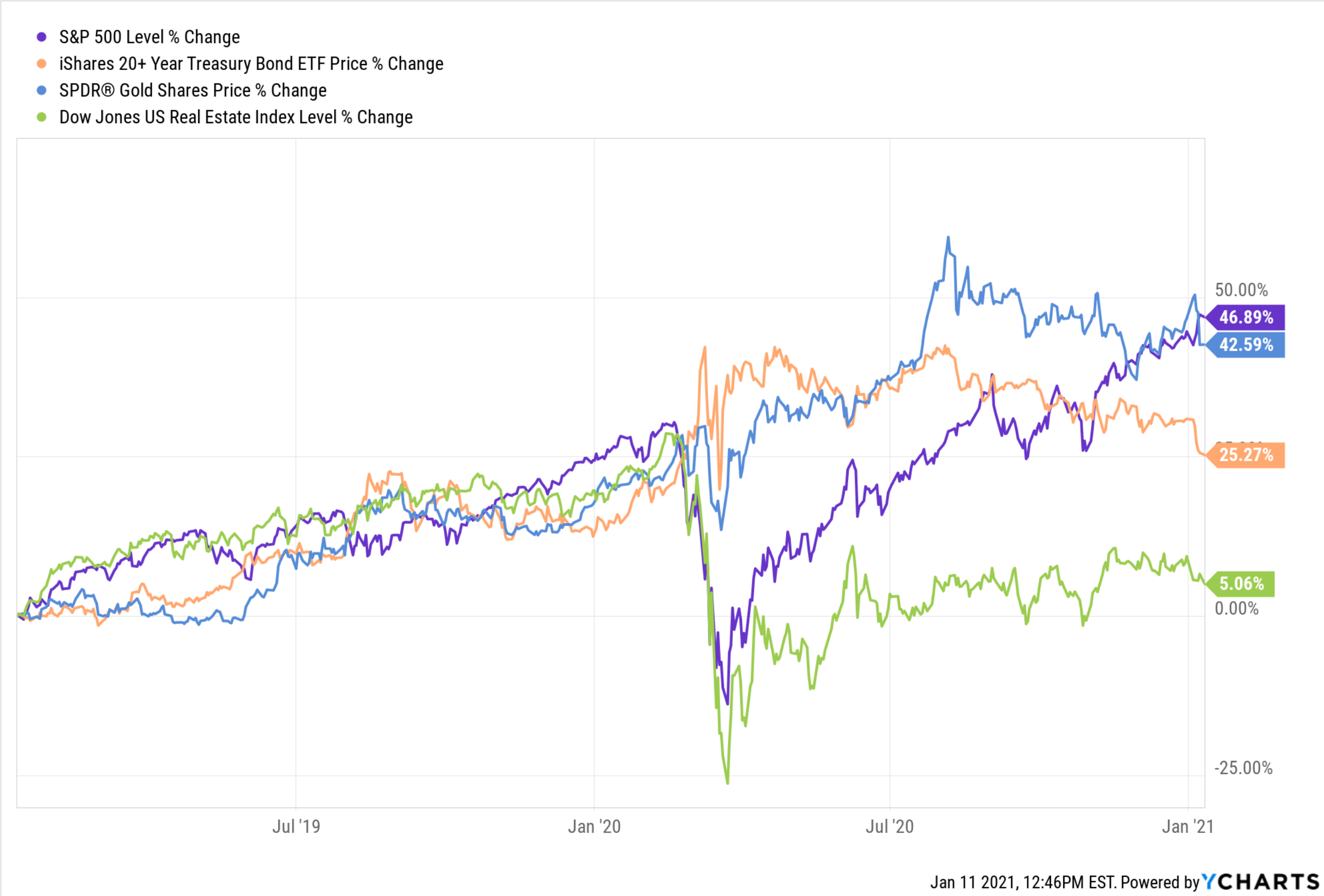

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Long term treasury yields ticked up a little since last month although the interest rate environment remains low. The shape of the yield curve remains positively sloped which is a good indication that the Federal Reserve's policies are working and helping financial markets. Inflation remains low while the employment picture is strong in some areas and seeing continued weakness in others such as hospitality and leisure. Successful re-opening of state economies is at the fore front and there are continued concerns about growing case numbers in hotspots like Los Angeles and San Francisco.

