2021 Market Outlook

The forecasts, estimates, risks listed below are a summary of 2021 outlooks from Barron's, The Wall Street Journal (WSJ), Fortune, BusinessWeek, Charles Schwab, Merrill Lynch, and my analysis of economic, business, and investment trends.

The markets have been strong despite the health and economic crisis. The markets could have another good year in 2021. The market has pulled forward performance and it could reduce returns in future years.

The technicals/price analysis remains more important for analyzing the markets because the fundamentals/valuations are stretched.

Bullish Case

- Vaccines have been approved and are being distributed. Vaccines have to turn into vaccinations to get to full herd immunity. Vaccinations and herd immunity are keys to a full economic recovery. Vaccines give us a light at the end of the tunnel... More on this in my 2021 Economic Outlook that should be out next month.

- Trillions of dollars in liquidity, relief, financial aid. At the time of this writing, President Biden has issued a proposal to raise another $1.9 trillion to help with the health and economic crisis. Now that the Democrats possess both branches of the legislature as well as the executive branch, a large aid/stimulus package is possible.

- The economic and earnings comparisons of 2020 versus 2021 will be easier to beat and could be bullish for the markets.

- The market has had a bullish bias for about the last four years. It tends to rally despite bad economic and business conditions. Some of the reasons for the bullishness is listed below.

- I've written many times about how once the market makes new highs, it is likely to keep making new highs. This is one of the reasons for the market's strength.
  See the Technical/Price Analysis section to understand new highs.

- Most recessions are exacerbated by a credit crunch. With all the liquidity from the Fed, we may avoid a credit crunch during this recession. The bond markets have stabilized.

- The Fed has stated several times that they will do all they can to help the economy. The Fed has the economies and investors back.

- Low-interest rates have allowed some homeowners to refinance their homes and the extra cash is spurring spending helping the economy.

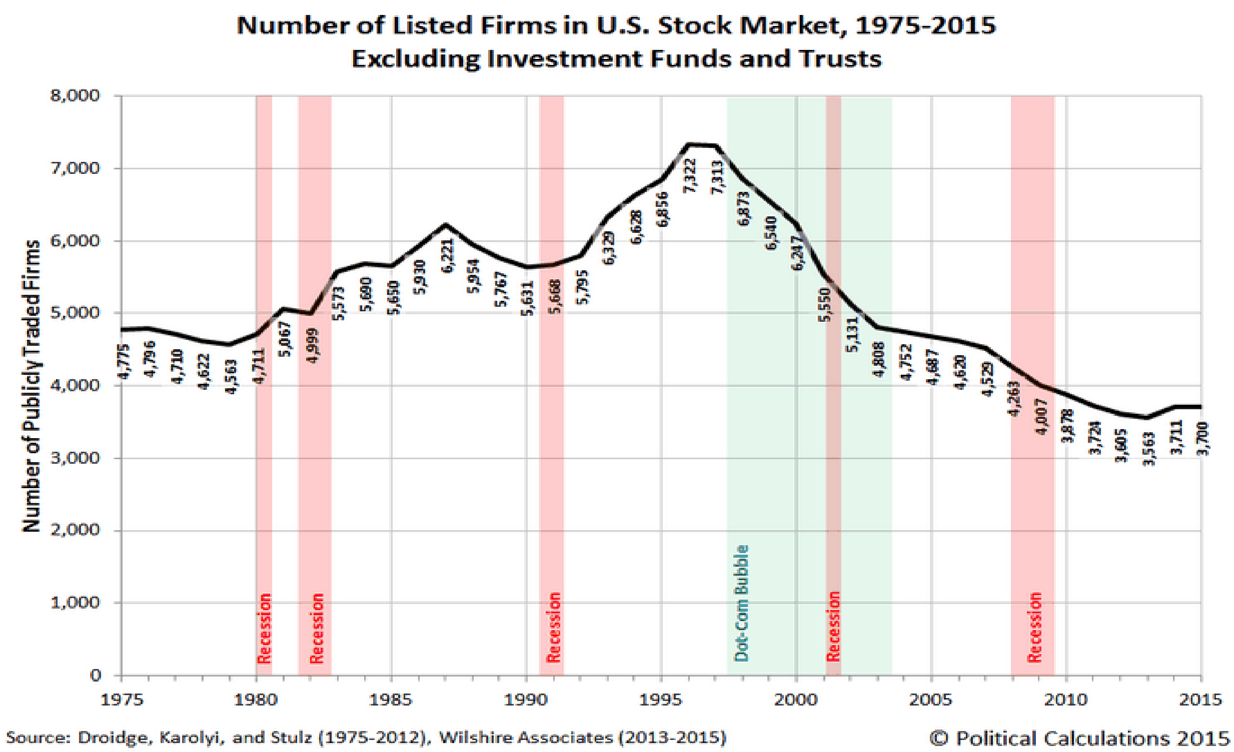
- Low oil prices and less driving is saving consumers money

