

Market Rallies

On Powell's "Easy Money" Promise



In this 03-27-21 issue of "Market Rallies On Powell's Easy Money Promise."

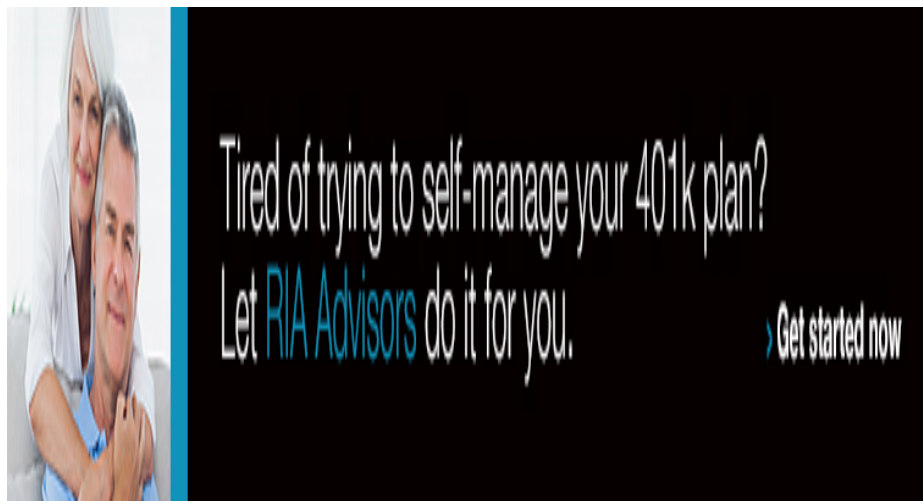
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- **401k Plan Manager**

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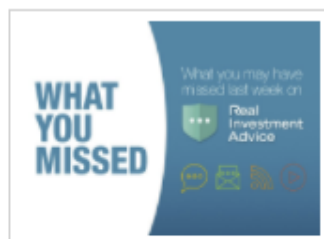
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#WhatYouMissed On RIA This Week: 3-26-21

Written by Lance Roberts | Mar 26, 2021

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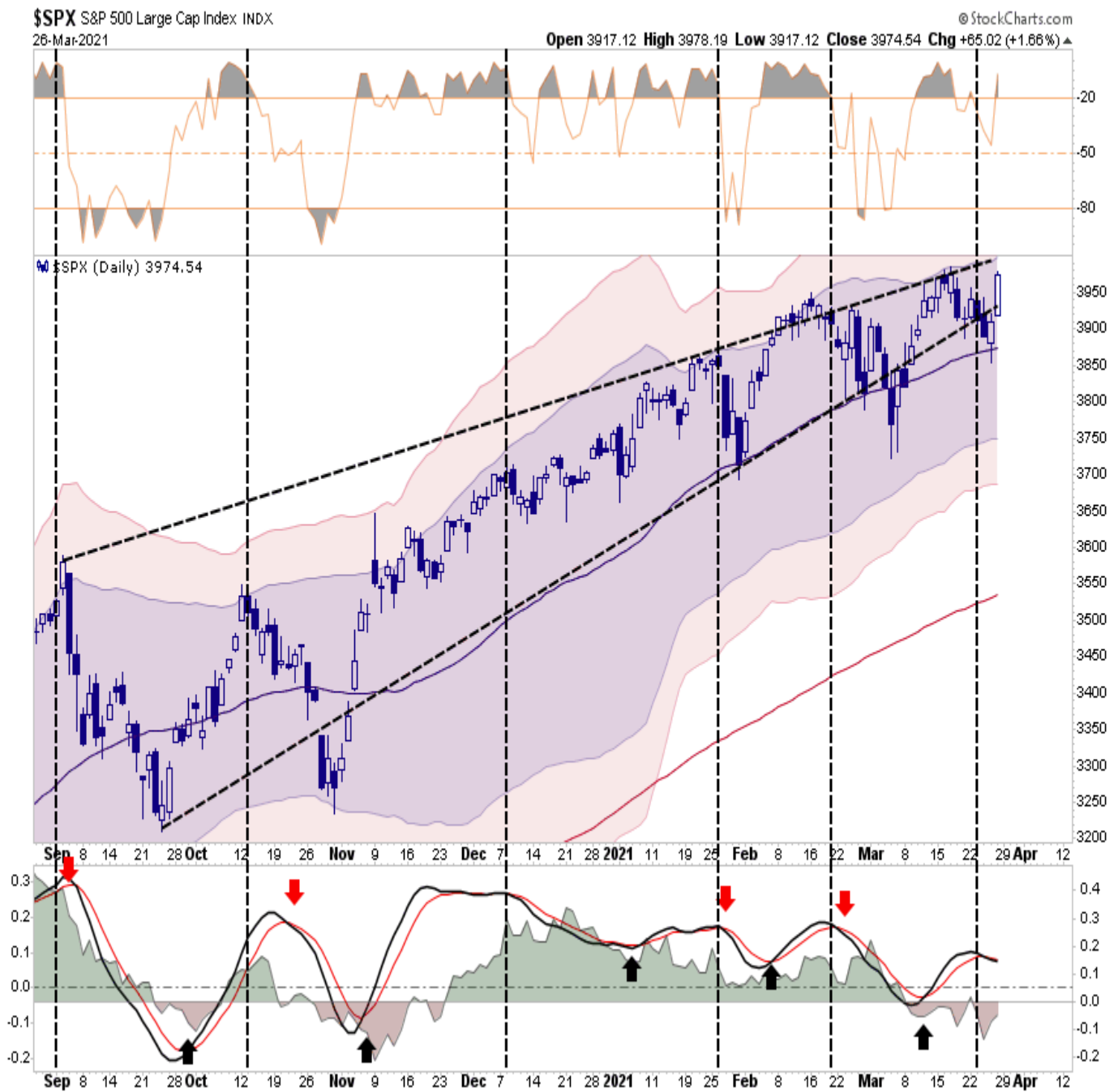
Market Review & Update

I could almost repeat last week's market update.

"Over the past week, the market didn't make a lot of headway, as price rises were limited while intraday dips got repeatedly bought. Such is what we would expect with the 'money flow' indicators we have discussed over the last several weeks back on "sell signals." (Importantly, note that Friday's early morning decline held the uptrend

line from the October lows.)"

This week was much the same story, with stocks slopping around all week. **However, on Friday, a late afternoon buying surge sent the market back to all-time highs.** Again, as noted, stocks haven't made a lot of headway since the February peak despite a lot of volatility. But Powell's promise of continue "easy money" certainly didn't hurt.