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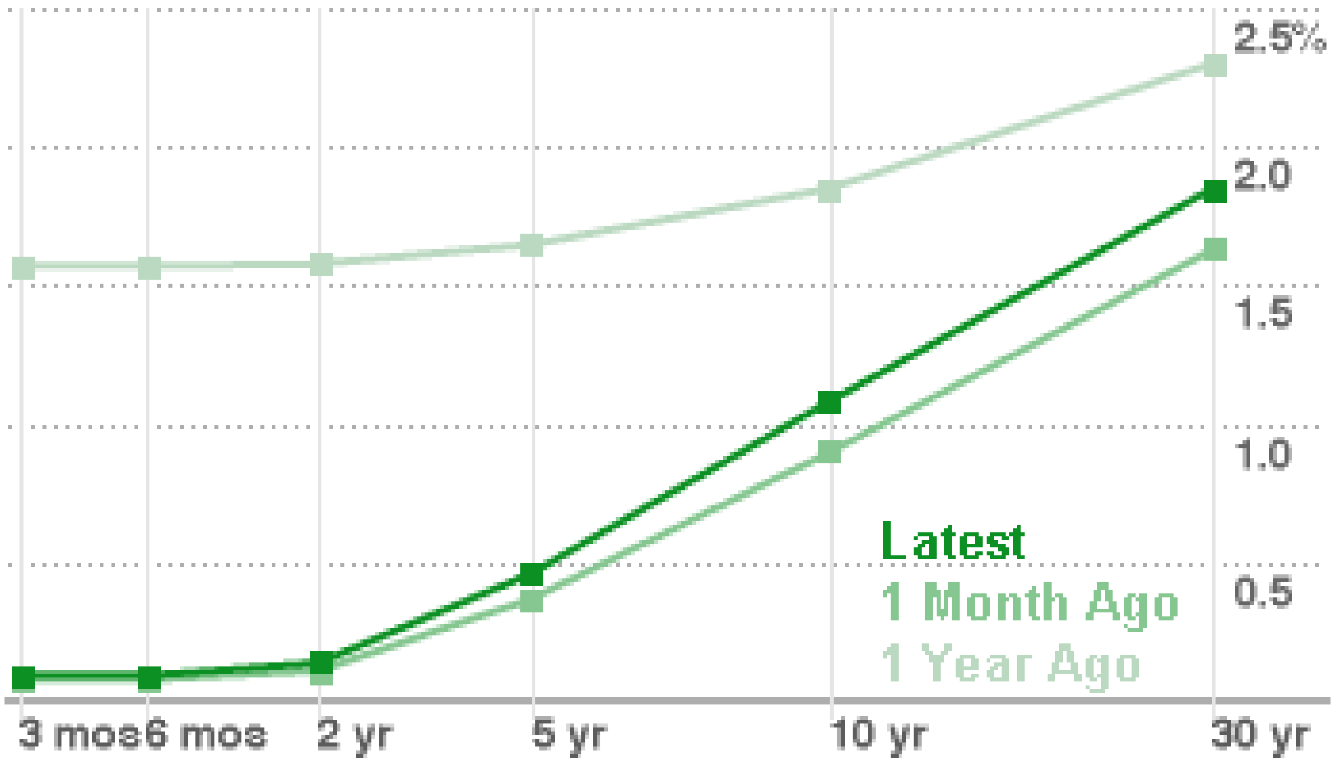

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Our biggest concern currently is the divisive political climate. We are hopeful that after Biden's Inauguration that things may calm down.

We are starting to see the anticipated broadening in the market toward value stocks and anticipate this trend to continue as the year goes on. We also believe that there are some overheated areas of the markets in bigger tech names and have some concerns with momentum stocks at extraordinary high valuations. The momentum in these names can continue for a while but buying these high earnings multiple stocks is very risky for any investor at this point in our opinion.

Having a disciplined investment and risk management process, regardless of market action, is the foundational elements to our portfolio designs. It is this portion of the approach of portfolio management, that helps consistently reduce the long run risk taken in a portfolio of investments. Speculating about near term directions in the markets can be and often is a difficult and risky proposition. We can control the risk and process we take in our portfolio construction, but we cannot control market performance.

Overall, we prefer domestic equities over international equities. We prefer more value-oriented stocks vs. growth stocks for longer term growth, as we see growth stocks as more fully valued. However, high quality growth stocks are likely to continue to outperform the market in the short term. We are currently neutral to bearish on fixed-income and interest rates. It is important to maintain discipline regarding long-term strategic asset allocation. However, as market conditions dictate, we are looking at tactical opportunities to reduce risk in portfolios, if necessary.

If you have questions or would like to discuss this further regarding your personal portfolio, please contact me at 310-433-5378.

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