- FOMO, fear of missing out. There are lots of investors like my clients and me who are trying to get invested for the next economic and market cycle. My clients and I were about 20% invested at the start of last year. We are now around 70% invested.

- Traders, speculators, and investors like me are buying on any pullbacks to add to our portfolios

- TINA, there is no alternatives, many investors believe that stocks remain the best investment.

- There are fewer stocks to invest in. Below is a chart that shows the decline in listed stocks.



Source: NBER, Political Calculations

There have been many Initial Public Offerings in 2020 and more are expected in 2021. We are probably close to 4,300, well below the peak in 1996. In economics, less supply leads to higher prices.

- Certain parts of the economy are doing well: housing, autos, online shopping, technology.

- There is less selling during the bear market last year because of 401Ks. There is about $5 trillion in 401Ks and many of these accounts are invested in target funds that see little selling.

- There is more money managed by financial advisors and they're telling their clients not to sell. Financial Advisors use asset allocation and rebalancing to provide risk reduction.

  Because the markets are overvalued, financial advisors are putting their clients into alternative, illiquid, high cost, risky investments. How do I know? I get calls and emails all the time asking me to consider these investments for my clients from salespeople. Their pitch - high and trailing commissions.

Bearish Case

- The markets remain overvalued. See valuation section below

- Most economists and analysts agree that we have a K economy. Certain sectors in the economy are growing (housing, mortgages, technology, grocers, online retail), but some sectors are struggling (retail, restaurants, airlines, small businesses, entertainment, many service workers).

- The vaccination effort has gotten off to a poor start. Last year, investors thought that we would get past the health crisis during the summer of 2020. According to health experts, we need at least 70% to achieve herd immunity. This will be a challenge because we're such a large geographically, diverse country. There is also a percentage of the population who will not get the vaccine for various reasons.

  The bottom line for the above reasons, it will take more time to achieve herd immunity. The earliest would be this summer.

- I was surprised to read that many experts, analysts are concerned about inflation, and the potential for higher rates. Since most valuation models include inflation and interest rate factors, rising rates could be a headwind for the markets. When rates rise most assets become less valuable and vice versa. The models are basically saying when rates rise, the risk-free rate may offer a better opportunity with less risk and other assets become riskier and less attractive when rates rise. I will write more about inflation and interest rates in my 2021 Economic Outlook.

- President Biden has a big list of problems to tackle: Covid, the economy, small business, bringing down health care costs, education and training for this economy and the future, Iran, China, North Korea, Russia, climate and the environment, immigration, racial and economic inequality

- The markets have not priced in the new President Biden and his new economic policies. His policies are a dramatic departure from President Trump. Biden will be focused on workers, unions, income inequality, climate change. Trump was focused on the economy, trade, and the markets.

  One member of President Biden's Council of Economic Advisors is Heather Boushey. Her research and focus are on wealth inequality. Again, President Biden's economic agenda is a big change from President Trump and the markets haven't adjusted to these changes.

- President Biden will have to raise taxes on corporations and the rich. The markets have not priced in higher corporate taxes. To make sure the economic recovery is on solid footing, tax cuts may not occur in 2021, but 2022. See fundamental section.

- There is a lot of speculation in the markets. Younger participants are having an impact on the markets. They are speculating in: Tesla, bitcoin, penny, and low-priced stocks, options. According to the WSJ, 20% of the market volume are these young participants. Tesla is having an impact on the S & P index, see Technical/Price anlalysis section.

