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Market Thoughts – Q1 2021

In all my years in the investment world, I have never lived through a year like 2020.

There have been short, violent bear markets like 1987 and long, protracted bear markets like 2000 to 2009. The long-term secular bear markets are difficult periods with short cyclical bulls occurring. In my opinion, last year was a cyclical (short-term) bear within the context of a long-term bull. I feel we entered into a new (long-term) secular bull market in 2009, and if we are lucky enough to get results equal to the last great bull from 1982 to 2000, then we have a few more good years ahead.

Nevertheless, last year was challenging in many ways, and our lives changed because of it. I think many of us have gotten used to social distancing, and some of the other habits we have adopted may stick with us as well. We have all had dinners in crowded bistros where the next table is too loud and too close. Some distance may be appreciated. We are, however, social creatures and need each other, so as I see it, our "new normal" could be quite welcoming.

The equity markets overall provided decent returns for the year (if you stayed the course), but it was an exciting ride. In the midst of the selloff in March, the "stay-at-home" stocks became the place to be, along with big business that could still operate in the context of the stay-at-home theme. Those businesses that couldn't do this effectively suffered and are still suffering. I think valuations of some stay-at-home-themed stocks have more than run their course, especially when they trade at a big multiple of sales. They are good businesses, but very overvalued in some cases, in my opinion.

The backdrop for all of this was our Federal Reserve to the rescue, expanding its balance sheet from $4 trillion to about $8 trillion in the form of aid. My friend Bill O'Grady from Confluence Investment Management has maintained a long-term chart showing the correlation between the growth of the Fed balance sheet and the S&P 500 index. It's logical, since that much liquidity added to an economy goes somewhere, and last year, it found stocks and real estate. Mid-year, my focus was on where to consider adding "open up" names and playing that theme. The back-and-forth trading action of these two themes played itself out over many trading days dependent on COVID-19 news. The open-up theme will likely still play out, and that is where I plan on considering potential opportunities – think airlines, cruise lines, travel, and industrials that support this theme.

We will have new worries this year, which start with an extension of last year. In addition, we have more debt and a bond market with yields as low as I have ever seen. We may go negative in our yield on 90- day T-bills, and with inflation looking to heat up again, you can't get too excited about a 10-year treasury under 1%. That means bonds get difficult to buy and own. Income alternatives that play into the recovery theme may be attractive, but you need to know what you own. I will likely give some consideration to names in these areas looking to play the recovery in economic activity and potential income increases from that.

I expect it to be a challenging year, yet I see potential opportunities of which to take advantage. We still have continuing trends that provide opportunities to invest, such as the build-out of cloud and 5G. We also have new exciting trends, like autonomous driving, which will change the way we do many things over the course of this decade. This will be a major disrupter. It all provides opportunity, and along with the resources at Stifel, we are here to help you address it and consider whether it is appropriate for you. I thank you for your confidence and look forward to 2021.

Sincerely,

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