WaterRock Global Asset Management, LLC

MARKET REVIEW & OUTLOOK

March 2021

BREAKING NEWS

- The March Jobs report showed the unemployment rate continuing to decline, dropping to 6% and the jobs added for the month beating expectations, coming in at 916,000.

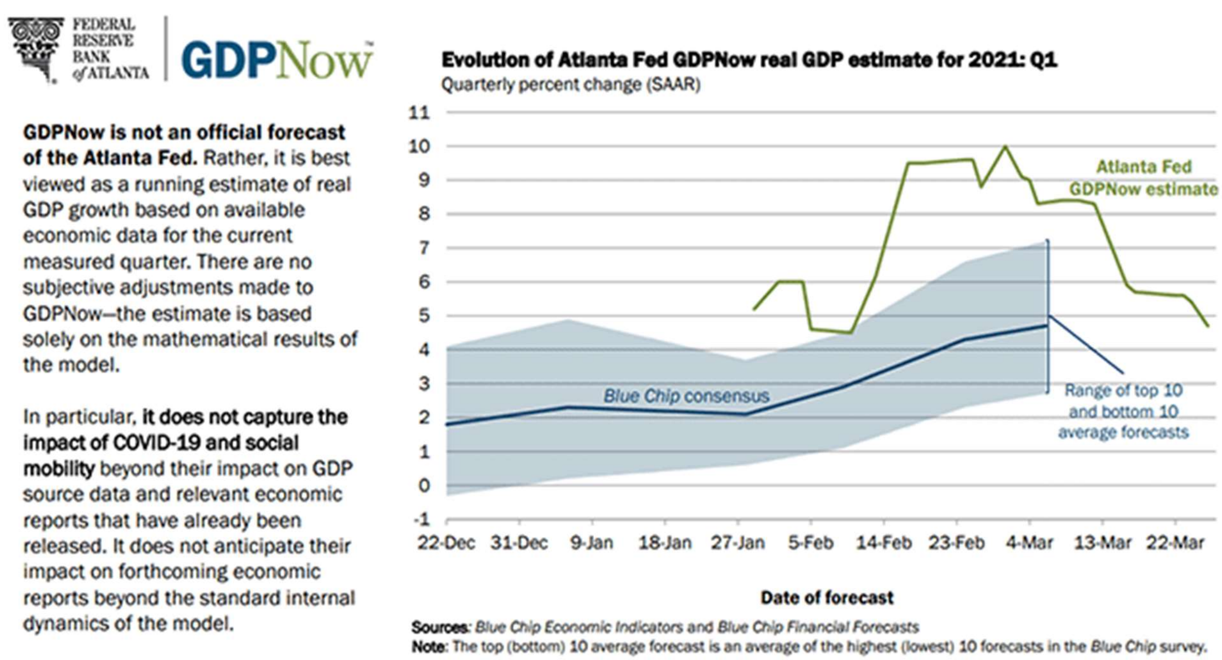
Back to our regularly scheduled program…

KEY TAKEAWAYS

- Global Equities were bifurcated, with the Dow 30 and S&P 500 continuing to fly high again setting all-time record highs. However, most other areas chopped sideways as higher interest rates brought out bouts of weakness during the month.
- The 1st quarter GDP report continues to look strong as cases and hospitalizations have dropped significantly since early January. Additionally, vaccinations continue to expand with the addition of JNJ into the fold.

The U.S. Economy

The stimulus package finally was passed, and checks began reaching people in mid-March, which should provide an additional boost to 1st quarter GDP. As shown in the chart below, the human forecasters, i.e. the Blue Chip consensus is making steady progress up in their forecast, though the computer driven GDPNow forecast has come down to meet where the Blue Chip has moved up at approximately 5%. However, with the additional vaccinations and economies opening throughout the U.S., 2nd quarter could end up with gangbuster growth.



Source: https://www.frbatlanta.org/cqer/research/gdpnow

Stocks and Bonds

The fixed income markets continued the theme of the year which has been steadily higher interest rates, as the yield on the 10-year Treasury advanced to the next major level of resistance at 1.75%. The continual rise in base Treasury rates again had a negative impact throughout the fixed income complex, including high quality fixed income. High-quality fixed income, as measured by the iShares US Aggregate Bond ETF, again saw negative returns, finishing the month with a loss of -1.24%. Once again, the diversifying fixed income vehicles, that represent approximately half of the fixed income exposure, fared much better than the index. The U.S. 10-year treasury bond yield ended the month at the top of the range at 1.75%, up from February's close of 1.46%.