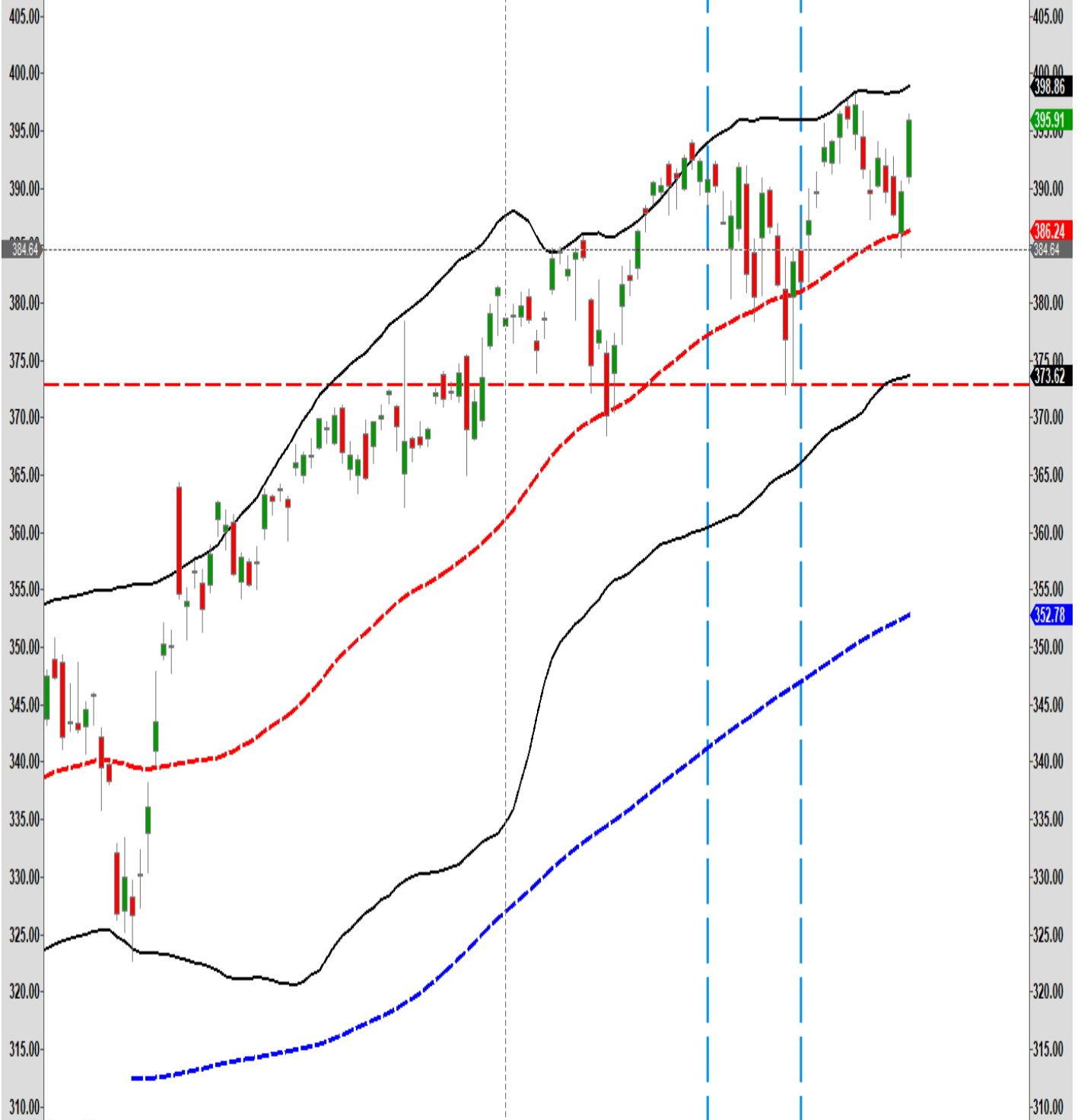
As discussed last week, the "sell signal" triggering on a short-term basis coincides with our concerns of quarter-end rebalancing for pension funds. We discuss the confluence of the long- and short-term indicators and the market's potential outcome in Thursday's ["3-minutes"](#) video.

<https://www.youtube.com/watch?v=-Y-wvFGskWA>

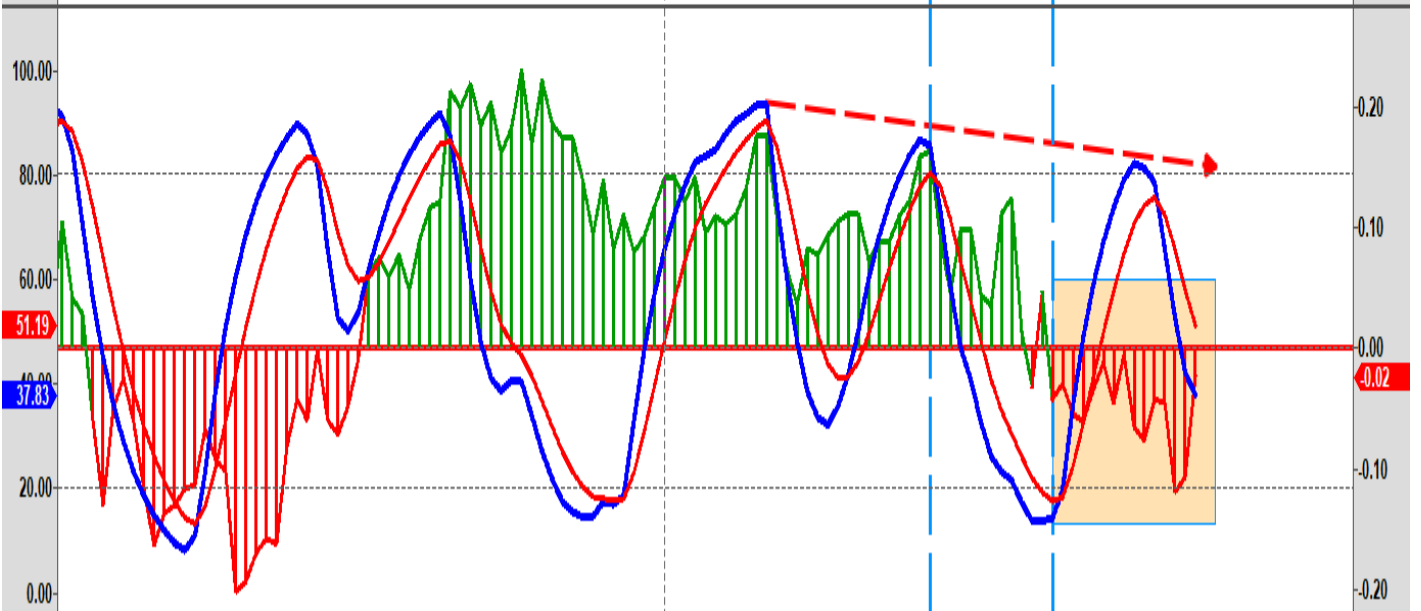
I think we saw a good bit of that rebalancing this past week and are likely close to its conclusion. **As noted, the positive weekly money flows keep downside risk somewhat mitigated for now.** As seen over the last two weeks, **dips continue to be bought despite overall price weakness.** We also see relatively rapid rotations between the defensive and offensive market sectors. As

stated previously, such suggests rallies may remain limited until the subsequent "*buy signals*" are triggered.

* SPY, SPDR S&P 500 ETF TRUST, D (Dynamic)



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I suspect we may have some additional quarter-end rebalancing risk early next week. **However, buying on Thursday and Friday next week, as second-quarter positioning gets underway, would not be surprising.**

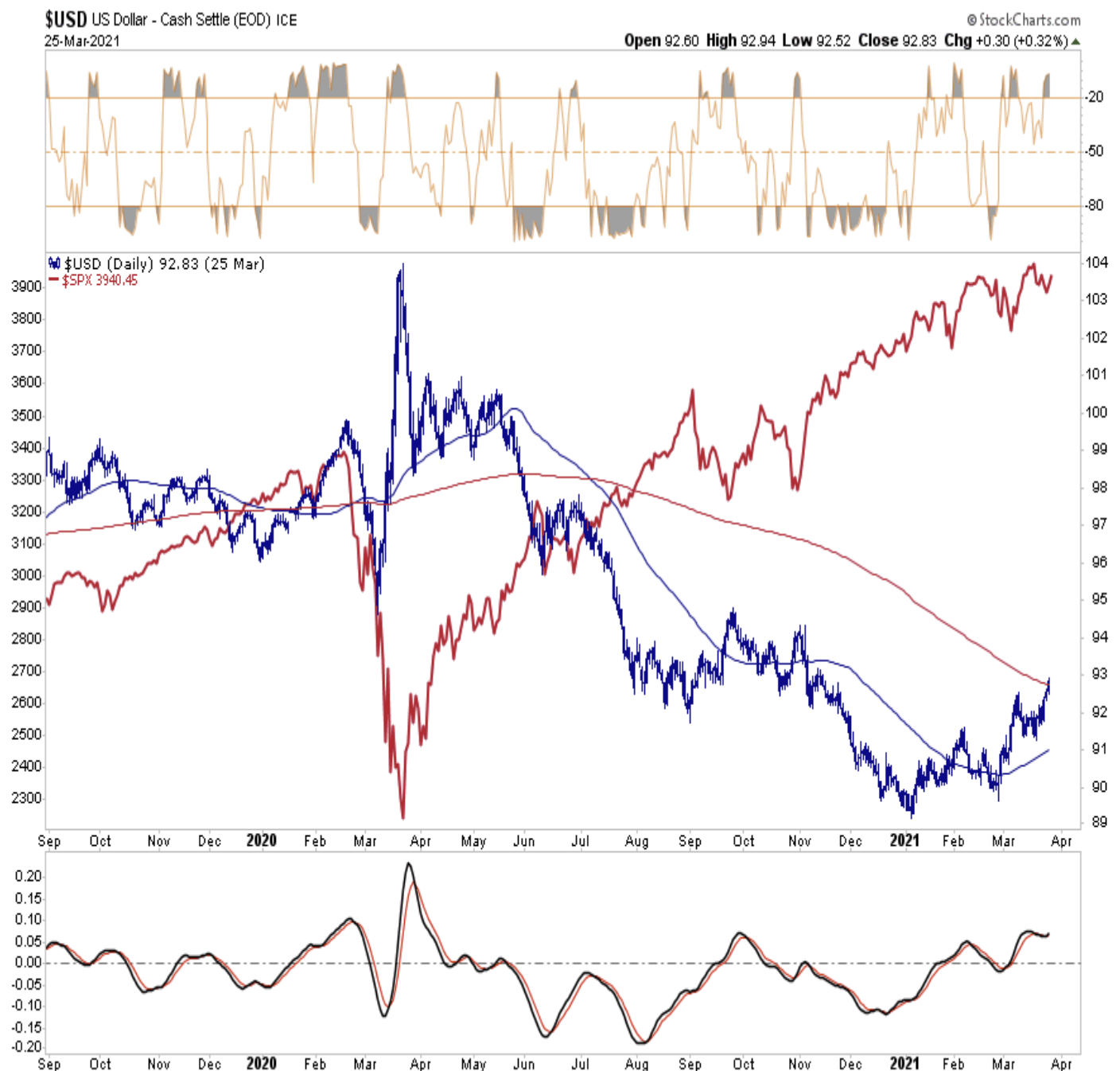
As such, hold positions early next week and look for weaknesses to add to exposures as needed.

