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Market Update: January 2021

Stocks started the new year off with strong gains, but ended January with the worst weekly declines since October. When the dust had settled, global stock measures were only slightly off for the month.

Overall, January will be remembered not just for ongoing coronavirus and related vaccine concerns, but more for an army of individual traders that got the best of some of Wall Street's finest.

> **It's certainly high financial drama to see armies of retail investors on Reddit hunting the so-called wolves of Wall Street.**
>
> **The Editorial Board – WSJ 1/28/21**

By now, pretty much everyone knows what happened. War broke out between hedge fund professionals and amateur traders, banded together by social media and trading on commission-free platforms.

The recent turmoil focused on two companies, GameStop and AMC. As the hedge fund managers bet against those stocks by shorting their shares, the individual investors feverishly purchased their shares … creating what is known as a *short squeeze*. For the week ended January 29, GameStop and AMC soared by 400% and 278%, respectively. The hedge fund managers lost billions.

> **It's as if a bunch of couch potatoes watching a Los Angeles Lakers basketball game on TV belted down their beer and nachos, barged onto the court – and proceeded to block LeBron James' shots and mercilessly dunk on Anthony Davis.**
>
> **Jason Zweig – WSJ 1/30/21**

So, what exactly is a short squeeze? A short squeeze occurs when a stock jumps sharply higher, forcing traders who had bet that its price would fall, to buy it in order to prevent even greater losses. Their scramble to buy only adds to the upward pressure on the stock's price.

Some described the confrontation as the culmination of the ongoing democratization of the markets. Others simply loved the idea of David beating Goliath. During some days, AMC was actually the most actively traded stock in the entire market … even though Apple Inc. is more than 350 times its size. GameStop now has a market value greater than Delta Air Lines, Inc.

> **Day traders might be able to drive GameStop shares temporarily from $20 to $483. They can't make GameStop a $483 company.**
>
> **Holman W. Jenkins, Jr. – WSJ 1/29/21**

In the end, people will be hurt … some really bad. That's how these things generally end. When the music stops, and it always does, many investors will be left without a chair.

By the way, one of those commission-free trading platforms, Robinhood, recently agreed to pay $65 million in fines to settle SEC charges. The SEC said that Robinhood's customers paid over $34 million more than they would have paid to other brokerage firms that charged fees. So much for robbing from the rich to give to the poor.

The Commerce Department reported U.S. GDP rose at a 4% annual rate, seasonally and inflation adjusted, during the fourth quarter of 2020. For the calendar year, the economy contracted by 3.5% … the first decline since the financial crisis and the worst decline since 1946.

> **Following a sharp rebound in economic activity last summer, the pace of the recovery has moderated in recent months, with the weakness concentrated in the sectors of the economy most**

adversely affected by the resurgence of the virus and by greater social distancing.

Jerome Powell, Fed Chairman – WSJ 1/27/21

Congress and the White House approved a $900 billion pandemic relief package in December, which included $600 checks to many Americans. The Biden administration has already proposed $1.9 trillion in additional aid this year, which would include sending checks for $1,400 to many households.

There's basically a wall of money being thrown at the economy.

James Knightley, ING Financial Markets LLC – WSJ 1/28/21

Americans saved $1.4 trillion in the first three quarters of calendar 2020 … or about twice as much as last year according to Berenberg Economics. This is the equivalent of approximately 10% of household spending.

In this unusual recession, governments have been unusually generous, people have not been able to spend the money, and hence they have the money and will to spend.

Holger Schmieding, Berenberg Chief Economist – WSJ 1/26/21

Home sales in the U.S. reached their highest level in 14 years. Demand was high, thanks to low mortgage rates and pandemic related influences, but supply remains extremely low.

According to the National Association of Realtors (NAR), homes for sale are down 23% from a year earlier, and represent a record low 1.9 months of supply at the current sales pace. The median existing-home price in December was $309,800, up nearly 13% from a year earlier.

Homeowners are smiling, because they are seeing prices increasing. The frustration is coming from the first-time buyers.

