John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday December 2, 2020

U.S. stock indexes have reached record high levels. The Dow Jones Industrial Average breached 30,000 for the first time and both the NASDAQ and S&P 500 also reached new highs. Four years ago, on Election Day 2016 the Dow closed at 18,332. At 30,000 the Dow is up 63.6%. That is quite a run. Something prognosticators last March would have labeled as impossible. The question now is can this continue? Yes, there are vaccines being readied for wide spread distribution. It is now possible that we will be able to go out to restaurants, theaters, shopping and traveling by next spring or early summer. Even now the American economy is operating as an engine of prosperity. The jobless rate keeps falling in spite of a new surge in Covid infections. The Atlanta Federal Reserve bank estimates the economy will grow 5.6% this quarter, which is now two-thirds over. There are risks and uncertainties. Many companies have changed their business models and discovered they can operate with fewer employees. That means it may take a while before pre-pandemic full employment is reached.

The editorial board of *The Wall Street Journal* has this to say about where we are and the risks ahead: "Investors are looking at the medical miracles of Covid vaccines that portend the end of the pandemic in 2021. The fading chance of post-election trauma helps, but the biggest boost to the market has come from the prospect of a Republican Senate acting as a check on Joe Biden's destructive tax increases. He can still do damage with regulation, but that takes more time and is subject to legal challenge. The two Georgia runoffs on January 5 producing a Democratic Senate are, apart from shutdowns, the biggest market risk ahead."

History tells us that stock markets can go up when Democrats are in control of the White House. It is just that the gains under Democrats have tended to be less than under Republicans. A gain of 30% instead of 60% in the coming four years might be disappointing to some, but acceptable to most investors. I was pleasantly surprised when Joe Biden selected Janet Yellen as Treasury Secretary for his administration. She was a solid leader as Chair of the Federal Reserve. I am sure her selection is a disappointment to the more radical Democrats, but in my view she is a wise choice and a signal that Biden understands the need for a solid, growing economy.

The Secretary of the Treasury has more power over the economy than generally understood. The current Secretary of the Treasury Steven Mnuchin has demonstrated that with his recent decision to end most of the Federal Reserve's special pandemic lending facilities on December 31, as Congress intended. These special lending programs were created as a part of the Cares Act in an emergency at the onset of the pandemic when the financial markets were in danger of melting down. The Federal Reserve did not actually do much lending under those programs. The Treasury provided $195 billion in Cares Act cash to fund the programs. The Fed used only $25 billion to make loans. The reason? The Cares Act worked. Financial markets healed as confidence grew thanks to the promise of the emergency lending programs. Small and large businesses found ample liquidity and access to credit. There has been and still is a lot of complaining about credit for cities and states. But they too have had adequate liquidity. New Jersey, for example considered asking for cash from the Fed but last week sold $3.7 billion in bonds paying 1.95% in the private market and the offer was oversubscribed.

Milton Friedman used to say that nothing is so permanent as a temporary government program. All too often that has been true and our economy has suffered from the clutter of government programs that should have been shut down. Secretary Mnuchin is doing the country a big favor by ending a temporary emergency lending facility that is no longer needed. Congress can always enact future emergency lending programs when and if another crisis comes along.

Back in the days when inflation was a threat to stock and bond markets experts paid a lot of attention to the velocity of money. That measures how often money changes hands. When money velocity rose so did inflation. Lately, with inflation and interest rates low the velocity of money has not gotten much attention. This year the velocity of money has plummeted. For the first time on record it dropped below one in the second quarter, meaning that the average dollar was exchanged less than once between April and June. In April the personal savings rate shot up to 33.6% of disposable income. As some parts of the economy reopened the savings rate came down but was still 14.3% in October, higher than in all pre-pandemic months since 1975. What I find amazing is that the U.S. GDP grew at a 33.1% in the second quarter as the savings rate shot up and the velocity of money plummeted. This says the underlying strength of the U.S. economy is far better than even optimists believed. A terrible pandemic and widespread lockdowns could not destroy the economy's ability to come bouncing back. The money velocity data also support the optimists' expectation of more future growth as vaccines are added to the economic mix. Consumers are sitting on a whole lot of cash. Some say they will hang on to the cash even after vaccines are widely available. I doubt that. Housing is booming.

Auto sales are robust. These indicate that once they feel comfortable consumers will spend extra cash and the savings rate will return to historical levels.

As for the near-term outlook for stocks, volatility has been collapsing, down to levels not seen since February. Falling volatility is a sign of investor optimism. There most likely will be pull backs from recent new highs. But the longer-term outlook remains positive for stocks.

I will have the next market review and update one week from today on Wednesday December 9, 2020.

All the best,

John Dessauer