2021 April Market Outlook

Last year the market was able to look past the many bearish aspects of the pandemic and rally strongly after the market low. Also helping was the massive aid from lawmakers and the Fed. This year the market is now considering the bearish case and bullish case of the current market. As usual, I go over the bullish and bearish cases for the markets below.

Bullish Case

There are three main bullish variables: 1. progress towards beating covid 2. Economic growth/GDP is expected to be about 6% 3. Earnings growth is expected to increase by about 31% and as high as 70% during the year. Earnings estimates keep rising.

GDP was just announced and 1st quarter GDP growth was 6.4%, beating the consensus estimate.

- As I've been writing about for the past year – solving the health crisis is key to the economy. Fortunately, progress is being made in beating covid in the U.S.
  Below are the latest numbers regarding covid:

  #### The Latest Numbers

  225,640,460 vaccine doses given so far in the U.S.

  53,363 new U.S. cases recorded yesterday

  724 deaths in the U.S. recorded yesterday

  571,964 total U.S. deaths

  32,049,185 total confirmed cases in the U.S.

  146,615,147 confirmed cases world-wide, and 3,101,964 deaths

  Sources: Johns Hopkins University as of 11:30 a.m. ET; Vaccination figures from the Centers for Disease Control and Prevention.

  An optimistic view could be: If the remaining 157.6 million got fully vaccinated plus the 32 million would be 257 million, that would be about 77% (257 (67.5 million vaccinated plus one-shot persons got second shot 157 million plus 32 million who have been infected and probably have the antibodies to keep them safe divided by 330 approximate population of U.S.) – enough for herd immunity making it difficult for the virus to spread.

  Will all the 157.5 million get the 2nd shot? Probably not. But that could still leave us above 70%. Also, the U.S. is still vaccinating close to 2 million a day.

  The U.S. is making very good progress.

- Trillions of dollars in liquidity, relief, financial aid, and stimulus have been released into the U.S. economy. Similar liquidity has been provided by other global central banks to their economies. Our economy is doing better than most developed countries because of the fiscal and monetary aid, support, and now stimulus.

- The Fed has stated several times that they will do all they can to help the economy, especially those being left behind in terms of employment. The Fed has the economy and investors' back. They have committed to keeping interest rates ultra-low until 2023.

  This administration, the Fed, and Treasury have stated several times they are concerned about the service industry and its high unemployment. They want to keep interest rates as low as possible for as long as possible to boost the economy and help those being left behind in terms of the millions that are unemployed due to the pandemic.

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

- TINA – **T**here **I**s **N**o **A**lternative to stocks. Bond yields are low and there is capital loss risk if rates continue to rise. See the Bearish section below and the bullet points about interest rates and inflation.

- Financial Planners, 401ks are not selling. I've written many times about these two participants of the market and both control trillions of dollars and they normally don't sell but rebalance. This is a fairly new phenomenon that I've monitored for about the last five years.

- Another behavior of market participants has been that they consistently buy on pullbacks.

  Both phenomenons (key participants don't sell and participants buy on pullbacks) have kept the markets resilient compared to past market cycles. This is true despite the many headwinds (health and financial crisis, trade wars, conflicts with China, fears of rising inflation, and interest rates) the markets have faced.

  If these trends continue, we should feel relatively comfortable at the start of this economic and market cycle.

- Markets have been making new highs, this can continue. See the chart, explanation below in the Technical Analysis section.

- The anticipated growth in the U.S. and China might be enough to pull the global economy out of the global recession.

Bearish Case

- There are three main variables for the bearish case: 1. The pandemic is getting worse in certain parts of the world (Brazil, India, Sub-Sahara Africa) Europe is behind because of the vaccination roll out and problems with its main vaccine from AstraZeneca 2. Inflation and rising rates are major concerns among debt and equity investors, traders. 3. The markets are overvalued. See Valuation section below

More countries are losing the battle to covid than are winning. If this trend continues the global economy could continue to suffer. The real fear is that we have more mutations of the virus and some might be more contagious and deadly. Keeping these mutations out of the U.S. will be a challenge.