The Dollar's Silent Action

Over the last couple of months, we repeatedly discussed the market's ongoing rise, particularly the "*value*" rotation, depended on continuing dollar weakness.

The recent rotation to value has been primarily a function of a *weaker dollar*, which boosts commodities. **As noted, if economic growth does strengthen, leading to higher rates will attract foreign inflows into the dollar for a higher yield. Such also undermines corporate profitability, given that roughly 40% of corporate profits are from abroad.**

The dollar has been gaining strength this year on expectations of more robust economic growth. A break above the 200-dma could accelerate buying as shorts begin to cover their positions.



The risk not factored into the current *?value?* trade is the inflation and interest rate increase due to the massive amounts of stimulus. However, that stimulus will quickly flow through the system, leaving consumers tapped by higher inflation and rates eroding disposable income.

In other words, the *?value trade?* could be just a fleeting as the *?economic recovery?* itself.

We are firm believers in *?value investing?* However, after years of artificial interventions, accounting gimmicks, share buybacks, and massive balance sheet leveraging, there is little *?real?* value in the markets currently.

Given that the markets have not been allowed to reset, speculators are now simply chasing the next *?momentum?* trade called *?value?*

Powell's "Easy Money" Promise

Last week, we discussed Powell's latest change to monetary policy, or rather, lack thereof.

"The U.S. economy is heading for its strongest growth in nearly 40 years, the Federal Reserve said on Wednesday, and central bank policymakers are pledging to keep their foot on the gas despite an expected surge of inflation." - Reuters

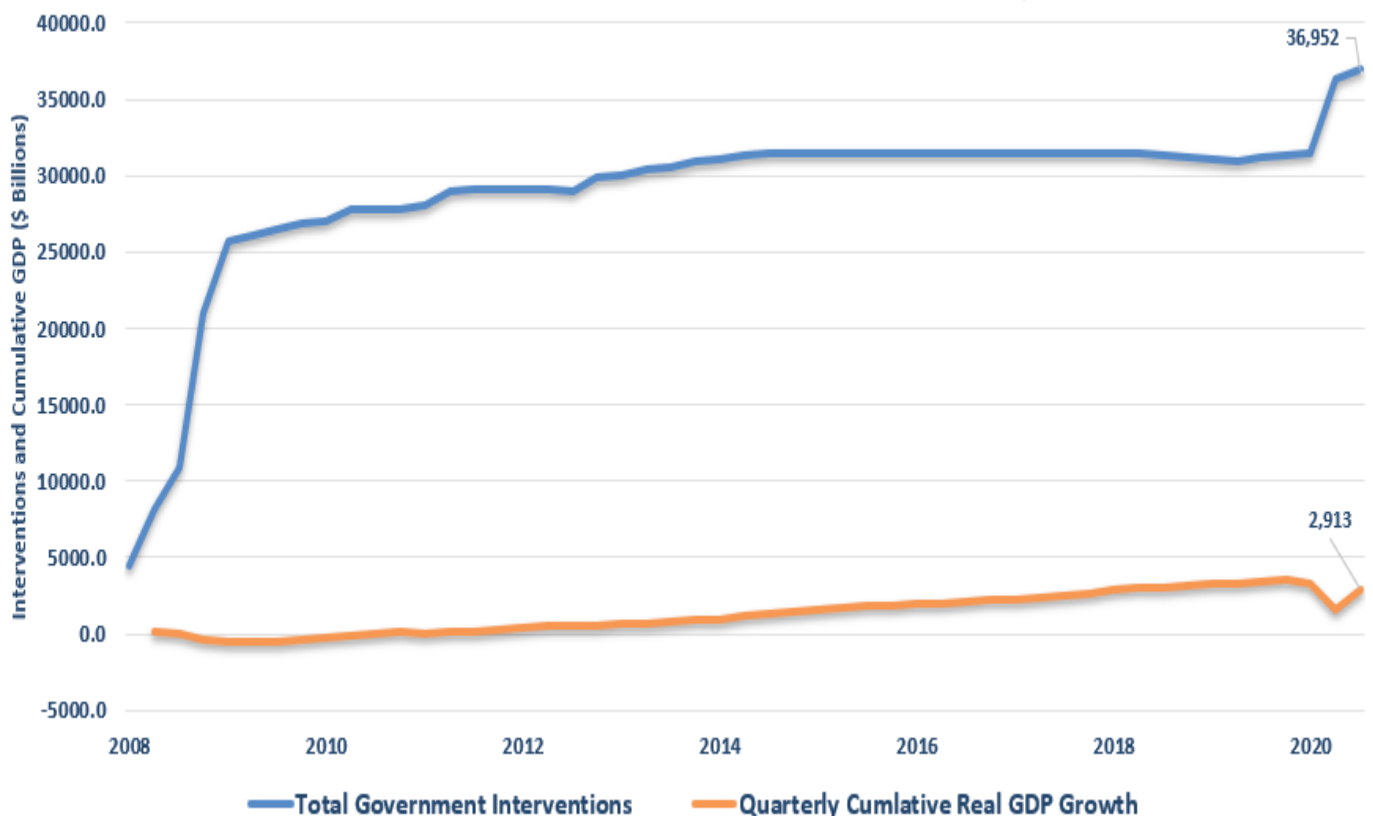
In other words, despite the Fed's mandate of maximum employment and price stability, the Fed is opting to let things run 'hot' for some time to ensure that growth is 'sticky.'"

That stance makes some sense, given the economy still requires massive liquidity support more than a decade after the financial crisis. As discussed previously in ['Forever Stimulus:'](#)

"What this equates to is more than \$12 of liquidity for each \$1 of economic growth."

Cumulative Fed / Government Bailouts Vs Real GDP Growth

REAL INVESTMENT ADVICE



The question that financial markets wanted answering was just how much of a decline in asset prices the Fed will tolerate before providing reassurance.

It only took a 3% clip off of all-time highs before there was a scramble by Fed members to assuage market concerns. My colleague, [Mish Shedlock](#), put together an excellent summary:

"Easy Money" Quotes

- On Thursday, Fed Chair Jerome Powell said even with the economy rebounding faster than expected, any change in monetary policy would happen **?very, very gradually over time and with great transparency. Only when the economy has all but fully recovered.?**
- Fed Vice Chair Richard Clarida said the central bank would stay in the game until the recovery is **?well and truly complete.?**
- Fed Governor Lael Brainard promised **?resolute patience.?**
- San Francisco Fed President Mary Daly said the central bank would show at least ?a healthy dose? of patience. **?We are not going to take this punch bowl away.?**
- Richmond Fed President Thomas Barkin said that **the United States might well see economic growth remain above trend for several years given the amount of pent-up demand.** Nonetheless, **?What matters is what outcomes we get.** I will see where we go and am not trying to overthink the date (of any policy change). I am trying to think about the outcome.?

