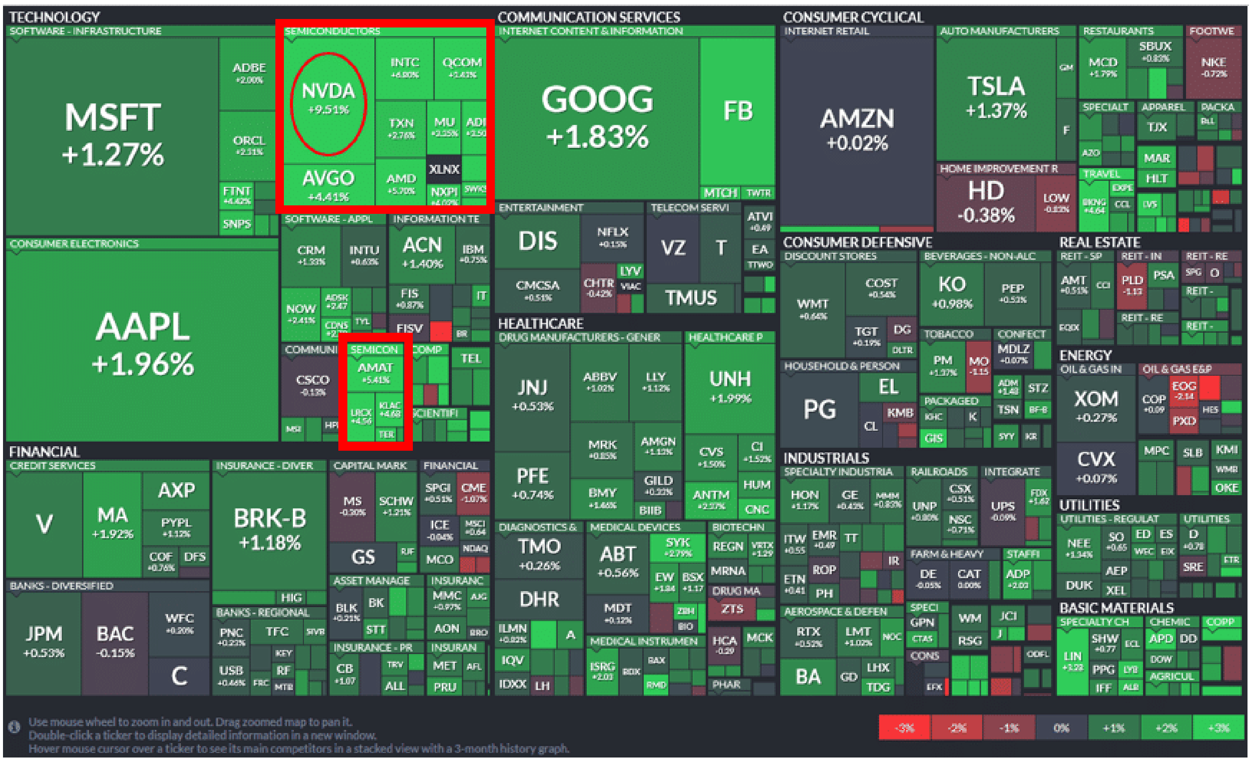
RIA Advice

Chips Ahoy! Semiconductor Stocks Lead the Way

On Thursday, Nvidia (NVDA) led the market and other chip stocks higher. It appears chip investors are enthused with their investor day presentation. The Finviz heat map below highlights the gains for large chip stocks and the broad outperformance of the semiconductor industry versus other sectors. At its presentation, NVDA shared its plans to provide semiconductor chips and software for the gaming, AI, robotics, enterprise software, and automotive industries. Furthermore, the CEO provided spoke about its Omniverse platform. Omniverse is the equivalent of FaceBook's Metaverse. Many technology gurus expect the "verse" to be the next big thing. At a forward P/E of 53, NVDA has a higher valuation than most competitors. However, the valuation is somewhat justified by its robust revenue growth and commitment to future growth. *Disclaimer- we hold NVDA and AMD in our equity models*.