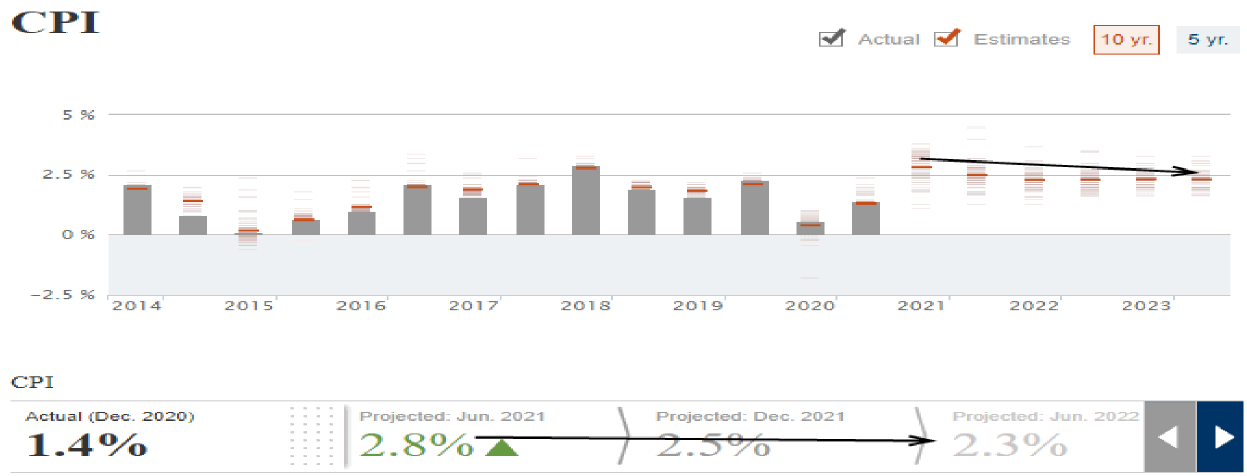
- The markets have not adjusted to the major changes in the economic direction and policies of the new administration. The previous administration was focused on the markets and economy. This administration is focused on Main Street and workers, and not Wall Street. They are also focused on climate change. The new administration has introduced bills to increase taxes on the rich and corporations to pay for their many programs. The markets so far have not adjusted to these changes.

- Some analysts and investors are concerned about rising inflation and interest rates. Investors have been worried about rising inflation and interest for over ten years and so far inflation and interest rates have remained at historically low levels.

  Recently, interest rates have had a substantial increase:

The 10-year Treasury has increased from around .5% to about 1.6% an increase of about 300%. But, rates are still at historically low levels as the chart above shows.

The 10-year is finally paying close to the rate of inflation but there is not a time premium. Below are forecasts for CPI from a WSJ survey of over 60 economists:



Source: WSJ

Currently, inflation is around 1.4% but is expected to double by this summer, then fall to the low 2% range by 2022. According to many economists and analysts, increasing inflation and interest rates are shorter-term trends.

There is inflation in equity and debt prices. See valuation section below.

- One of the dynamics that helped the markets in the last market cycle was the shrinking supply of stocks, but this may be changing with SPACs and IPOs. The market will not have the advantage of a declining supply of listed stocks.

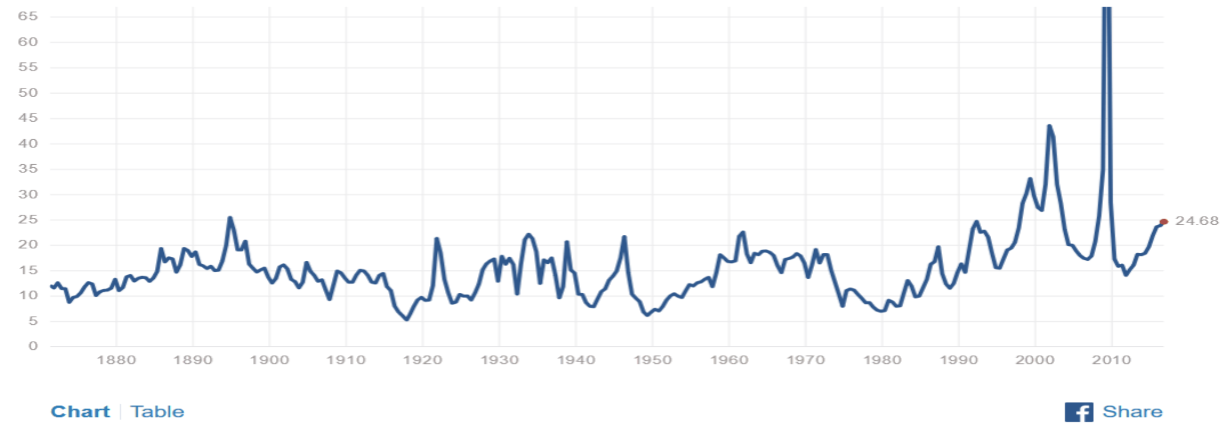
- Buybacks helped the last bull market cycle. There are normally fewer buybacks after a recession. We will probably see fewer buybacks at the start of this market cycle.