- We don't know how much the U.S. and global economic damage will be done because of this pandemic. So far it's been terrible. Parts of the market are reacting as though there is no damage, risk, and uncertainty.

- The markets have celebrated all the relief, aid, and liquidity released into the economy and financial markets. The reason why there is so much money released into the economy is high unemployment, small businesses, and many low-income consumers are struggling, the economy is in a recession, and there is lots of uncertainty that will take lots of relief, aid to get to the other side of this pandemic.

- Companies, federal, state, and local governments have too much debt and will probably be headwinds in the future.

Valuations

Below is a chart that shows the history of P/Es for the U.S.:

Chart | Table   Share

Current S&P 500 PE Ratio: 24.68 +0.00 (0.02%)
4:09 pm EDT, Fri Oct 14

Mean:	15.62	
Median:	14.64	
Min:	5.31	(Dec 1917)
Max:	123.73	(May 2009)

According to the chart, the average P/E is about 15.62. It's normally best to invest when the market P/E is below 15.

Here are the valuations for the S & P and Dow 30:

THE WALL STREET JOURNAL.

EQUITIES

Dow Jones Industrial Average

31176.01 ▼12.37, or 0.04%
High, low, open and close for each trading day of the past three months.

	Last	Year ago
Trailing P/E ratio	29.53	21.34
P/E estimate *	25.45	19.57
Dividend yield	1.94	2.17
All-time high	31188.38, 01/20/21	

Current divisor 0.15198707565833

S&P 500 Index

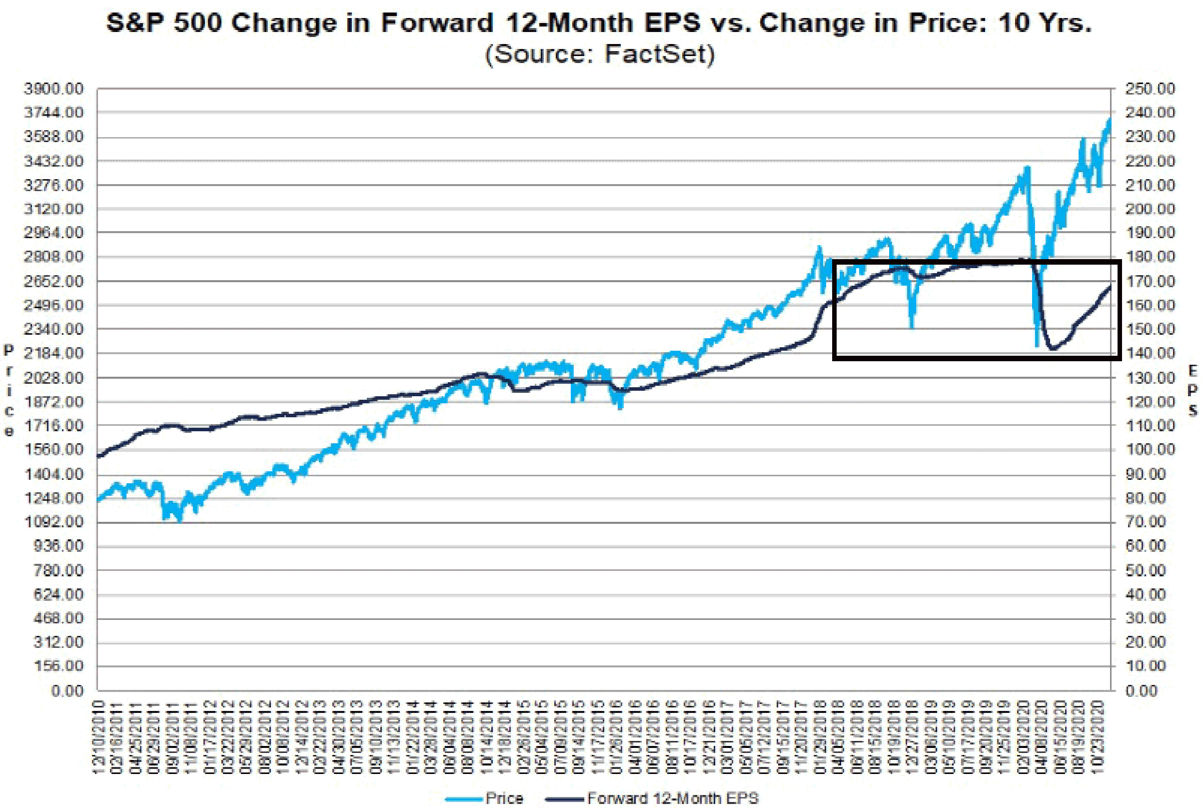
3853.07 ▲1.22, or 0.03%
High, low, open and close for each trading day of the past three months.

