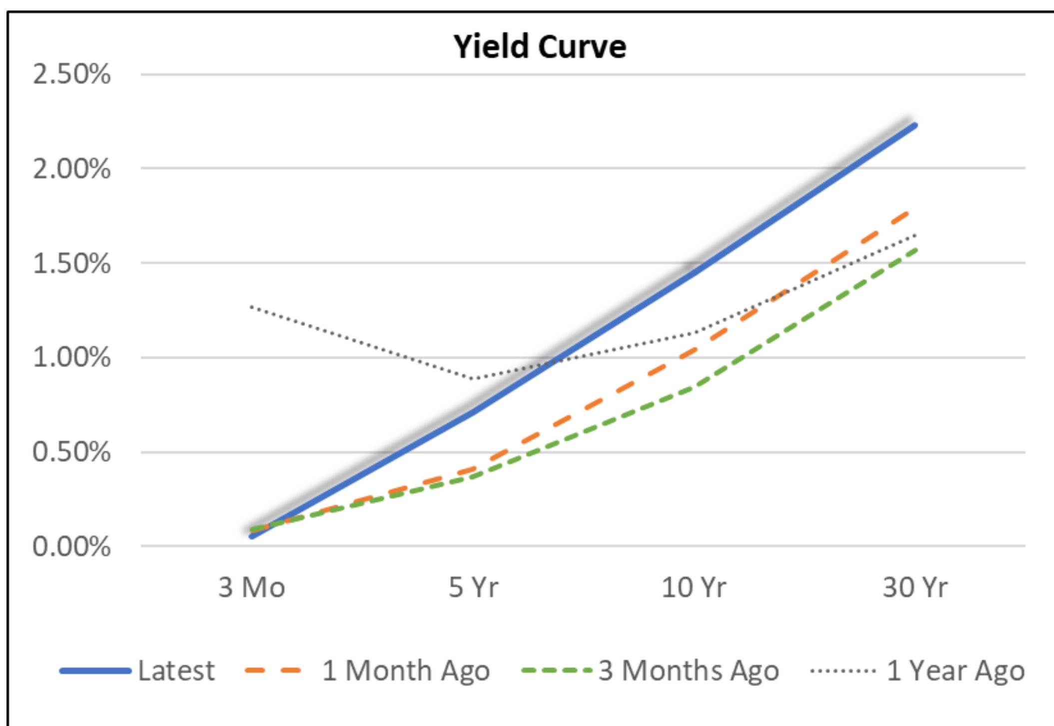
Sixty Guilders
VALUE RESEARCH

March 2, 2021

Marker Dashboard – Will This Time Be Different?