The U.S. Large Cap ex-Tech stock market continued to climb but other areas made little progress in the face of continued yield increases. The Dow Jones Industrial Average soared +6.62%, the S&P 500 jumped +4.24%, and the small cap Russell 2000 slipped -0.94%. The developed international markets followed a similar, though less robust, path as the U.S. The MSCI EAFE iShares Core International Developed Markets ETF Index climbed +2.33% and the MSCI Emerging Markets iShares Core ETF Index fell -1.15%.

In March, we saw sector performance to the extreme in a green direction. Every sector saw gains for the month, especially the more value-oriented sectors. As the chart below shows, generally Value oriented sectors dominated the strength and in a rare occurrence, Tech was at the bottom of the pile.

The best performers were…

- Utilities: +9.73%
- Industrials: +8.65%
- Consumer Staples: +8.26%

The worst relative performers were…

- Energy: 2.60%
- Communication Services: +2.45%
- Technology: +1.62%

Source: https://www.sectorspdr.com/sectorspdr/tools/sector-tracker

Oil Report

In March, crude oil started the month very strong on continued optimism that economies were going to continue to reopen. As the month wore on, several countries in Europe reinstituted lockdowns which took the bloom off the rose. Then supply disruptions in the Suez Canal combined with continued cooperation from OPEC+ provided enough of an offset for prices to spend the balance of the month chopping around the $60 level. The current NYMEX WTI Crude Oil futures settled at $59.16 and posted a loss of almost 4% from the prior month close of $61.50 a barrel. The price for RBOB gasoline followed a similar path to crude oil, though eked out a small gain. RBOB finished slightly higher up 1% for the month of March. The oil patch continues to look across the valley as the news out of Europe was not great but hope springs eternal. Again, even though gas prices continue to rise, the impact on the consumer will still be mitigated by the large contingency of people working from home. The trucking industry on the other hand is moving a lot of goods and thus getting hit by the sharp rise in prices.