	Last	Year ago
Trailing P/E ratio *	40.98	26.00
P/E estimate *	24.15	19.45
Dividend yield *	1.56	1.80
All-time high	3853.07, 01/21/21	

*Weekly P/E data based on as-reported earnings from Birinyi Associates Inc.; †Based on Nasdaq-100 Index

Market P/E multiples are near historic highs. The markets are overvalued. Portfolio managers and analysts justify the higher multiples due to: the Fed's liquidity, low inflation and interest rates, FOMO, TINA, lower supply of stocks, certain participants in the market do not pay attention to valuations. Some of this is true, but they do not justify these high multiples. I do agree that multiples could be higher for the above reasons.

The P/Es, valuations of the markets are growing faster than earnings growth as the chart below shows:



When the black line (EPS) is greater than the blue line (prices) then the markets are undervalued. When prices are greater than EPS then the markets are overvalued. EPS has barely budged since 2018, but prices are up about 30%. There is a big gap between EPS and market prices. Again the markets are overvalued.

Last year, earnings will probably be down about 15%, but the market was up about 16% anticipating that things would be better by the end of 2020. The markets have been wrong. The markets have brought forward some gains, so future gains could be smaller. Investors need growth, especially through earnaings and earnings have barely grown.

Below are my target forecasts for the Dow 30 and S & P 500:

2021 FORECAST					
	EARNINGS ESTIMATES	**P/E**	**FORECAST**	**CURRENT PX**	**PTNTL %**
DJIA	1210.766208	18	**21,793.79**	30,814.00	-41.39%
DJIA CURRENT P/E		**25.45**	-		
S & P	172	18	**3,096.00**	3,798.00	-22.67%
S & P CURRENT P/E		**22.08**			

