WASATCH CAPITAL MANAGEMENT OF RAYMOND JAMES®

SEPTEMBER 2020

\- - - - - -

INSIDE THIS NEWSLETTER

- SEPTEMBER COMMENTARY: ALCHEMY
- WASATCH TEAM UPDATE

Alchemy -Article by Mark Lazar

***Monetary policy does not work like a scalpel, but more like a sledgehammer.* Liaquat Ahamed**

After peaking in February, the stock market correctly anticipated some of the worst forthcoming economic data (in such a short period) in US history, including a record plunge in retail sales, employment, and growth. Consequently, the S&P 500 dropped nearly 35% top-to-bottom.

Item	YTD Change
Dow Jones Ind Avg	-1.42%
S&P 500 Index	6.07%
Foreign Index	-5.77%
Emerging Market Index	-.60%
2020 Federal Budget Deficit	$3.7 Trillion
US Q3 GDP Forecast	29.60%
Unemployment Rate	9.91%

**All data as of 9/4/2020*

But after bottoming March 23rd, something remarkable happened; the market again correctly forecast that while the impending economic data would be bad, it would be *less bad* than predicted—a lot less. Over the coming months, both the S&P and Nasdaq went on to hit record highs. This left a lot of market experts scratching their collective heads. Yes, we know the stock market is forward-looking, but let's be frank; things weren't (and still aren't) exactly rosy, with some sectors of the economy (i.e. airlines, hotels, cruise lines, theme parks, sporting events, concert venues, casinos, etc.) limping along, at best. Let's look at some of the factors that are driving the market, which may explain such a swift market rebound.

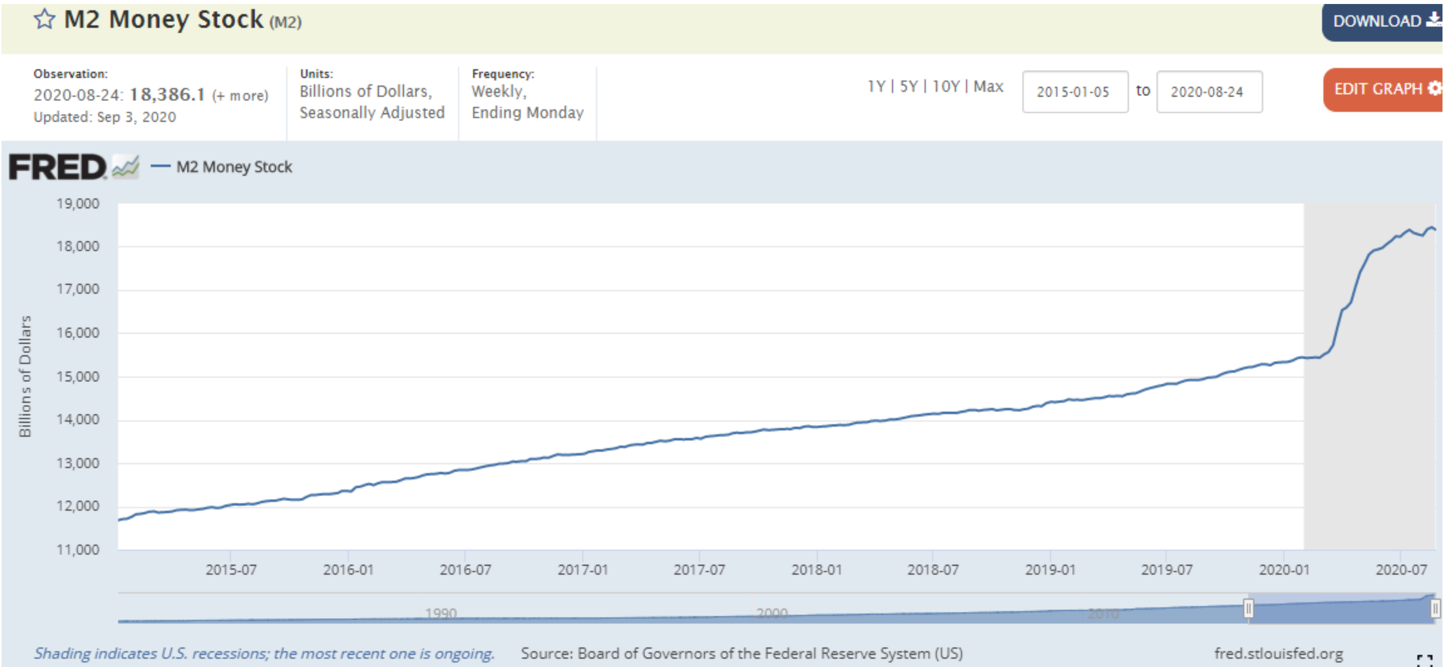
Markets are Forward-Looking
As previously mentioned, markets don't care what happened yesterday. Rather, they're attempting to divine what's going to happen tomorrow; specifically, 6–9 months in the future. Mr. Market clearly believes tomorrow is a better day.

