INVESTMENT STRATEGY UPDATE

MARKET REPORT
QUARTER 1 • 2021

ASCENTIAL WEALTH ADVISORS

RECOVERY CONTINUES ONE YEAR LATER

Market Index	Q1 2021	Last 12 Mths (3/31/2021)	2020 Correction (2/19/20-3/23/20)
S&P 500	6.2%	56.4%	-33.8%
Dow Jones Industrial Avg	8.3%	53.8%	-36.5%
NASDAQ	2.8%	72.0%	-30.1%
Russell 2000	12.7%	94.9%	-40.7%
MSCI EAFE	3.5%	44.6%	-32.7%
MSCI Emerging Markets	2.3%	58.4%	-31.2%
BBG Barclays US AGG Bond	-3.4%	0.7%	-0.9%
Relative Risk Index			
DJ Global Conservative	-2.0%	9.6%	-7.5%
DJ Global Moderate	2.5%	35.5%	-23.7%
DJ Global Aggressive	6.6%	63.4%	-36.1%

The first quarter of 2021 marks the one-year anniversary of the start of the COVID-19 pandemic and the bear market correction that resulted. After bottoming on March 23, 2020, markets have recovered significantly, and they continued to climb higher this quarter. Whereas markets have made new highs, the economy is not quite back to pre-pandemic levels, but is improving with the help of large amounts of economic stimulus and increased economic activity spurred by the distribution of vaccines.

Concerns have surfaced that the unprecedented amounts of economic stimulus will cause inflation. This has put pressure on bonds, pushing long-term interest rates higher and bond prices lower in the US. In the first quarter, the ten-year US treasury yield rose from 0.93% to 1.74% and the 30-year yield from 1.66% to 2.35%. The market clearly expects interest rates to rise despite ongoing statements from the Federal Reserve that rates will remain low for longer, until both inflation and unemployment meet their targets. While unemployment has fallen to 6.2% in February 2021, after peaking at 14.8% in April 2020, there are still 9 million fewer jobs in the US than pre-pandemic, leaving room for continued economic improvement. Markets seems to believe this improvement will occur faster than the Fed is projecting.

The challenge to returning to pre-pandemic activity is now vaccinating enough people before new variants of the virus can spread broadly. While COVID-19 case counts worldwide have been rising again, vaccination rates are also encouraging. As more people are vaccinated, we are likely to see an increase in economic activity, fueled by stimulus money and pent-up demand for travel, entertainment, and services. We expect a surge in spending when consumers feel comfortable returning to more normal activities. This could mean a change in the top performing sectors, and suggests the need to use a forward-looking approach when considering investments.

2021 OUTLOOK

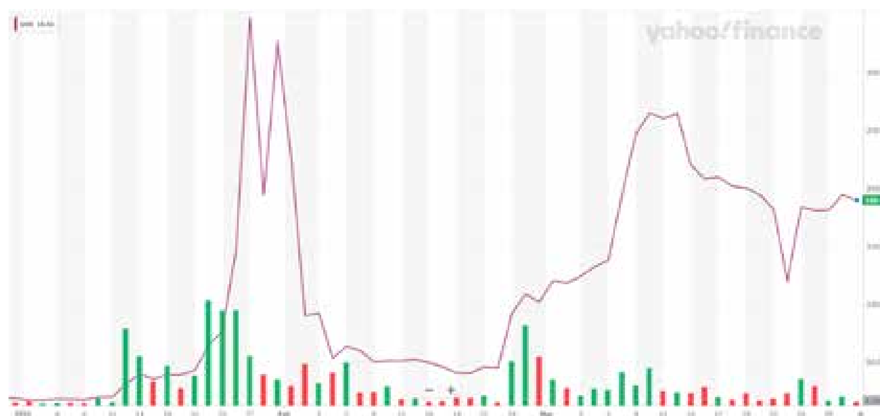
FIXED INCOME — In an environment of potential inflation and rising interest rates, we are in favor of utilizing active bond managers to guide fixed income portfolios. Although we see some near-term challenges, bonds remain an important tool for managing overall portfolio volatility and equity risk. We continue to favor owning alternative strategies as a complement to bonds, which helps with risk management and the inherent interest rate risk that some bonds carry.

US EQUITIES — We are optimistic that the economic recovery in the US will continue to propel stocks higher. Selectivity may be more important going forward, given the difference in valuations after the rise in stocks over the past year. We feel outperformance of value which we have seen in the first quarter will continue, and recommend a relatively equal weighting between value and growth at this time. Stocks generally have offered an inflation hedge, and remain a good option if inflation ticks up as well.

INTERNATIONAL EQUITIES — Foreign stocks are relatively cheaper than US stocks, with the MSCI All Country World Ex-US Index trading at a price to earnings discount of -25.7% relative to the to S&P 500 at the end of March. (JP Morgan, Guide to Markets, March 31, 2021) In addition, foreign equity markets are more heavily weighted to cyclical sectors which look attractive in a sustained recovery, and consensus projections are for higher earnings growth outside the US for 2021. We like foreign stocks for these prospects and feel exposure to them will be beneficial.

GAMESTOP – WHAT CAUSED THE FRENZY?

As January kicked off a new year, the media headlines shifted from talks around elections and vaccines to breaking news on a little-known company called GameStop, whose brick & mortar business model of selling video games, accessories, and merchandise, saw its stock price soar. In less than a month the company's stock price rocketed up almost +2100% driven by a socially engineered buying spree from small investors seeking to challenge Wall Street norms.



To understand what happened it's important to know the situation leading up to the boom in its price. GameStop was struggling and Wall Street firms knew it. Some of these firms, mostly hedge funds, were looking to profit from this weakness by using an investment strategy called short-selling.

"Short-selling" is borrowing shares from another investor, selling these borrowed shares, and buying them back in the future to return to their original owner. The goal of a short-seller is to buy the stock back at a lower price than what they sold it for and keep the difference. If the stock price goes down, they make money, if it goes up, they lose money.

There were lots of short-sellers in GameStop and this caught the attention of people on a social media platform called Reddit, where millions of users can discuss a wide-range of topics including stocks & investing. In the Reddit group, "wallstreetbets," followers realized if they started buying GameStop's stock, together they could push up the price and force the short-sellers to buy back their stock too. When short-sellers are forced to buy back their stock, it's called a "short-squeeze", which often leads to a self-perpetuating force pushing the stock price higher and higher.

The "wallstreetbets" movement accomplished its goal, with many of its followers profiting from the stock moving higher while at the same time inflicting large losses on the short hedge funds. During the month of January, the price of GameStop's stock moved up from $18.84/share (12/31/20) to a peak of $483.00/share (01/29/21), inflicting losses approaching $20 billion for multiple hedge funds who were short the stock.

However, by the end of March, the stock price had fallen back to $189.82/share, likely leaving some "wallstreetbets" followers with losses as well.

What does this mean for investors and the stock market? Not much. The situation in GameStop was somewhat unique and cannot be implemented at a large scale to impact the broader stock market. Investors who follow a diversified, long-term investment strategy automatically dampen the impact of individual stocks on their portfolios. Following a diversified strategy over time, and sticking with it, has shown to provide growth without the wild swings of owning individual stocks. If you would like to discuss any of these topics please don't hesitate to reach out to us, we enjoy hearing from you.

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