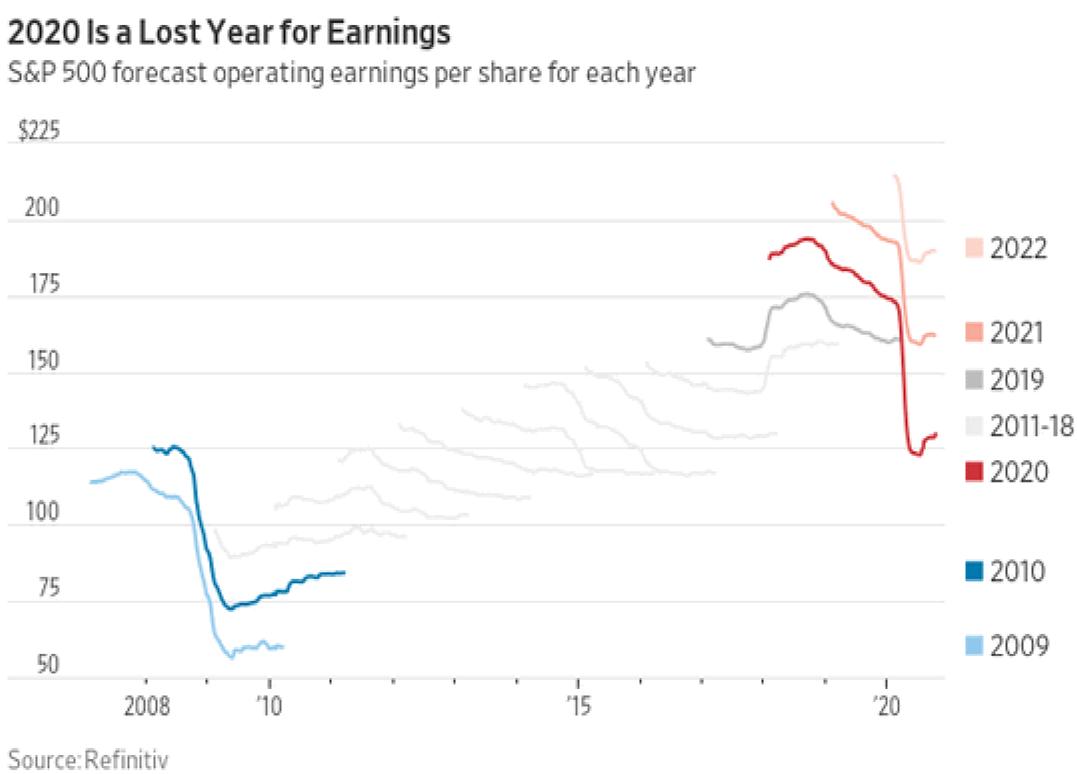
Source: Barron's, WSJ

In a perfect market with low risk and no inflation, the P/E could be 20. If we reduce by expected inflation of 2%, then the P/E could be 18. I use 18 in the above price targets. It should be lower because of the risks listed in the above Bearish section.

The markets are very overvalued.

Currently, the 2021 S & P earnings forecast consensus is about 172. Late last year the forecast was about 200. 2021 forecasts are dropping again.

The chart below shows how most year's earnings forecasts are too optimistic and come down as earnings are reported each quarter. Notice 2018 was the exception where earnings forecasts were adjusted upwards thanks to President Trump's tax cuts.



Also, notice how earnings fell in 2020 to about 130. Earnings comparisons from 2020 to 2021 will be easy to beat and this could help the markets when earnings are reported. Again the problems are valuations.

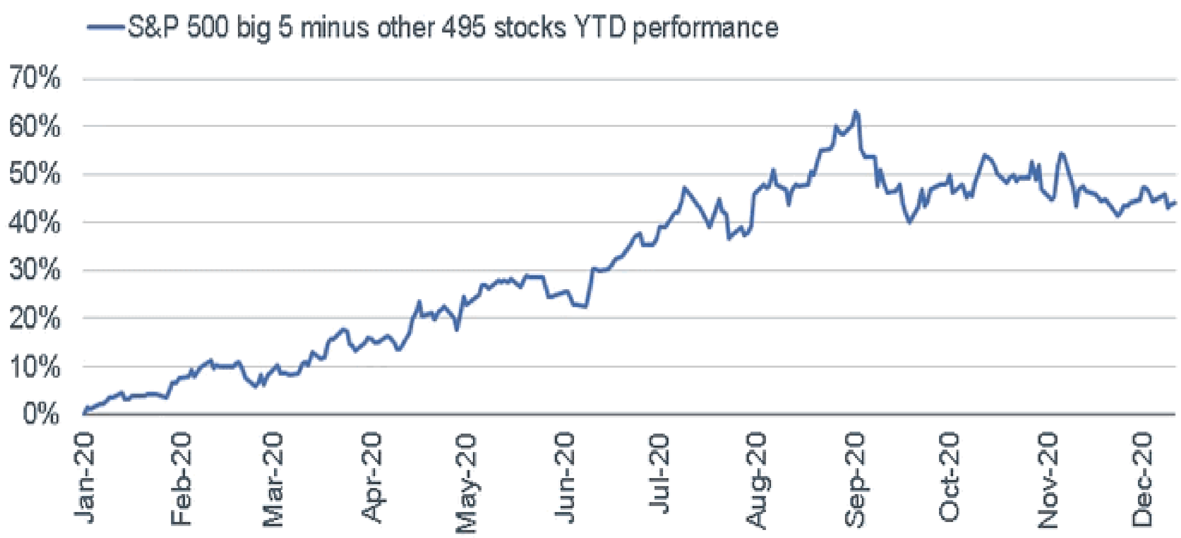
Future estimates may have to come down as it's anticipated that President Biden will raise taxes.

Technical/Price Analysis

5 stocks have an unusual influence in the S & P 500, and they beat the other 495 stocks.