Unprecedented Fiscal Stimulus
Uncle Sam has been throwing everything, *including* the kitchen sink, at the economy to prevent a temporary contraction in consumption and spending from becoming something much worse. With a (current) price tag of over $2 trillion, the CARES Act was unprecedented in size and scope. This included programs like the Paycheck Protection Program (PPP), stimulus checks ($2,400 per couple, $500 per eligible child), copious unemployment benefits, bailouts for affected industries, etc.

TINA: There Is No Alternative
As referenced in the May 2020 commentary, post-selloff, the stock market has been the prettiest ugly girl in the room. Compared to other asset classes (bonds, real estate, cash, alternatives, etc.), stocks appeared relatively attractive.

Monetary Stimulus
I believe the biggest driver of the stock market post-COVID has been monetary policy. There's a reason for the old saying, *don't fight the Fed*; when the Federal Reserve is accommodative (i.e. lowering interest rates, increasing the money supply, expanding credit, etc.), it's bullish for risk asset prices. In other words, loose monetary policy boosts stock prices, bond prices, real estate, gold, commodities, etc. In other words, there's an inverse relationship between interest rates and asset prices.

The chart below illustrates just how aggressively the Fed has been printing money:



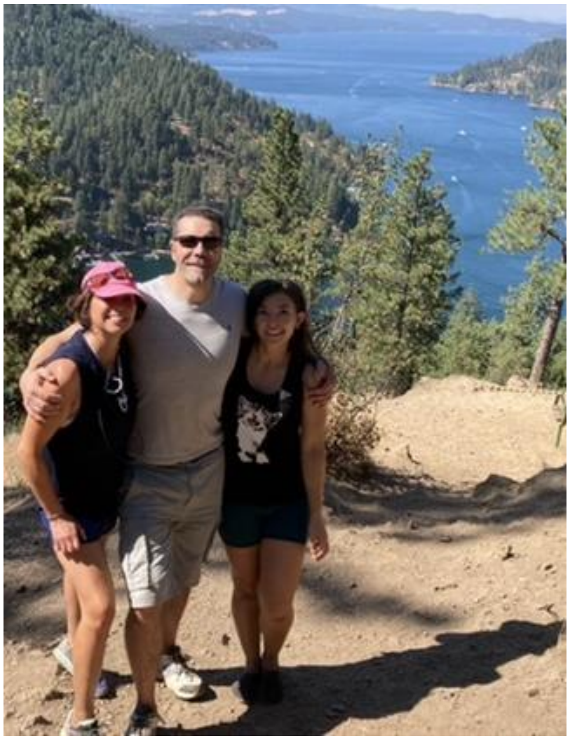
https://fred.stlouisfed.org/series/M2

The 10-year Treasury yield hit a record low of .32% earlier this year. Considering most pension plans have an assumed rate of return of 7%, it's evident that number can't be achieved by purchasing bonds. What's a pension plan to do in a record-low interest rate environment? TINA; move up the risk/reward spectrum and buy stocks and other risky assets that can at least potentially hit their target return.