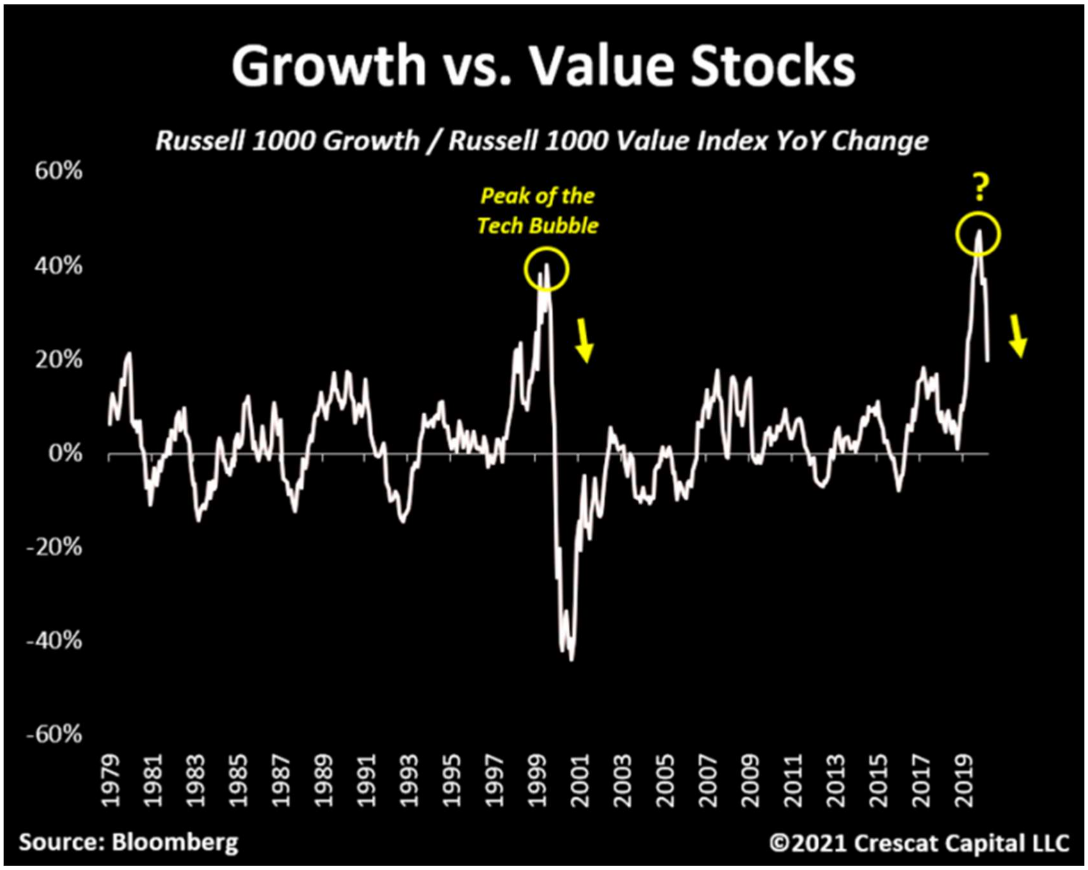
The Rest of the Data

The news cycle seems to be that good news is a given going forward, which with the additional stimulus may well be true. As with asset prices, the economic news is starting to get that, “this is as good as it is going to get”, feel. As any mountain climber knows once you reach the summit the only place to go is down. That’s not to say we fall off a cliff, but the peak of good times/economy may be right in front of us. The strength of commodity prices in combination with the continued rise in long term Treasury yields merit monitoring.

The February ISM Manufacturing Index increased 2.1 points to 60.8 from January’s reading of 58.7, as previously mentioned, the strong commodity prices are a potential sign of inflation as prices paid continue to strengthen. However, the ISM Services Index fell to 55.3 from 58.7 in January. Any reading above 50 generally indicates improving conditions. Consumer confidence soared to 109.7 in March, which compares to a downwardly revised figure of 90.4 in February. The unemployment rate dropped, coming in at 6.2%, as the economy added a stronger than expectations, 379,000 jobs in February. The Consumer Price Index for All Urban Consumers (CPI-U) was up +0.4% in February on a seasonally adjusted basis. Over the last 12 months, the All-Items Index increased +1.7% on a non-seasonally adjusted basis. Overall, these numbers are painting the same picture as last month, stable middling single digit growth rate for the economy. The risks to growth rates still seem to be to the upside with building tailwinds. The ongoing area of concern is the strength of raw material costs and pressure from rising interest rates. The Fed remains steadfast in their belief that the inflation, which is likely to soar in the next couple of months, is transitory. We will probably have a much better sense of what the impact of interest rates and inflation will have on markets and the economy as time passes in April.

Summary

The story of the last couple of months has not really changed, expected improvement has become realized improvement. The Fed is hoping that the improvement will continue through the bump in inflation and well into the end of the year. The bond market seems to accept the notion of continued economic improvement but is not as certain that inflation will fade off into the sunset. We are starting to see pockets of the equity market share some of the bond markets concern. As seen in the chart below, Growth, dominated by Technology, has significantly underperformed Value the last few months. Technology has had massive outperformance the last 10+ years supported with super cheap money. If money becomes dearer, that likely takes some of the bloom off Growth stocks.



Source: https://www.zerohedge.com/markets/caught-between-roaring-20s-rock-liquidity-crisis-hard-place

To reiterate, this is not meant to cause fear but to draw attention to extended valuations and potential downside risks. We have built our asset allocation models with dynamic features and quarterly rebalancing, both in fixed income and equities. If the markets continue to march higher, we will capture some of those gains and reallocate to less volatile high-quality bonds. If the equity markets enter a period of negative performance, we have dynamic investment vehicles that utilize rules-based defense mechanisms to reduce the risk of the portfolio. Further, if the market gets too extended on the upside, some of the vehicles will capture partial gains and wait for the extension to correct.

If you have specific questions about your portfolio or financial situation, we are here to help. Long-term financial planning is designed to deal with uncertainty like those we discussed above. Our portfolio management process is to design a prudent allocation across many asset classes. Equities are for long-term growth and several vehicles that we utilize offer defensive mechanisms to mitigate equity market declines.

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