Below is a chart of those 5 stocks:

Big 5 Has Trounced Other 495



Source: Charles Schwab, Bloomberg, as of 12/11/2020. Big 5 stocks include Alphabet, Amazon, Apple, Facebook, and Microsoft. **Past performance is no guarantee of future results.**

These stocks as a group peaked in September but they have been going sideways since July.

There are lessons here:

Lesson #1: What the market winners in a cycle aren't likely to be the winners in the next cycle. Below are the market winners for each decade. Notice that most of the winners for each decade change.

Biggest Gainers of the '80s*

By total percent price gain from
12/31/1979 to 12/29/1989

COMPANY NAME (SYMBOL)	% GAIN
1. **Circuit City Strs-Carmax Grp** (CC)	8,252
2. **Limited Inc** (LTD)	6,100
3. **Hasbro Inc** (HAS)	5,582
4. **Home Depot Inc** (HD)	4,997
5. **Wal Mart Stores Inc** (WMT)	4,032

* Only companies included in the S&P 500

Biggest Gainers of the '90s

By total percent price gain from
12/29/1989 or first trade date

COMPANY NAME (SYMBOL)	% GAIN
1. **America Online Inc** (AOL)	79,629
2. **Dell Computer Corp** (DELL)	72,445
3. **EMC Corp** (EMC)	69,638
4. **Cisco Systems Inc** (CSCO)	64,498
5. **CMGI Inc** (CMGI)	61,189

Source: Ned Davis Resource

2000 to 2001 best gainer list

A $1,000 investment a decade ago would today be worth:

1. **Apple (AAPL) -- $32,280**
2. **Southwestern Energy (SWN) -- $31,880**
3. **Cliffs Natural Resources (CLF) -- $26,460**
4. **Coach (COH) -- $21,320**
5. **Ventas (VTR) -- $19,420**
6. **Cognizant Technology (CTSH) -- $18,870**
7. **CarMax (KMX) -- $15,080**
8. **Freeport-McMoRan Copper & Gold (FCX) -- $14,630**
9. **Cummins (CMI) -- $13,010**
10. **Range Resources (RRC) -- $12,440**

I keep hearing analysts, investors on the cable financial news channels that investors need to invest in growth and keep mentioning the 5 top S & P stocks. Normally the markets and time are not kind to these market leaders.

Lesson #2: Nobody can predict what is going to happen next year, 5 years, 10 years from now. As with earnings, it is best to monitor economic and investment trends and adjust and adapt. Also, it helps tremendously if you buy when assets are cheap/undervalued. Entry into an investment is key.

Once prices break out to new highs, we can expect prices to continue to make new highs. I've written about this many times. Here is what I wrote in November 2017:

"One of the main reasons why this market has been strong is because once prices break to new highs, most of the resistance and supply is gone, and it will be easy for prices to continue to make new highs. I rarely hear market analysts on cable financial news talk about this. Below is a long-term chart that shows the breakouts and new highs over the last 18 years:

Source: erlangerchartroom.com

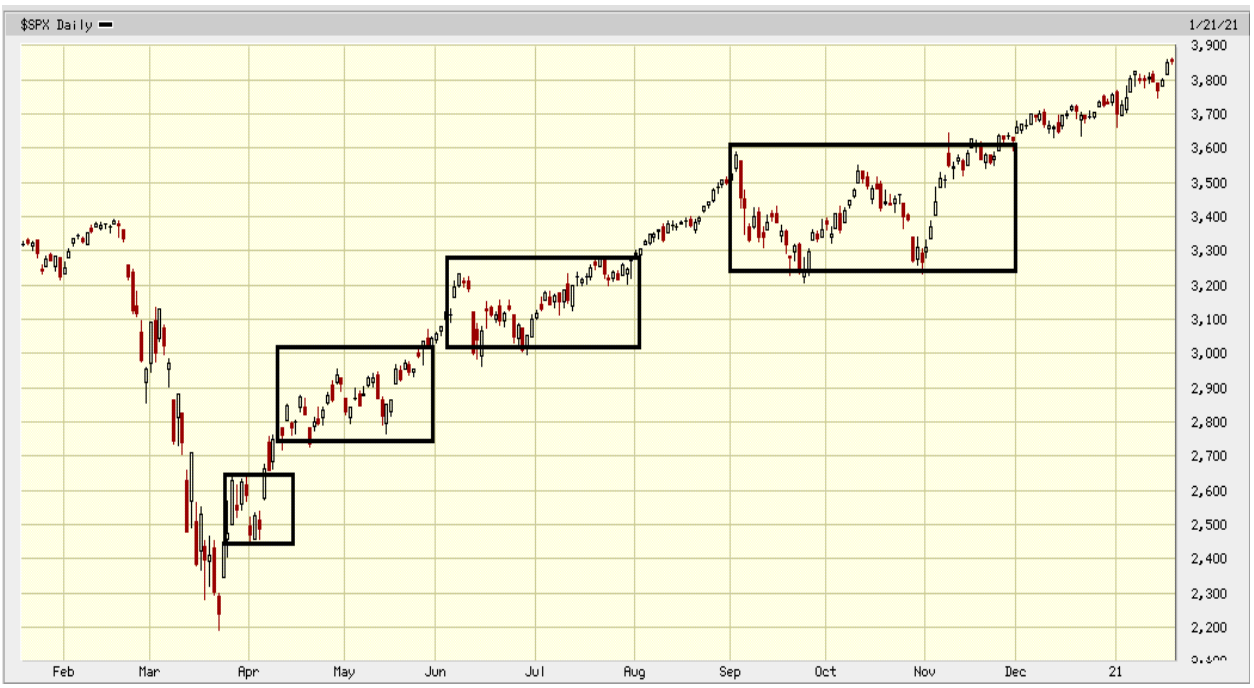
Let’s review the chart and breakouts:

• The Dow 30 was stuck below 11,500 from the late 1990s to 2006. Once prices broke above 11,500 the market was able to make new highs for about another year. Notice that after prices make new highs, many white candles are made. Many large candles show strength. This is true in each breakout, especially the breakout that started late last year.

• Prices were stuck below 14,000 from 2007 to 2013, and prices finally broke out to new highs. Prices were able to make new highs until 2015. Prices bottomed in 2009 at around 7000. There was supply resistance at 8000, 9000, 10000 to 14000. Once all the supply and resistance was taken out, prices were able to make new highs for a couple of years. Earnings growth and a recovering economy, low-interest rates, and inflation also helped market performance.

• Prices were stuck below the 18,000 level from 2014 to 2016. Prices broke out to new highs in late 2016. Prices have been making new highs all year. We can expect prices to make new highs in 2018. How much more depends on earnings and if investors will be willing to pay.”

Here is a current chart of the market:



Let’s review the chart:

- The markets entered into a bear market last March as the markets were down about 35% A market is considered in a bear market when it is down 20% or more from its previous peak. When it’s associated with a recession, a bear market is more serious. The National Bureau of Economic Research declared the U.S. entered a recession in February 2020. We remain in a recession.

- As described in the previous section about “new highs” we can see prices make a move and then consolidate/pause. Once the pause ends the next move occurs. The market broke out to new highs last November, so we can expect the market to continue to make new highs this year.

- Where will prices consolidate, pause next? Round numbers is one of the clues we can use. In this case 3,900, 4,000 could also be a major resistance, selling level.