Not surprisingly, the Fed is very cautious about the financial markets due to its inherent impact on consumer confidence. However, at this juncture, with rates at zero, stimulus checks in the mail, and QE running \$120 billion per month, verbal support is all they can do currently.

As Mish concludes:

*"The Fed's 2% inflation target is monetary insanity. Full speed ahead with the stimulus in search of inflation that would be visible to anyone who was not wearing groupthink blinders. **Japan has tried what the Fed is doing now for over a decade, with no results.**"*

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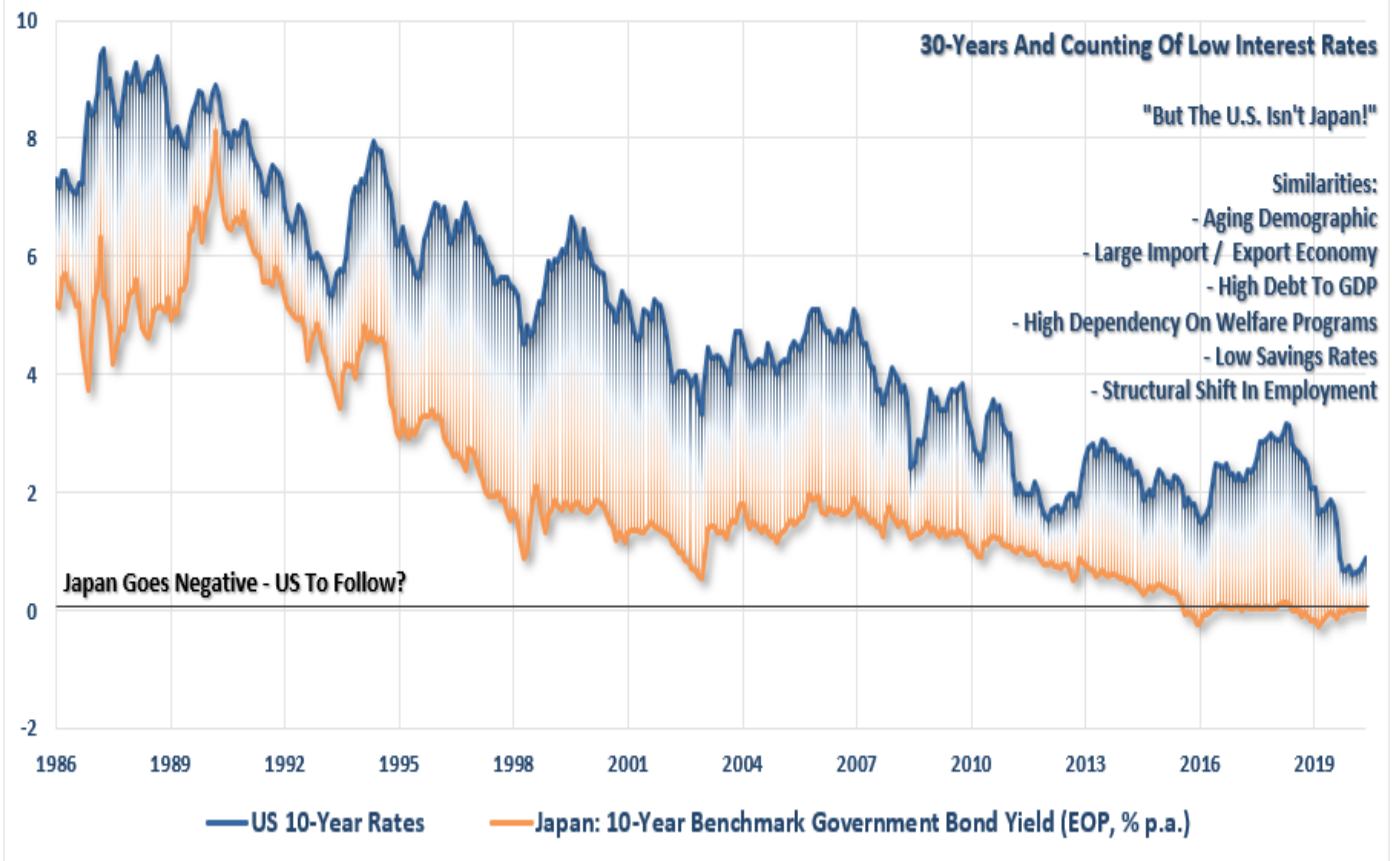
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Japanification

He is correct. The Fed's "inflation policy" will likely backfire on them badly. As discussed previously in ["Japanification:"](#)

?The U.S., like Japan, is caught in an ongoing ?liquidity trap? where maintaining ultra-low interest rates are the key to sustaining an economic pulse. The unintended consequence of such actions, as we are witnessing in the U.S. currently, is the battle with deflationary pressures. The lower interest rates go ? the less economic return that can be generated. An ultra-low interest rate environment, contrary to mainstream thought, has a negative impact on making productive investments, and risk begins to outweigh the potential return.?

Japan vs. U.S. - Interest Rates Are All Relative



As my colleague Doug Kass noted, **Japan is a template of the fragility of global economic growth.**

?The bigger picture takeaway the fact that financial engineering does not help an economy, it probably hurts it. If it helped, after mega-doses of the stuff in every imaginable form, the Japanese economy would be humming. But the Japanese economy is doing the opposite. Japan tried to substitute monetary policy for sound fiscal and economic policy. And the result is terrible.?

I agree with Doug, as does the data, that while financial engineering props up asset prices, it does nothing for an economy over the medium to longer-term. **It actually has negative consequences.**



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Stock Buybacks Gone Wild

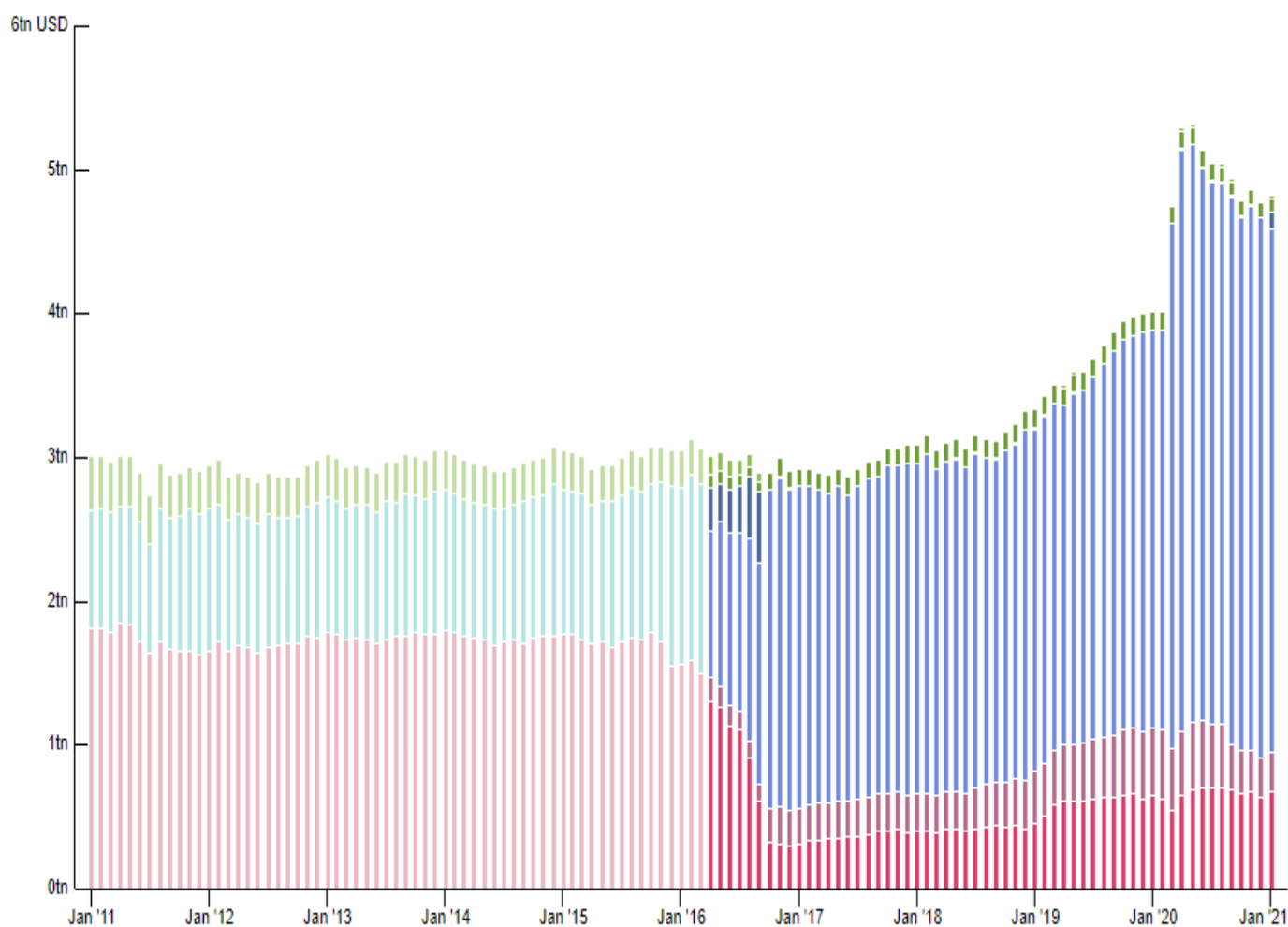
Two weeks ago, I addressed the "*Money On The Sidelines*" myth stating:

