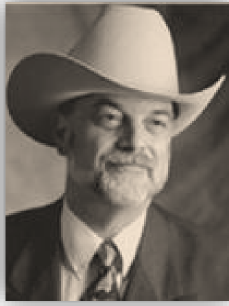

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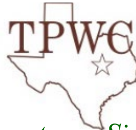

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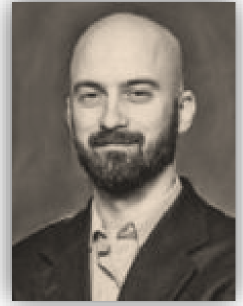

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January 21, 2021

TPWC Market and Economic Update

The Markets

The S&P 500 Stock Index (SPX) appears to be, like many of us, a bit under the weather, suffering from a mild dose of COVID Omicron combined with Federal Reserve interest rate anxiety. The Index sagged 5.68% for the week, down to 4397.94, its lowest close since mid-October of last year. It is now down 7.73% from its high, recorded at the end of 2021. On the plus side, it remains up 14.5% from where it was last January at this time. Apparently, SPX traders have finally concluded that the Omicron variant will slow things down, and the evidence is there that it already has. Investors are also becoming aware that the Fed will raise rates, and those increased interest rates will make it more expensive for high-tech firms to borrow more money. When they plugged that into their equations, it appeared that some of the relatively higher-flying companies might not get the astronomical earnings growth into the future that they have seen in the past couple of years. As of today, we are only another 2.27% away from an official market correction; one that is probably long overdue. Corrections are a healthy part of bull markets. The CRSP Mid-Cap Value Index closed at 2488.65, down 5.46% for the week, but only down 4.18% year-to-date, and from the top.

The benchmark 10-year U.S. Treasury note yield ended the business week at 1.763%, down 1.62% for the week, but down far more from its high on Wednesday of about 1.9%. The 30-year bond slipped a bit too, declining to 2.080% but leaving the yield curve slope still well into positive territory. West Texas Intermediate crude oil ended the week pretty much where it started at $84.76 per barrel, up 0.41%.

The Economy

The financial headlines for the week ending on 1/21/22 were mostly about inflation and interest rates, but the bond market seems to be continuing not to watch TV or read the worried pronouncements. The 2-year Treasury note, where one would expect to see fears of higher rates and inflation hit the hardest, remained focused around 1%. Since the Federal Reserve does not control that rate, if bond traders thought high inflation was going to be with us for even the next 24 months, the 2-year note should be much higher and create the dreaded inverted rate curve, but it hasn't. Janet Yellen, the former chairperson of the Federal Reserve and current Secretary of the Treasury, stated that in her opinion, inflation has been cranked up by a series of one-time events and should be back down around 2% by late 2022. The bond market appears to agree with Sec. Yellen.

Another area where the headlines clustered was around the rather substantial decline in the market price of Bitcoin, meme-stocks, and SPACs, all of which we have written about as dangerous and unstable investments. Bitcoin is down about 40% since November, an impressive decline, but only in second place to its 52% crash from April through July of last year. SPACs, those, "Invest now and we will tell you what we are going to do with your money later." shares, on average, are down about 50%. GameStop stock has spiraled down about 68%.

In our humble opinion, the headlines should have been about the Conference Board's Index of Leading Economic Indicators (LEI). That very reliably predictive index rose 0.8% in December after rising 0.7% in both October and November. In the six decades since the Conference Board started reporting on that venerable set of numbers, it has never failed to provide at least six months warning when a recession was on the way. The Conference Board's chief

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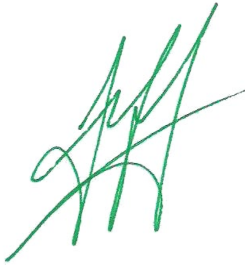
economist wrote that the Omicron outbreak put a dent in the December numbers and is likely to slow things down for a few months but that, in his opinion, once the outbreak trails off, probably in March, the economy is showing every sign of surging back to levels better than we saw last year.

Meanwhile, the Omicron variant is hurting economic growth, not because of shutdowns or any governmental action, but simply because there are a lot of people out sick. Union Pacific in its earnings report admitted that it underestimated the impact and was hit hard in its ability to deliver goods over the past couple of months on time, or in some cases, at all. Restaurants, school districts and a host of others are feeling the pain. The good news is that the new infection wave appears to have peaked along the East Coast where it hit first in the U.S. Since household balance sheets are still flush with cash, once this wave recedes, things look good for the party to resume.

The U.S. economy is still going strong and well on the way to a full recovery of where it would have probably been without the pandemic. As we predicted, Omicron is putting a dent in the growth rate, but is nowhere near reversing it. This inflation surge continues to appear as a passing event and unlikely to become entrenched. On the downside, the possibility of Russia invading Ukraine in an attempted remake of Germany's Pre-World War II actions looks more and more likely. We have written before that early 2022 would likely have some big bumps, but we remain confident that is all they are.

Until next week, we remain faithfully at our posts making every attempt to do what we do for you better, quicker, and more effective with each passing week.



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