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What To Watch Today

Economy

- 10:00 a.m. ET: **Pending home sales,** February month-over-month (1.0% expected, -5.7% in January)
- 10:00 a.m. ET: **University of Michigan Sentiment,** March final (59.7 expected, 59.7 in February)

Earnings

- *No notable reports scheduled for release*

Market Trading Update

The market continues to exhibit a more bullish attitude by following small pullbacks with strong rallies. That was the case yesterday, as technology, namely chips, rallied along with the rest of the market following Wednesday's decline. The market did break above the downtrend line and is back above the 200-dma. With portfolio managers underweight equities, quarter-end portfolio rebalancing will likely provide some additional lift to equities short-term. We still recommend using the rally to rebalance risk in your portfolio if you didn't like the January decline.

Risk Off

The terms "Risk-On" and "Risk-Off" apply to investors' sentiment and their collective desire to take risks. For much of 2020 and 2021 risk was decidedly on. Investors bought meme stocks, SPACs, cryptocurrencies, and many other risky assets. Those taking the most risk tended to do the best. Since 2022 risk has been off. Last Wednesday's Commentary has a short piece entitled *A Tech Bust Beneath the Surface*. It describes the significant losses in many of 2020 and 2021 popular risk-on assets. The Tweet below from Charlie Bilello shows that SPAC issuance is another victim of the current risk-off environment. Even if we annualize the current 2022 SPAC issuance it pales in comparison to the last two risk-on years.

Charlie Bilello
@charliebilello

There's been $10 billion in new US SPAC issuance so far this year. Same point last year: $96 billion in issuance.

US SPACs, IPO capital raised (billions)
2022 YTD: $10
2021: $163
2020: $83
2019: $14
2018: $11
2017: $10
2016: $3
2015: $4
2014: $2
2013: $1

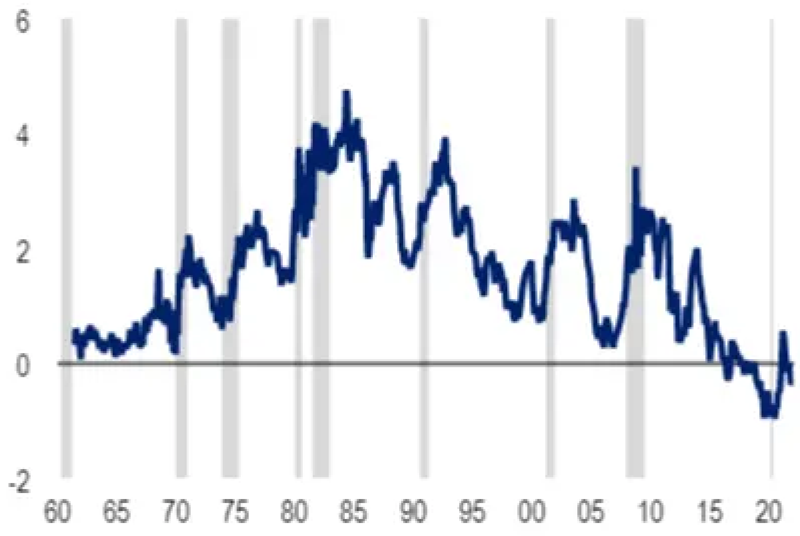
Two Parts Of Bond Yields

Long bond yields are made up of two parts: the sum of projected short-term rates, and then a premium on top of the sum, to compensate investors for locking up their money. But this latter part, the *?term premium?,* has been squeezed out of the market by central bank quantitative easing.

> *"The 10-year term premium has averaged about 1.5% over the postwar period. Hence, historically it took a very tight Fed and high fears of recession to trigger a yield curve inversion. Specifically, the market had to expect the future funds rate to average 150bp below the current funds rate to invert.*
>
> *The Fed only cuts that much in a recession. No wonder inversion was a good predictor of recessions. Today, the long end of the US yield curve is heavily distorted. The Fed has deliberately driven down the long end of the yield curve with its asset buying programme. At the same time, very low bond yields outside the US exert downward pressure on US yields. The upshot is that the term premium has now dropped into negative territory. The yield curve can now invert even if the market expects no rate cuts from the Fed." - Ethan Harris, BofA*

Exhibit 2: ACM term premium, 10 yr (EOP, %)