- “Sell in May and go away” is a strategy that investors may pursue. The market is anticipatory. The market tends to start gravitating toward the next years' price targets in November and most investors are positioned for the next year. By May the markets have normally come close to price targets and the markets tend to go sideways until November.

Valuations

Historically and in a perfect world (no inflation, manageable risk, earnings and GDP growth visibility), the P/E would be 20. The market will discount inflation and risks. The markets aren’t discounting inflation and covid and global economic risk. Below is a chart that shows the range of PEs going back to 1870.

Below is a chart that shows the historical average of P/Es.



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)

Source: WSJ

According to the above chart, the average historical P/E is about 15. Below are the recent prices and valuations for the markets. PEs normally spike during a recession when earnings (E of the P/E) collapse.

Source: WSJ

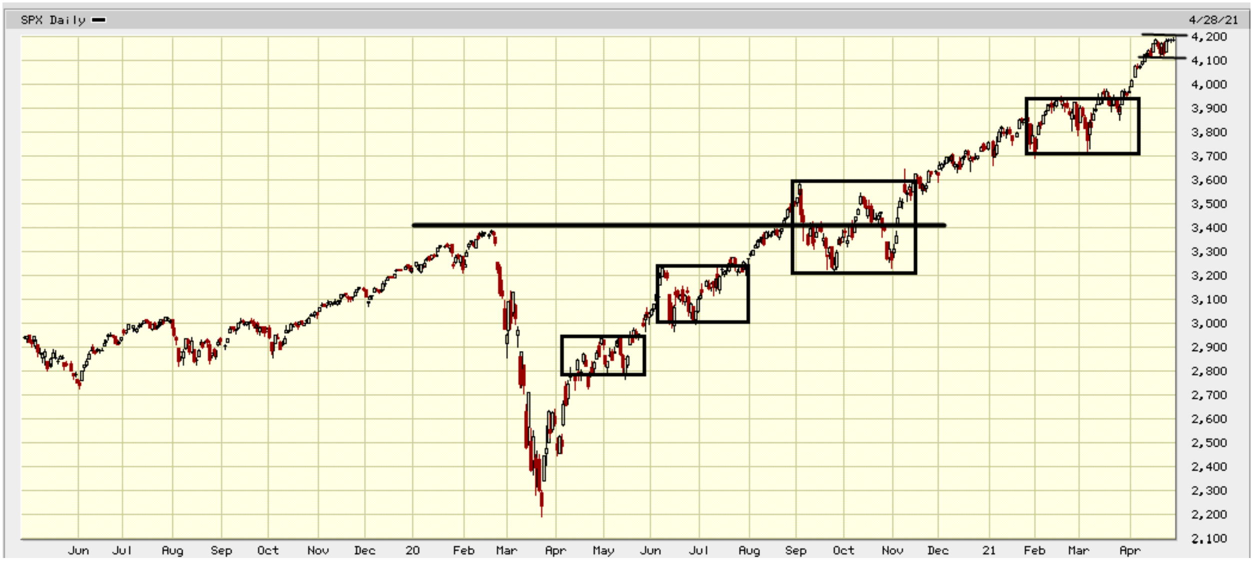
The historical average P/E is about 15, but current markets are above 20. The markets remain overvalued.

Because we're at the start of the cycle, companies/stocks can grow into their valuations.

When markets/stocks are overvalued, price analysis can be more helpful.

Technical/Price Analysis

Below is a chart going back to the market crash and the rally off the bottom.



Let's review the chart:

- The market cycle that started in 2009 ended in March of 2010, one of the longest bull markets in history

- The market fell about 35% from the February peak and entered into a bear market. The market bottomed very early in late March 2020.

- The market formed a v-shaped pattern. V-shaped bear markets are very unusual. The last time we had a v-shaped pattern, bear market was in 1998 caused by the global currency crisis. The strong rally was based on all the aid, support from Washington.

  It's also very rare that a market recovers that quickly amid a bad recession.