Lawrence Yun, NAR's Chief Economist – WSJ 1/22/21

Stubbornly high coronavirus infections and deaths, as well as delays in vaccine deliveries, are dampening Europe's near-term economic outlook. Unapproved vaccines currently account for the majority of the European Union's orders.

A return to normalcy by the summer seems extremely unlikely.

Catherine Hill, Epidemiologist/Biostatistician – WSJ 1/25/21

Oxford University estimates that the U.K. and the U.S. have inoculated 10% and 6.2% of their respective populations. The ratios range from 1.5% to 2.5% for Spain, Italy, Germany and France.

We will be very challenged at least for the next 10 weeks, and this will be the hardest phase of the pandemic.

Rudolf Anschober, Austria's Health Minister – WSJ 1/19/21

The U.K. is currently contending with a more contagious variant of the virus. They are currently in lockdown, scheduled at least through mid-February. Schools and nonessential shops are closed, and people have been told to leave home only if necessary. Their economy, which was already weakened by four years of Brexit negotiations, should continue to decline through the first quarter of 2021.

Global growth is expected to reach 5.5% this year. The outlook reflects the optimism surrounding vaccinations and improved therapies. Still, technologically advanced countries continue to fare better than those that depend on tourism and commodity prices. The IMF forecasts that 90 million people globally will fall into extreme poverty because of the pandemic … effectively wiping out much of the progress made over the past two decades.

Much depends on the outcome of this race between a mutating virus and vaccines, and the ability of policies to provide effective support until the pandemic ends. There remains tremendous uncertainty, and prospects vary greatly across countries.

Gita Gopinath, IMF Chief Economist – WSJ 1/26/21

Stock prices are at elevated levels based on pretty much every measure known to man … except maybe in relation to interest rates and bond yields.

We don't profess to know if stock prices are overvalued, and perhaps investors are right that Tesla deserves its price-earnings ratio of 1,600 based on future sales of its electric cars. But in the Federal Reserve's current world of negative interest rates, there is also plenty of speculative money chasing higher returns.

The Editorial Board – WSJ 1/28/21

Most investors apparently believe that interest rates will stay low for as far as the eye can see. After all, the Fed continues to pledge that it won't *take the punchbowl away* for at least the next couple of years. Still, Congress continues to throw money at the pandemic … borrowing about $3.5 trillion last year, with more to come this year.

In fact, there is some level of borrowing that would eventually push up inflation and interest rates. No one knows what that level is …

Greg Ip – WSJ 1/30/21

Let's not forget about tax increases. If the markets have been propped up by massive amounts of monetary and fiscal stimulus, we should expect stocks to take a hit when tax rates rise. Up to now, it doesn't appear the markets have discounted the potential for those future hikes as proposed by the current administration.

Whatever the politics of higher taxes on well-healed investors, the economics suggests they aren't positive for stock prices, all else being equal. What Washington giveth in stimulus it might taketh in taxes.

Randall W. Forsyth – Barron's 1/22/21

Remember that the stated economic growth of 4% for the fourth quarter was an annualized figure … just like the 33% rate of growth during the third quarter. In actual terms, the growth for the fourth and third quarters was 1% and 7.5%, respectively. Also, growth during the fourth quarter was starting to soften in November and December.

Mechanically, that makes it harder for GDP to register growth for the quarter – if it began the fourth quarter on third base, it began the current quarter in the batter's box and behind in the count.

Justin Lahart – WSJ 1/28/21

Investors have plenty of reasons to be cautious, whether it's high stock valuations, concerns about inflation or corporate tax hikes … or possibly the effects of emerging virus mutations on a weakening economic recovery. In any case, the markets probably need a rest after a strong ending to 2020, and the next few months should be challenging.

The good news is that consumers are flush with cash, and more is on the way … and vaccines are coming to the rescue. Let's all try to stay focused on the things we can control and hope that vaccines ultimately win the race against this relentless pandemic.

Daniel G. Corrigan, CPA/PFS, CFP®