"No, this is not the '[cash on the sidelines](#)' argument which I debunked previously. Following the pandemic, corporations drew down credit lines and hoarded cash due to economic uncertainty. Now, with expectations of recovery, corporations are

once again beginning to deploy that cash."

Total investments by each category of U.S. MMF

Data



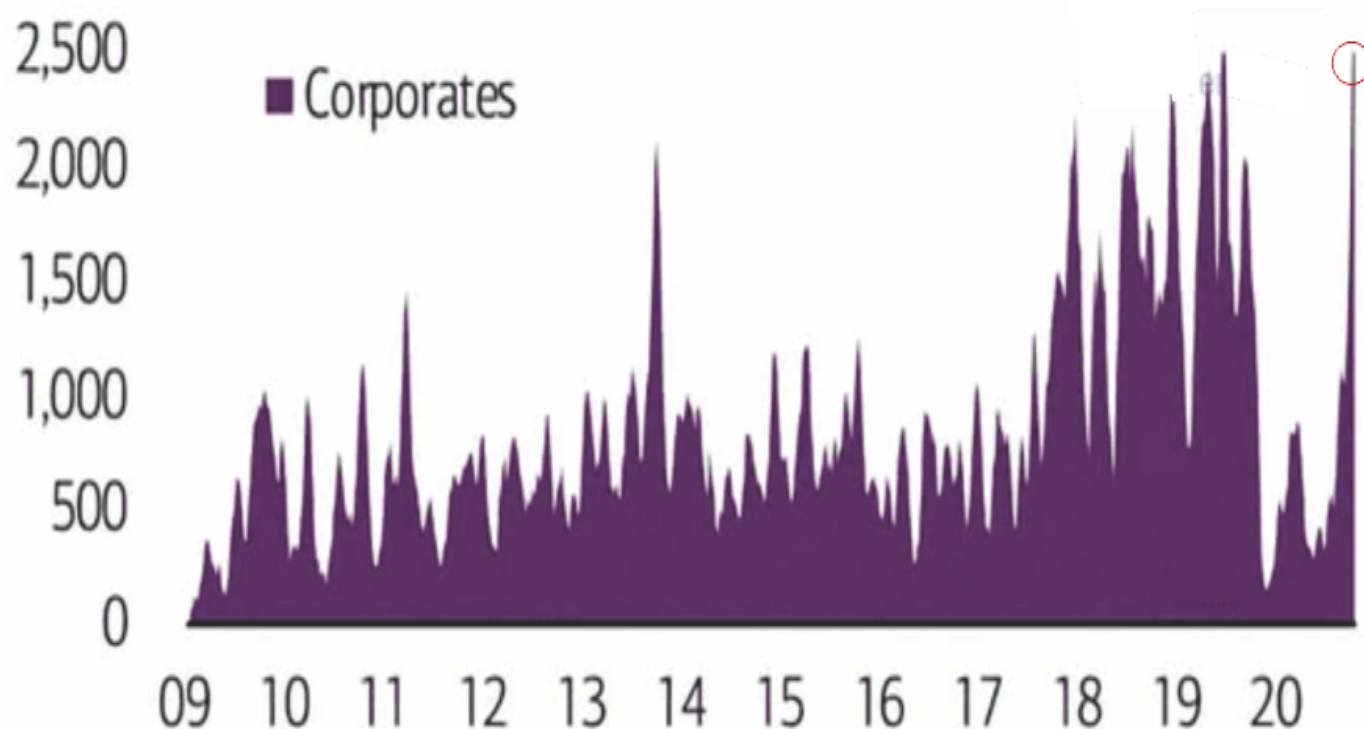
Sources: SEC Form N-MFP2, OFR Analysis

As I stated then, while the mainstream media hope is all this cash will be flowing back into the economy, the reality is that it will primarily go to stock buybacks. Again, while not necessarily bad, it is the *?least best?* use of the company?s cash. **Instead of expanding production, increasing sales, acquiring competitors, or making capital investments, the money gets used for a one-time boost to earnings on a per-share basis.**

This past week, share buybacks hit a new record.

Chart 27: Buybacks are accelerating and now at record levels

Corporate clients (4 wk. avg, \$ mn)

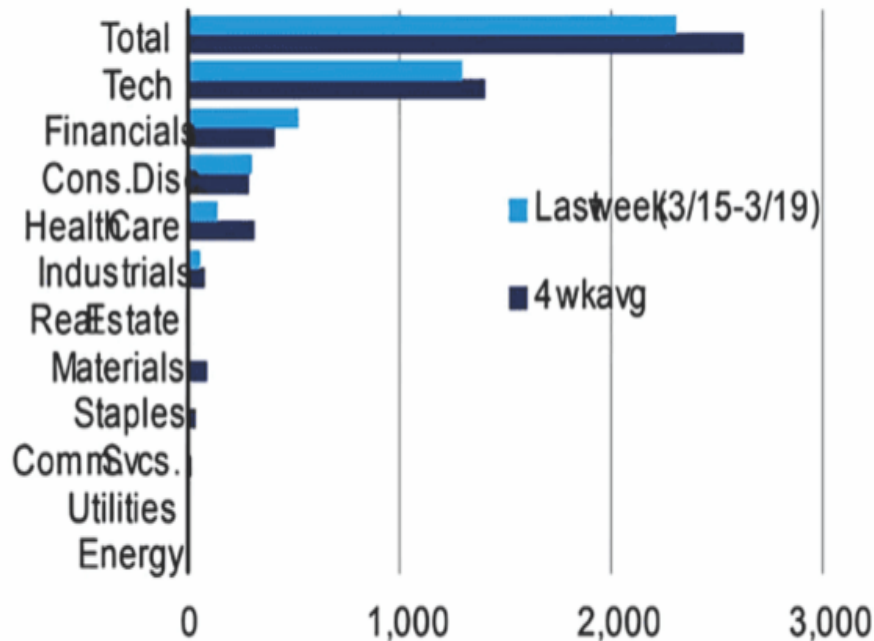


Source: BofA Securities

Not surprisingly, the most prominent players in buybacks are the ones that need to subsidize their earnings the most to beat estimates; technology and financials.