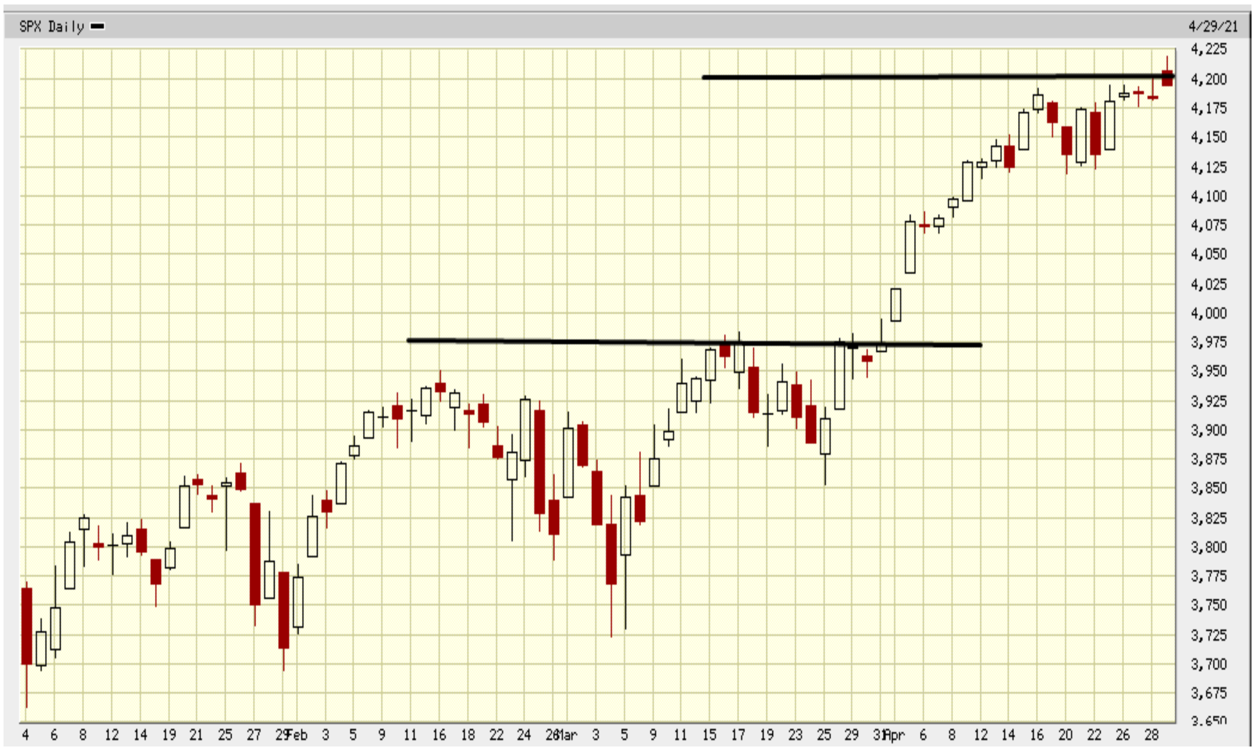
- Many sectors, stocks did not have v-shaped patterns. Many stocks, sectors had the normal basing pattern. See the KBWB chart below to see a normal bear market bottom.

- I've also written about how stocks make a move and then consolidates. The rectangles show four consolidations. When prices are in consolidation mode, it is a good time to write options against stocks in your portfolio that are consolidating.

- The market finally broke and stayed above the old high in November 2020.

- Currently, the market seems to be consolidating. It would not be surprising for prices to continue to make new highs as there is little resistance. In the next section below, I discuss new highs.

I’ve written about “new highs for the markets” many times. The market broke out to new highs last November. Below is a year-to-date chart for the S % P.



Let’s review the above chart:

- The market was able to make new highs for the first few months of the year

- It is normal for prices to stall at round numbers as the market did at the 3,900 to 4,000 levels.

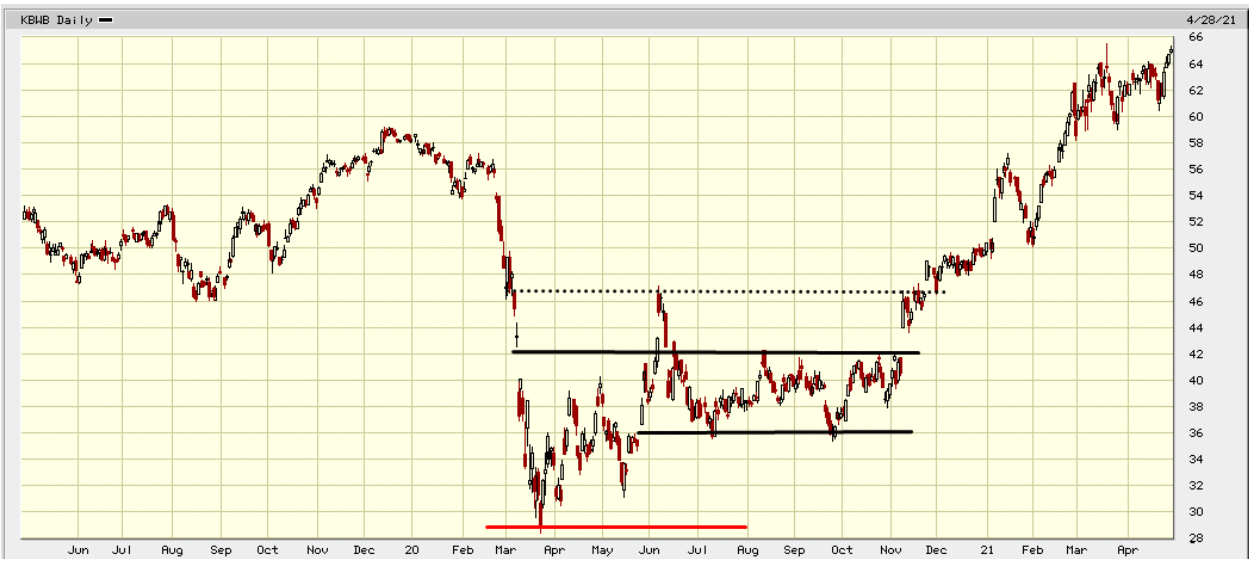
- Once prices broke out of the 4,000 area, prices made another bullish move