Furthermore, with the 10-year breakeven (expected) inflation rate of 1.70%, Treasury yields currently have a *negative* real return. In other words, with a current yield of about .70%, the ten-year note provides investors with a negative return of 1% annually for the next decade. Conversely, stocks have historically been a good hedge against inflation.

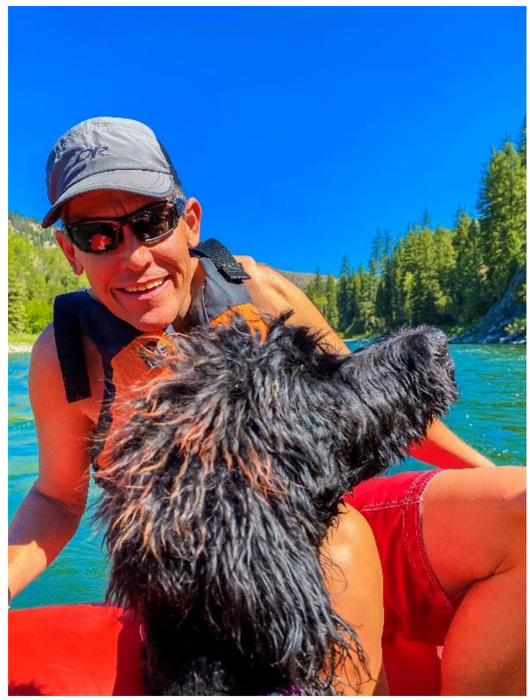
It could be argued that central bankers have become contemporary alchemists, turning lead into gold, effectively sprinkling monetary stimulus fairy dust on risk assets and, voila! Everything is worth more. I believe this to be at least partially true, however, I learned long ago that that when investors fight the Fed, they're almost always regretful.

Wasatch Team Vacation Updates



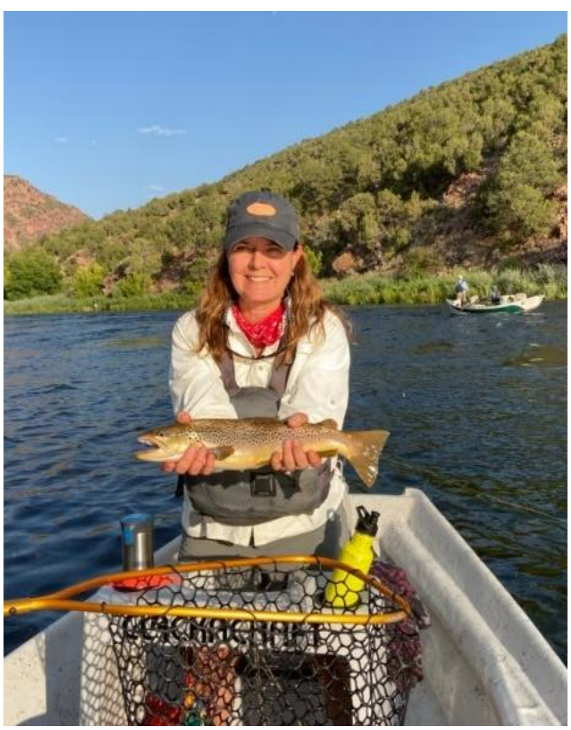
Mark

Mark & Savina hiking Tubbs Hill off Lake Coeur d'Alene



John

John rafting the Snake River outside Jackson, WY over Labor Day



Beth

Beth fishing the Green River last month

Mark Lazar, CFP®, MBA, Vice President- Investments | 385-275-3609

John Bergerson, CFA®, MBA, Investment Portfolio Associate | 385-275-3608

Beth Winter, Client Service Associate | 385-275-3593

2750 E Cottonwood Parkway, Suite 520, Cottonwood Heights, UT 84121

1389 Center Drive, Suite 200, Park City, UT 84098