10-year term premium has averaged about 1.5% over the post war period



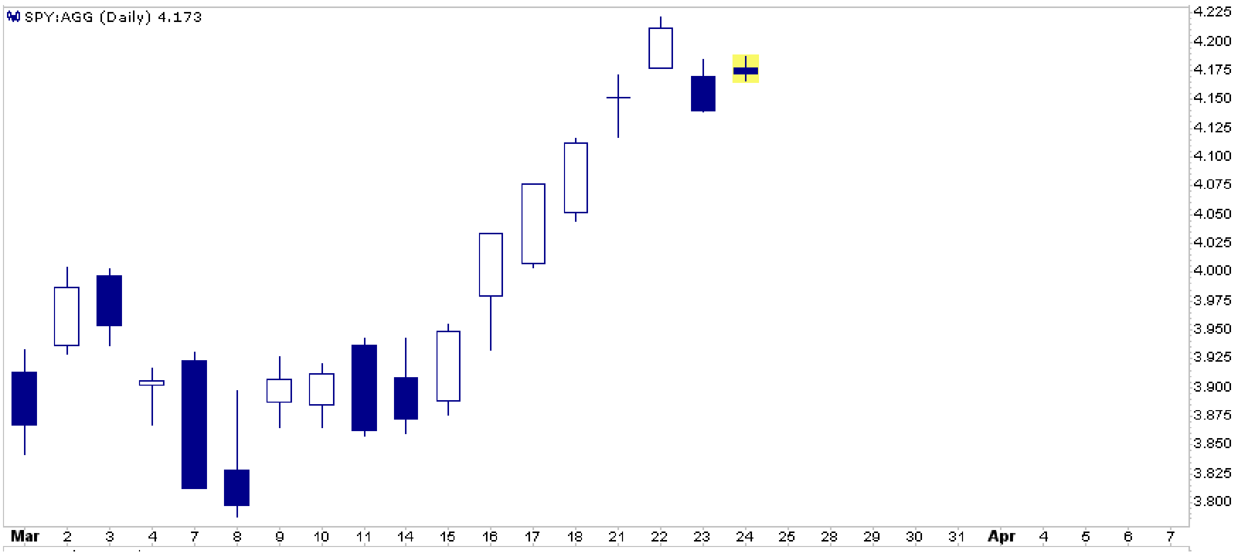
Source: FRBNY

BofA GLOBAL RESEARCH

Bonds May Find Some Love This Month End

Large mutual, pension, and endowment funds frequently rebalance their portfolios at month ends. By this, we mean they invest excess cash and bring the allocation of each asset back to their respective model weights. Weights drift over time due to gains and losses in the portfolios. Typically the drift in weights is minor, but with recent volatility and the sharp sell-off in bonds, this approaching month-end is likely causing more significant portfolio imbalances than is usual. As a proxy, the graph below shows the ratio of SPY (S&P 500) to AGG (Investment Grade Bond ETF). Simply, stocks greatly outperformed bonds this month. For balanced portfolios holding a fixed percentage of stocks and bonds, their allocation percentage to stocks rose while the allocations to bonds fell. A manager in this situation looking to rebalance will need to sell stocks and buy bonds.

ICI claims there are just under $2 trillion of assets in target-date funds. These balanced funds allocate between stocks and bonds based on a specific target date. Target funds are in all 401k plans. Further, they account for more than half of 401k assets, per EBRI. These funds are just one of many large institutional funds running balanced models. **We estimate that if the month were to end today, target funds would need to buy about $38 billion of fixed income assets to rebalance, assuming a 50/50 stock-bond ratio.** Again, that number is just for target funds. The amount of bonds needed if all balanced funds fully rebalance is likely much higher.



Jobless Claims at Lowest Level Since 1969

In July of 1969, Neil Armstrong and Buzz Aldrin landed on the moon. That event coincided with the last time initial jobless claims were at the same levels as today. In actuality, today's +187k initial jobless claims are much lower as a percent of the population. In May of 1969, jobless claims hit an all-time low of 181k. The population at the time was 202 million. Today jobless claims are 187k, and the population is 329 million. Next week's ADP and BLS employment report will shed more light on the jobs market.

The following quote from David Rosenberg is worth considering:

> "*I just heard a commentator on CNBC say there is no recession with initial jobless claims as low as 187k. Last time this happened? September 6th, 1969. When did the recession begin? Try? December 1969. This is otherwise known as classic late-cycle!*"

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