- Prices are consolidating again at the round number 4,200. The longer prices consolidate, the stronger the resistance. Because the resistance level is less than a month old, it could be easy to break to new highs. If prices break out then round numbers could be the next resistance levels. In this case, 4,300, 4,400…

- Once we find a new high, we will have a new higher consolidation pattern, trading range with a new higher resistance level. 4,000 should be support.

- Most consolidation periods last between one month to six months. If prices consolidate more than six months, the consolidation could turn into a major reversal topping pattern. We are too early in the cycle for topping patterns to develop.

Below is a chart of the banking index, KBWB, that shows the phases of a bear market, basing pattern. The best time to invest is when prices are basing in a bear market with a recession. If there is no recession, markets tend to recover faster.



Let's review this chart:

- Here are the basic phases of a normal bear market 1. The stocks, markets build a major reversal pattern top, once the topping pattern is broken, prices fall in a waterfall fashion. 2. A bottom is found 3. Prices normally consolidate after a bottom is made and the consolidation is called a basing pattern. 3. During the basing period prices, will normally test the bottom at least once. 4. Most basing periods last about 7 months, enough time to see improvements in the economy and businesses.

Many sectors including: financials, energy, retail, travel, restaurants, REITS went through the normal bear market phases. I was busy investing in these areas of the market for my clients and myself during the basing phase last year.

- Once the bottom was found, prices started to base with support between $36 to $31 and resistance between 42 to 46.
- Prices finally broke out in December when prices stayed above resistance of $46.

This year to add to returns, cash generation I've been trading stocks stuck in trading ranges. I use about 10% of a portfolio for trading. An example is AT & T, symbol T:

T has been stuck between about $28 to about $30 about a 5% return. If you sell a put to buy at $28 and a call at $30 the return could be about 9%. For the last 52 weeks, this has happened about 7 times. This could happen about three to four times a year going forward. Also. the stock pays about a 7% dividend and if you time the trades right you could capture a dividend or two increasing the return to over 10% potentially for each trade.

I've identified about nine stocks that trade like this. I'm trying to find more. I will write more about this in future Outlooks.

Psychology of the Market

Bulls are focused on: there is light at the end of the tunnel in terms of the health crisis; ultra-low interest rates; an accommodative Fed; lots of aid, support, and stimulus; expected strong GDP growth; expected strong earnings growth

The bears are focused on: rising inflation and interest rates; even though the U.S. is making real progress in beating covid, the rest of the world is struggling with surging infections, deaths, and mutations of the virus.

Summary and Conclusion

- We are making good progress in achieving herd immunity.

- Lawmakers and the Fed have provided plenty of aid, support, stimulus, and, liquidity to the economy, businesses, and workers and is helping us out of our health, financial crisis

- Analysts and investors are expecting strong economic and earnings growth.

- Because the markets have been overvalued for several years, technical/price analysis could be more helpful in making investment, trading decisions. As the market makes new highs, the next new resistance level is normally round numbers. For the S & P, it could be 4,300, 4,400…

- Rising inflation and interest rates could be a headwind for the markets and economy. I normally keep an eagle eye on inflation interest rates and will update readers on these important trends.

- We are at the start of a new market cycle. We are also probably at or near the start of an economic cycle. Investors should be invested at the start of an economic and market cycle. Most sectors in the market are now off their lows and breaking out of their basing patterns.

Next month I will provide my Quarterly Economic Outlook.