Chart 38: Buybacks concentrated in Tech

Buybacks by sector (\$ mn)



Source: BofA Securities

Net Purchases

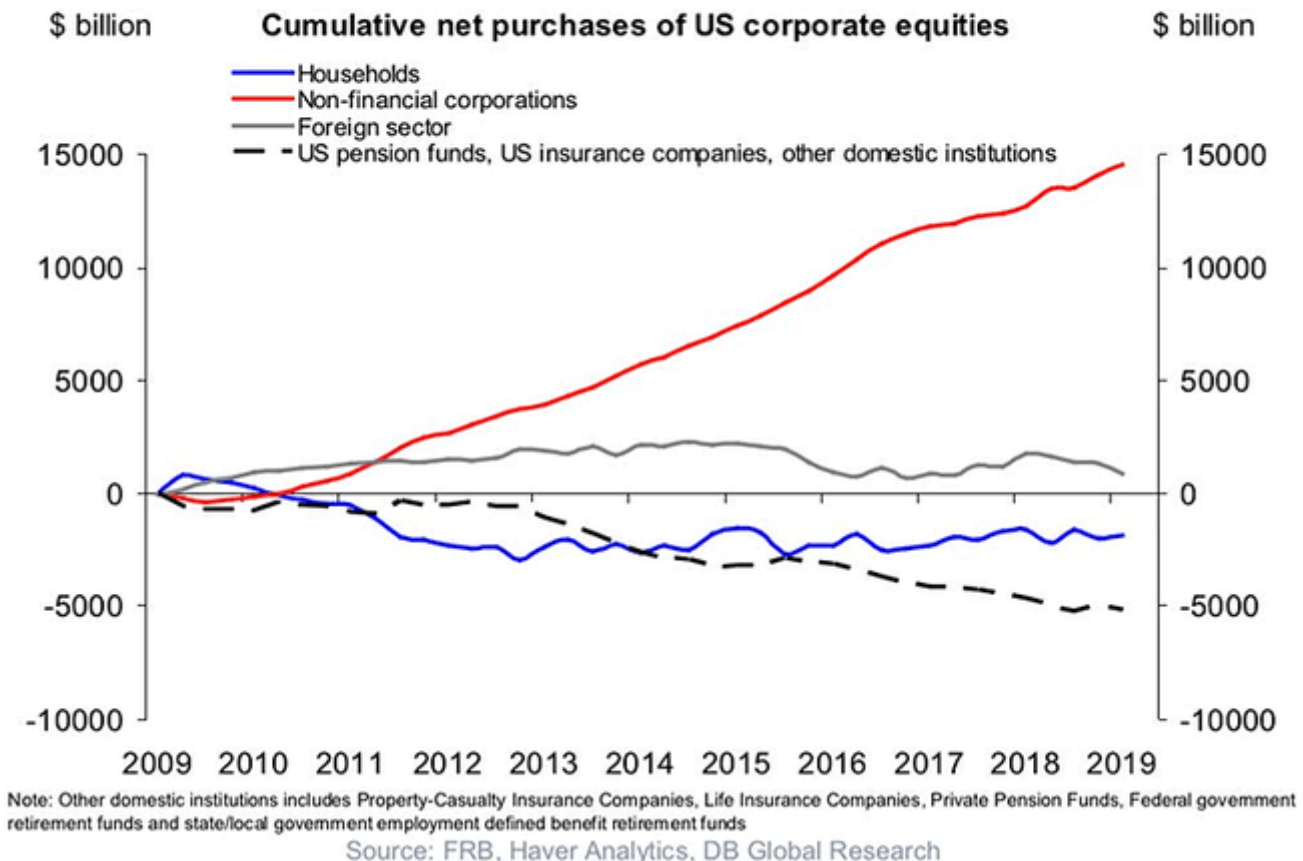
While share buybacks primarily are for the benefit of corporate insiders "*cashing out*," it does have the effect of supporting asset prices as well. [As I discussed in 2019](#), when stocks were hitting records amid record share repurchases:

*"What is clear, is that **the misuse, and abuse, of share buybacks to manipulate earnings and reward insiders has become problematic**. As [John Authers](#) recently pointed out:*

*'For much of the last decade, companies buying their own shares **have accounted for all net purchases**. The total amount of stock bought back by companies since the 2008 crisis even exceeds the Federal Reserve's spending on buying bonds over the same period as part of quantitative easing. Both pushed up asset prices.'*

*In other words, between the Federal Reserve injecting a massive amount of liquidity into the financial markets, and corporations buying back their own shares, **there have been effectively no other real buyers in the market.**"*

What's the source of the rally in the stock market since 2009? Buybacks




I bring this up for two reasons:

1. **The buybacks ARE SUPPORTIVE of asset prices in the short-term; and,**
2. **We just had to "bailout" these companies because they couldn't weather an economic downturn as they have spent years piling into debt and buying back shares.**

While Janet Yellen is okay with the buybacks, as she thinks the banks are healthier now, why doesn't anyone ask the question:

"If banks are so healthy, why do they need a constant monetary stimulus to remain in business and a bailout every time the economy declines?"

It doesn't sound very healthy to me.

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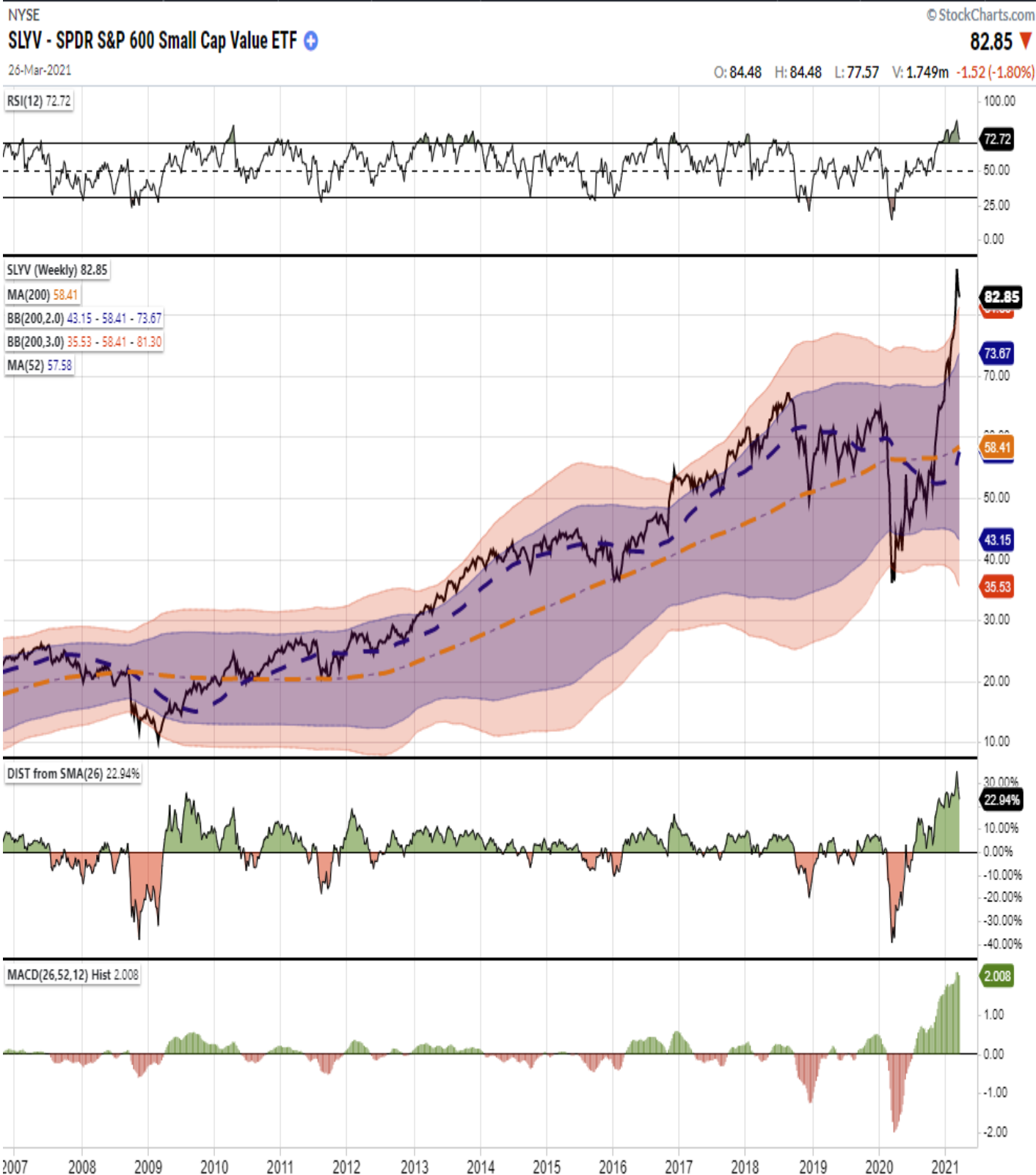
Portfolio Update

As noted above, with the "money flow" indicators now negative on both a daily and weekly basis, we are currently holding much higher levels of cash. Last week, we also added a bit of

"duration" to our bond portfolio by stepping into TLT to add a hedge against a potential pickup in volatility short-term.