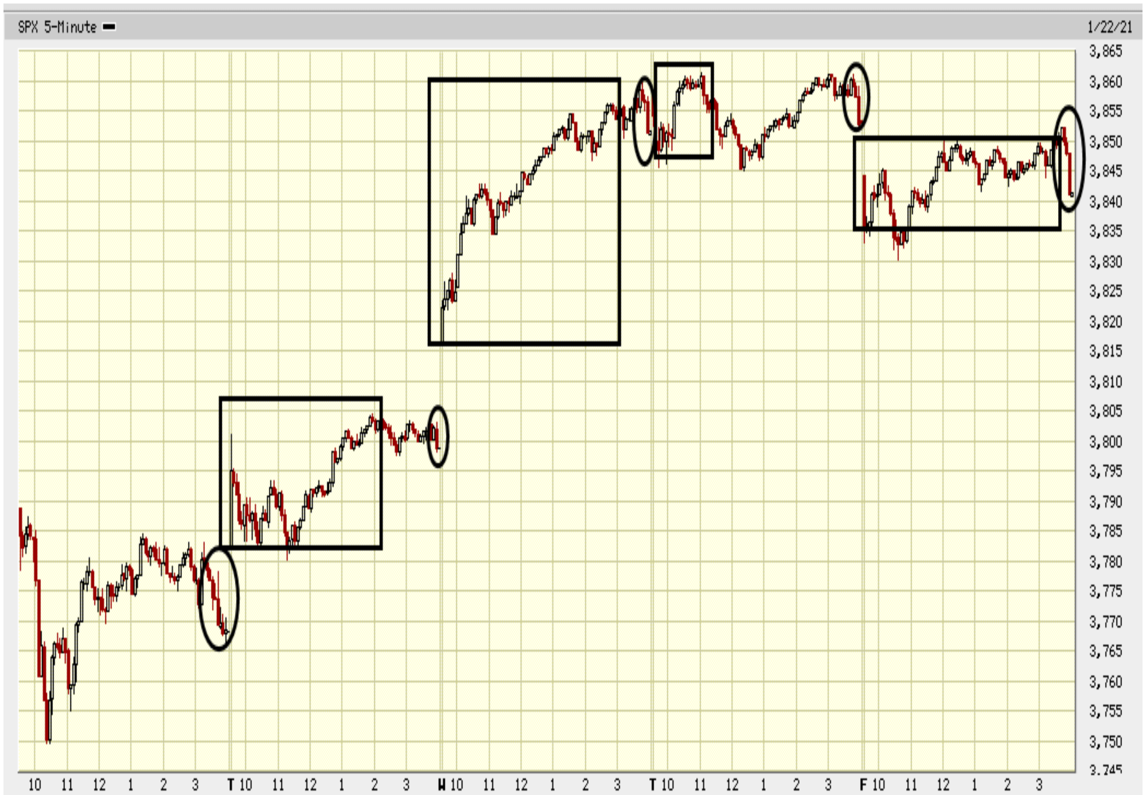
- When there is a major move, the move can take five to seven smaller moves within the major move. So far there have been 4 smaller moves, also called steps. The major move is probably about 70% (4 steps divided by 6 step average) done. I will write about what normally happens after a major move with 5 to 7 steps in a future update (Hint: I’ve written about retracements, Fibonacci a few times).

Since the “big 5” have been consolidating, what is moving the market? See chart below:

The chart above is for Tesla. Tesla was added to the S & P this last December. Because of Tesla’s large market cap and high price, Tesla will now have an influence on what happens to the S & P. We can see Tesla breaking out to new highs. It is consolidating, pausing now.

Volume is declining (volume could be considered money moving in or out) so the consolidation may continue.

Over the last few years, I noticed buying at the end of each day, probably by financial planners. I am now noticing selling at the end of each day. The 5-day chart below shows this pattern:



It will be interesting to see if this pattern of up during the day (rectangle areas) and profit-taking at the end of the day (circled areas) continues. I will monitor this phenomen and will write about it in future Updates if the findings are significant.

Summary and Conclusion

- Bullish factors: vaccines, accommodative Fed and monetary policies, FOMO, TINA, better economic and earnings comparisons of 2020 to 2021, less supply of stock.

- Bearish factors: valuations, infections are surging in the U.S. and globally, rising debt around the world at most levels, certain sectors of the economy (retail, restaurants, airlines, entertainment will take more time to recovery) are struggling, there is too much speculation

- This year may be another good year, but performance has been pulled forward, so returns may be smaller after this year.

- The technicals/price analysis are better to analyze than the fundamentals because many stocks and indexes are overvalued.

- There are bargains available so stock picking and fundamentals should be used instead of indexing.

- The last economic cycle ended in February 2020. We will be starting a new economic and market cycle. Investors such as myself are investing for the next cycle. Most cycles last about 5 years. This last cycle lasted over 10 years. This cycle will probably last at least 5 and maybe up to 10 years.

My Economic Outlook should be out next month, February.