February 3, 2021

Graves-Light January '21 Market Commentary

Vaccinations, Politics and Trading Frenzy Share Center Stage

Market Overview:

The new year began with a sense of optimism, as investors were eager to place 2020 firmly in rear-view. With governments across the globe commencing their respective roll-out plans to drive mass-inoculation, markets continued to "look-through" the economic havoc that permeated across both the local and global economy. Instead, market participants have focused on the timetable to recover lost economic output as well as repairing a labor market with improving, albeit still bloated, continuing unemployment claims. Ultimately (and in theory), as the myriad of vaccine treatments gain critical mass, mobility restrictions could further loosen, with improved economic output following suit.

Unsurprisingly, and as often is the case, idealism and reality seldom (and if ever) operate in a shared space. As the month progressed, a discernible unevenness in vaccine rollouts increased investor caution as the markets were explicitly reminded that a return to normal is still far away for much of the global economy.

Asset Performance:

Having started the year on an upward trend, equity performance waned as the month progressed, with notably weak performance over the final week of January. The S&P 500 finished the month at -1.0%, including dividends, with month-to-date gains entirely wiped out over the final two days of trading. The tech-heavy Nasdaq was comparably resilient, finishing the month +1.4% despite shared weakness over the final week.

We also draw attention to the US 10-Year Treasury Note which provides a broad barometer for expectations in US GDP growth, Central Bank (Fed) behavior, inflationary trends and fiscal spending. Since peaking at 1.14% on January 12th (from 0.92% on Dec. 31), the yield on this instrument rapidly retreated to 1.01% on January 27th before settling at 1.09% at month-end. Amidst this move were a litany of drivers, including a heightened likelihood that the Biden administration will have to walk-down from its targeted $1.9tn relief plan, a consistently "dovish" Federal Reserve which is anchoring expectations for low rates indefinitely, and additionally, an increased likelihood for vaccination delays. Each of these items increase investor caution, hence driving demand for defensive assets such as US government bonds while lowering the 10-Year rate from its recent highs (Remember: rates move inversely with price). In summary, the direction of travel for the US 10-Year Note encapsulated this tale of two halves witnessed in January as outright optimism became more tepid as the month progressed.

Separately, a frantic retail-led trading frenzy near month-end culminated in several brokerage houses imposing trade restrictions. Given the unprecedented nature of this event, the oft-cited Cboe VIX Index – a measure of expected volatility also known as the "fear gauge" - temporarily surged from the low 20's to 36, also dampening investor enthusiasm. The 10-year average for this index sits just below 20.

As previously mentioned, longer term government yields were volatile over the course of the month, with the US 10-Year ending the month at 1.09%, +19bps from year-end 2020 levels. We highlight that the 2-Year Note remained unchanged at 12bps, reflecting a gradual steepening of the US Treasury curve. Flat short-term rates are underpinned by accommodative monetary policy from the Federal Reserve.

Key US Index Returns	2020	Jan, '21
S&P 500	+18.3%	-1.0%
Nasdaq	+44.9%	+1.4%
Dow Jones Industrial Average	+9.7%	-2.0%

Relevant Fixed Income Yields	YE 2020	Jan, '21
US 10-Year Treasury Note	0.92%	1.09%
Investment Grade Corp. (C0A0)	1.8%	1.9%
High Yield Corp. (H0A0)	4.2%	4.3%

Source: Factset as of 01/31/21

Closing Thoughts:

While markets continuously evolve, we remain steadfast in approach. We reiterate our view that a bullish market narrative remains largely priced in. To this effect, January's performance reflects the fragile nature of markets were potentially adverse events to transpire, particularly with regards to the large-scale rollout of vaccinations across the globe. While we do see signs of optimism for an economic rebound, we also believe that amidst great uncertainty investors should be all the more prudent in *not* reaching for returns. As such, we remain focused on long-term portfolio positioning, namely avoiding sectors where equity multiples appear stretched, and additionally, lowering long-term interest rate exposure in order to protect principal.

Warm regards,

Ash Heatwole, CFA

Portfolio Manager

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