With the market now about 1/3rd of the way through the correction cycle, there is limited downside risk currently as we remain in the year's seasonally strong period. However, such doesn't mean we can't have a lot of volatility in the meantime.

We remain wary of **the rise in yields, and ultimately the dollar, which remains the key to the current market cycle.** As discussed last week, the "*value trade*," which had become excessively overbought, corrected in earnest this past week. While we may see some "*bottom-fishing*" in the short-term, there is still substantially more room for a correction given the extension from long-term means.



Our more significant concern over the next quarter is the extremely high net positioning of institutions in the markets. Historically, when "everyone is in the pool," outcomes have not been all that pleasant. While we continue to remain allocated toward equity risk currently, we do it with a constant eye on the risk. We suspect that we could see a fairly substantial correction during the summer.

Figure 1: Discretionary positioning is near all-time highs but in line with very strong growth



But that is a story we will discuss when we get there.

Continue to manage risk until we start to see *"buy signals"* across our indicators once again.

The MacroView



#MacroView: Could A "Transaction Tax" Be A Good Thing?

Written by Lance Roberts | Mar 26, 2021

Could a "financial transaction tax" be a good thing for investors if it slows down the frequency of trading and reduces predatory Hedge fund practices?

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See You Next Week

By Lance Roberts, CIO

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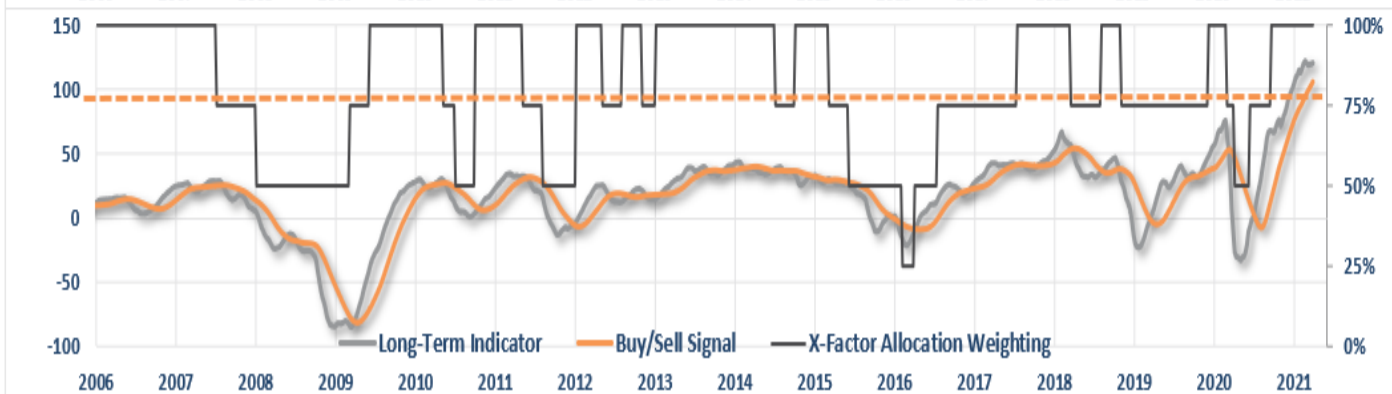
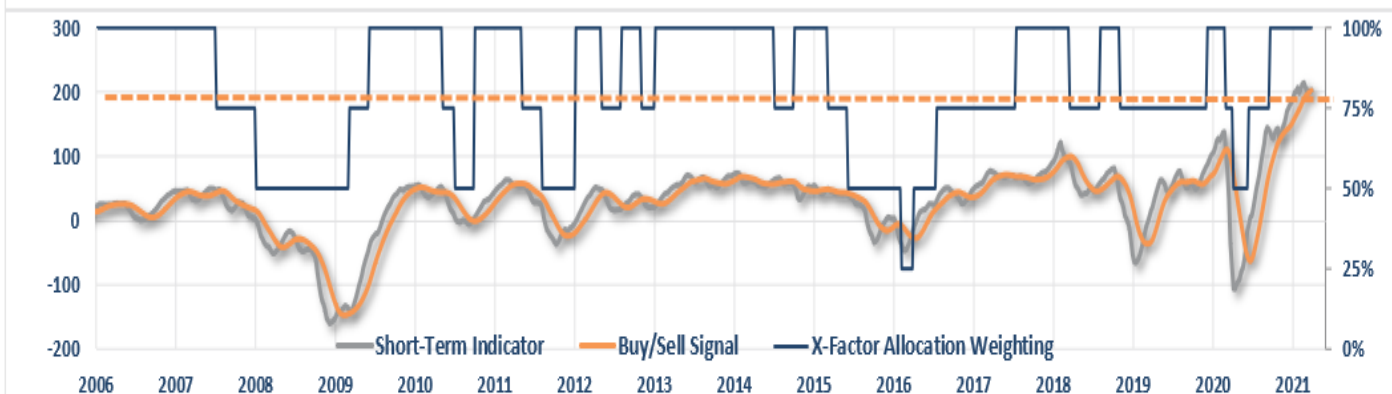
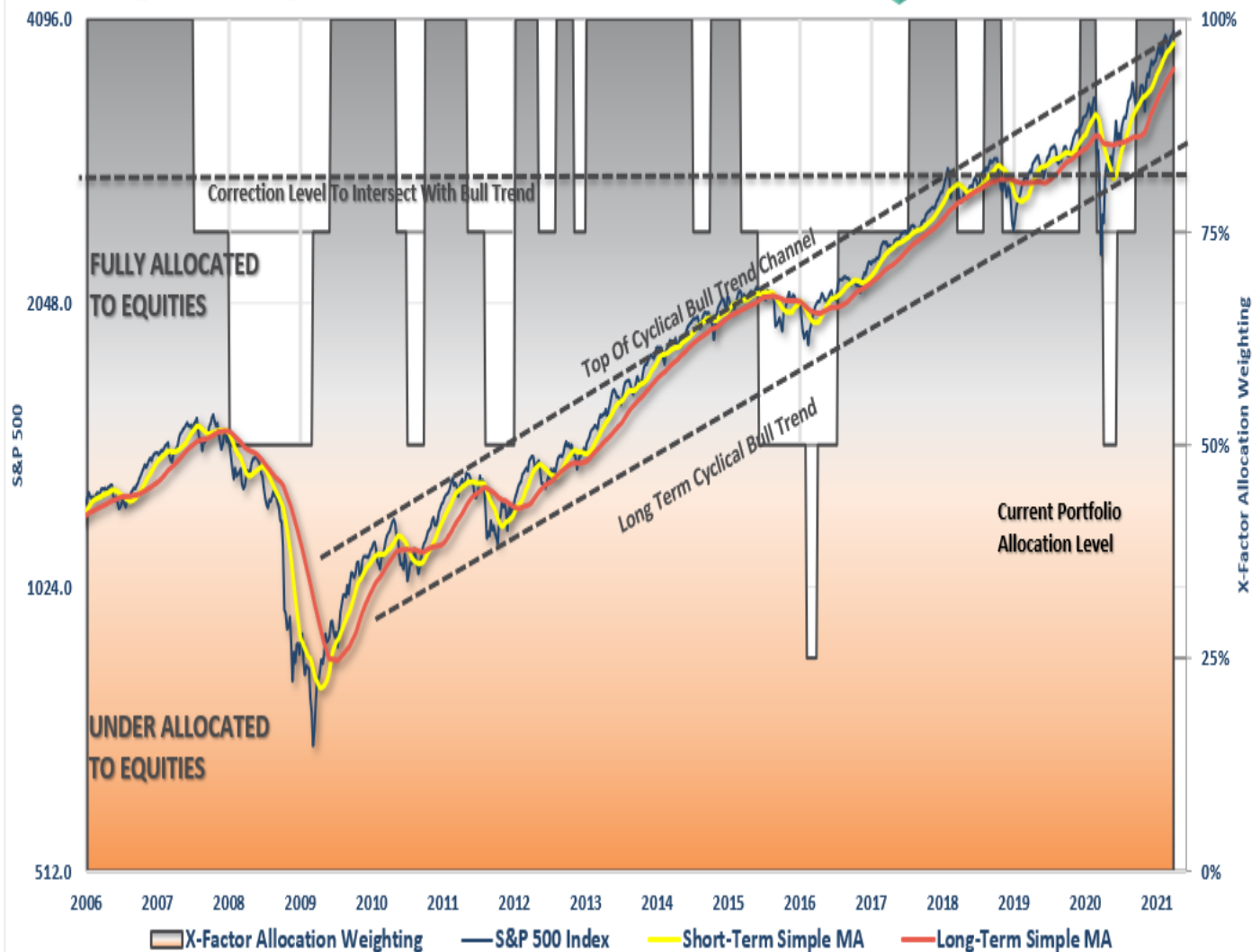
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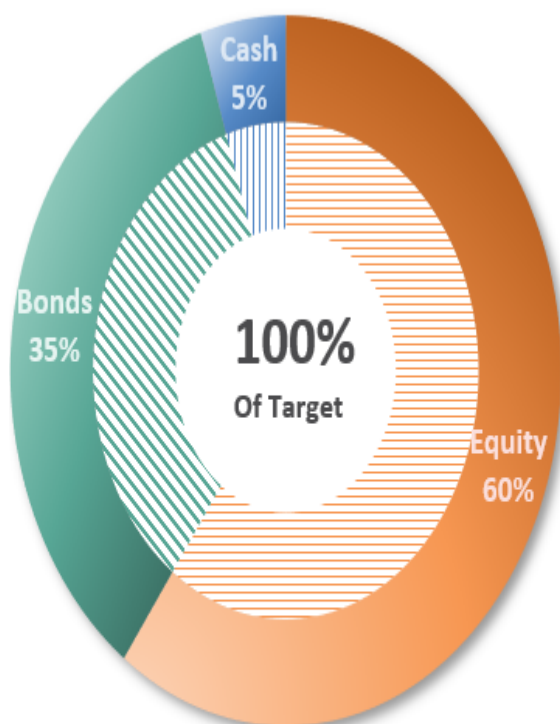
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Risk Management Analysis



Current Portfolio Weighting



Current 401k Allocation Model

5.00% Cash + All Future Contributions

Primary concern is the protection of investment capital

Examples: Stable Value, Money Market, Retirement Reserves

35.00% Fixed Income (Bonds)

Bond Funds reflect the direction of interest rates

Examples: Short Duration, Total Return and Real Return Funds

60.00% Equity (Stocks)

The vast majority of funds track an index.

Therefore, select on ONE fund from each category.

Keep it Simple.

20% Equity Income, Balanced or Conservative Allocation

30% Large Cap Growth (S&P 500 Index)

5% International

5% Mid-Cap

Portfolio Instructions:

Allocation Level To Equities	Recommendation	When To Take Action
Less Than Target Allocation	Hold Current Exposure	Hold Exposure
Equal To Target Allocation	Hold Current Exposure	Hold Exposure
Over Target Allocation	Hold Current Exposure	Hold Exposure

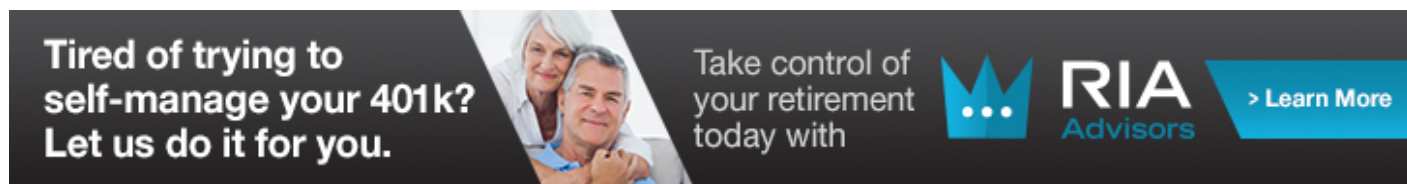
Commentary

After rallying off the 50-dma last week, the market rallied back towards all-time highs on Friday. With quarter-end pension fund rebalancing complete, the market is likely clear for a rally into early April.

If you need to increase equity exposure, the opportunity to do so is available. But as always monitor the risk you take as we are very extended into the current market cycle. If you are close to retirement, think about being more conservative as you don't have the time to make up substantial losses if they occur.

Maintain exposures, but rebalance positions that have grown to outsize weightings in portfolio. International and small-cap stocks have had decent corrections, but remain extended from long-term means. You can add weight to these sectors, but keep a watch on the dollar. A stronger dollar will undermine these areas specifically.

If you need help after reading the alert, do not hesitate to [contact me](#).

A horizontal banner with a dark background. On the left, white text reads "Tired of trying to self-manage your 401k? Let us do it for you." In the center, there is a photo of an older couple smiling. To the right of the photo, white text says "Take control of your retirement today with". Further right is the RIA Advisors logo, which consists of a blue crown icon with three white dots inside, followed by the text "RIA Advisors" in white. On the far right, a blue button with white text says "> Learn More".

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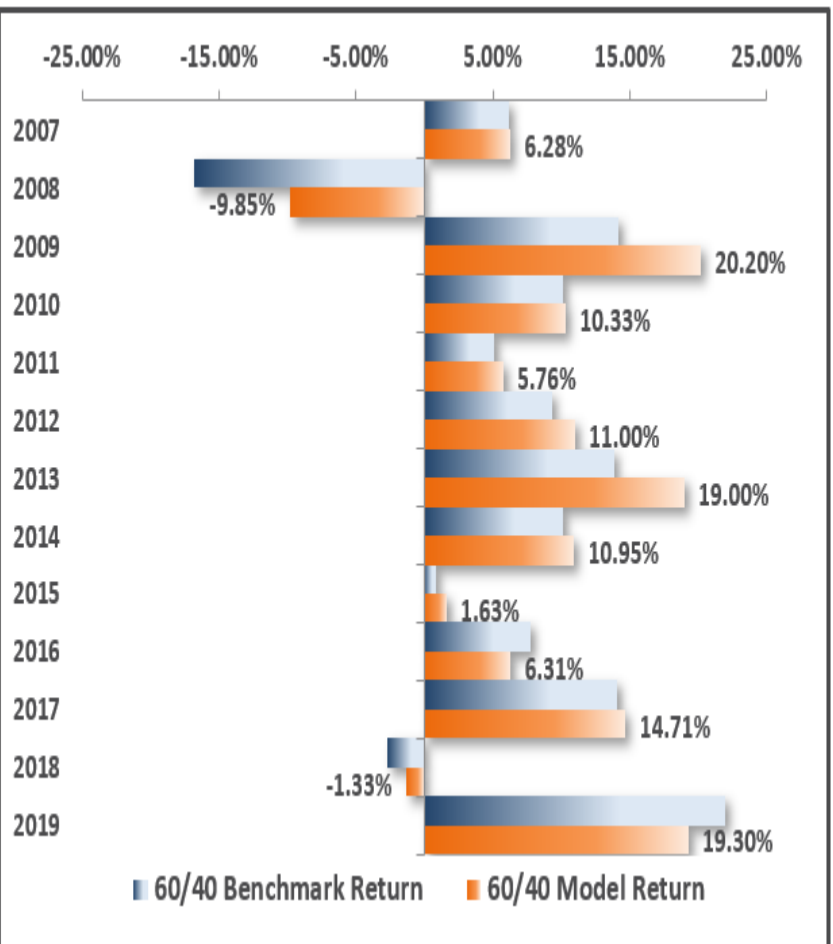
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Year	60/40 Benchmark Return	60/40 Model Return
2007	6.15%	6.28%
2008	-16.79%	-9.85%
2009	14.22%	20.20%
2010	10.17%	10.33%
2011	5.14%	5.76%
2012	9.33%	11.00%
2013	13.91%	19.00%
2014	10.08%	10.95%
2015	0.83%	1.63%
2016	7.79%	6.31%
2017	14.12%	14.71%
2018	-2.72%	-1.33%
2019	21.96%	19.30%



Portfolio vs Benchmark Statistics	
Number of Up Years	11
Number of Down Years	2
Best One Year Return Of Benchmark	21.96%
Best One Year Return Of Model	20.20%
Worst One Year Return Of Benchmark	-16.79%
Worst One Year Return Of Model	-9.85%
Benchmark Return 2007-Present	123.78%
Model Return 2007-Present	173.11%
Total Alpha Generated	49.33%
Mean Annual Return Of Benchmark	7.25%
Mean Annual Return Of Model	8.79%
Beta Of Model vs Benchmark	0.86
Jensens Alpha	2.30%
Sharpe Ratio	0.29