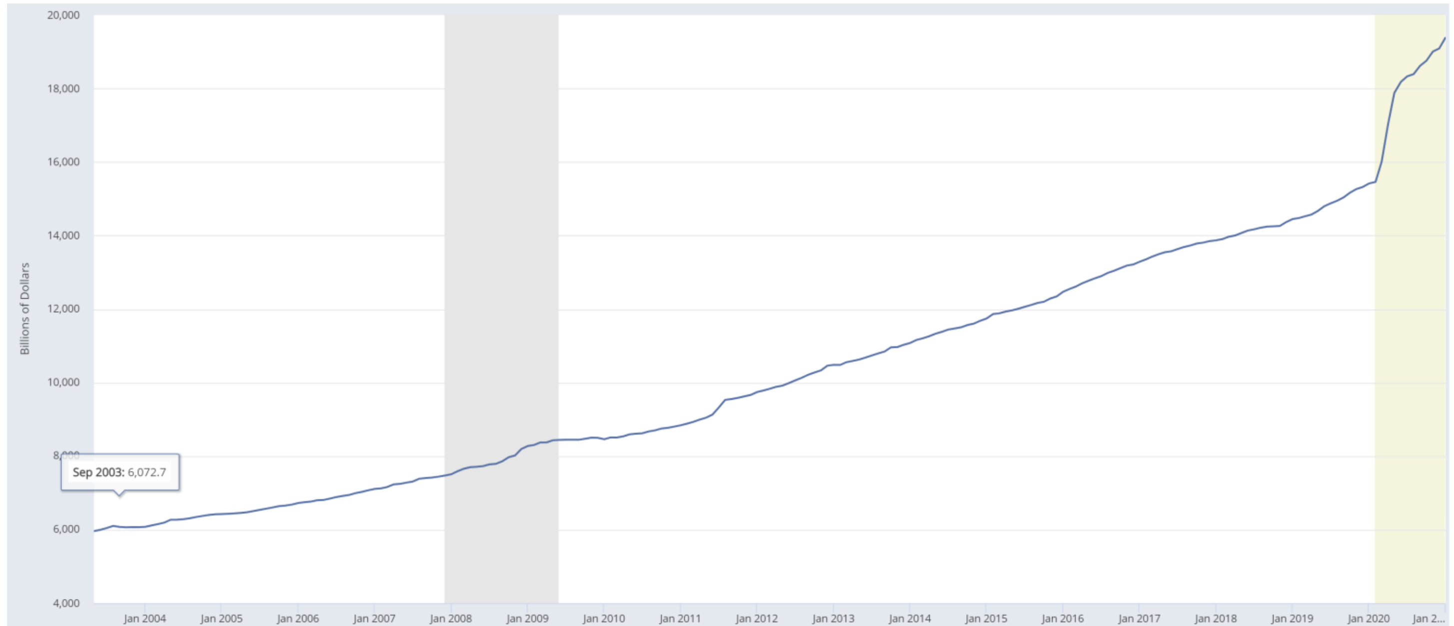
As the US Congress is in the process of passing additional fiscal stimulus to counter the negative effect of the pandemic and related US state lockdowns, the US equity market is experiencing jitters primarily as a result of the action in the bond market. As can be seen in the attached chart, the US government bond yield curve has begun to steepen, with the 10 year Treasury note now touching 1.50%, up from 0.85% just three months ago. While a steepening yield curve can be a sign of a healthy economic outlook, the rapid pace of the repricing of time value of money implies more than just a healthy outlook. It potentially implies that the "bond vigilantes" (to use an almost forgotten term to describe the wisdom of the market to keep fiscal and monetary policy honest) are raising a caution flag to all the money sloshing around since last spring, with no end appearing in sight.



Source: YCharts, Inc.; Sixty Guilders Management, LLC

The bond market appears to be beginning to pay attention to the massive increase in money in circulation as a result of deficit spending, as well as the Fed's continued asset purchase program. As can be seen by the accompanying chart, the money supply (as measured by M2), has increased by about $4 trillion since last March. By comparison, we note that even following the 2008 financial crisis, M2 increase only about $1 trillion.

M2 Money Supply



Source: https://fred.stlouisfed.org/series/M2SL

This increase in money supply has been a result of a near dollar-for-dollar increase in the Fed's balance sheet, which has swelled from around $4 trillion to around $7.5 trillion. Note again the magnitude, compared to the financial crisis, where the Fed's assets only increased about $1 billion in 2009. Its new asset purchases have put new $s into the US economy, pushing down yields, and forcing investors out the risk curve to seek yields previously available in less risky securities (something we've touched on in prior Dashboard updates).

Federal Reserve Assets

Source: https://fred.stlouisfed.org/series/WALCL#0

One would think that the warning signals coming out of the bond market would serve as a gut check for the Federal Reserve and its continued helicopter money policy, but it appears that at least the Chairman of the Fed, Jerome Powell, feels there's nothing to see here. This time, the explosion in money, in his view appears to be that it's not an issue. Herein is an excerpt of an exchange with Senator Kennedy on February 23, 2021 during Chairman Powell's Congressional testimony:

Senator Kennedy: (01:18:14)

Let me stop you, Mr. Chairman, because I'm going to have one last question quickly. M2, the money supply is up. I think about $4 trillion over the past year, or $6 trillion. $4 trillion, $6 trillion, what's a few trillion? It's up 26%, the highest amounts since 1943. What does that tell you?

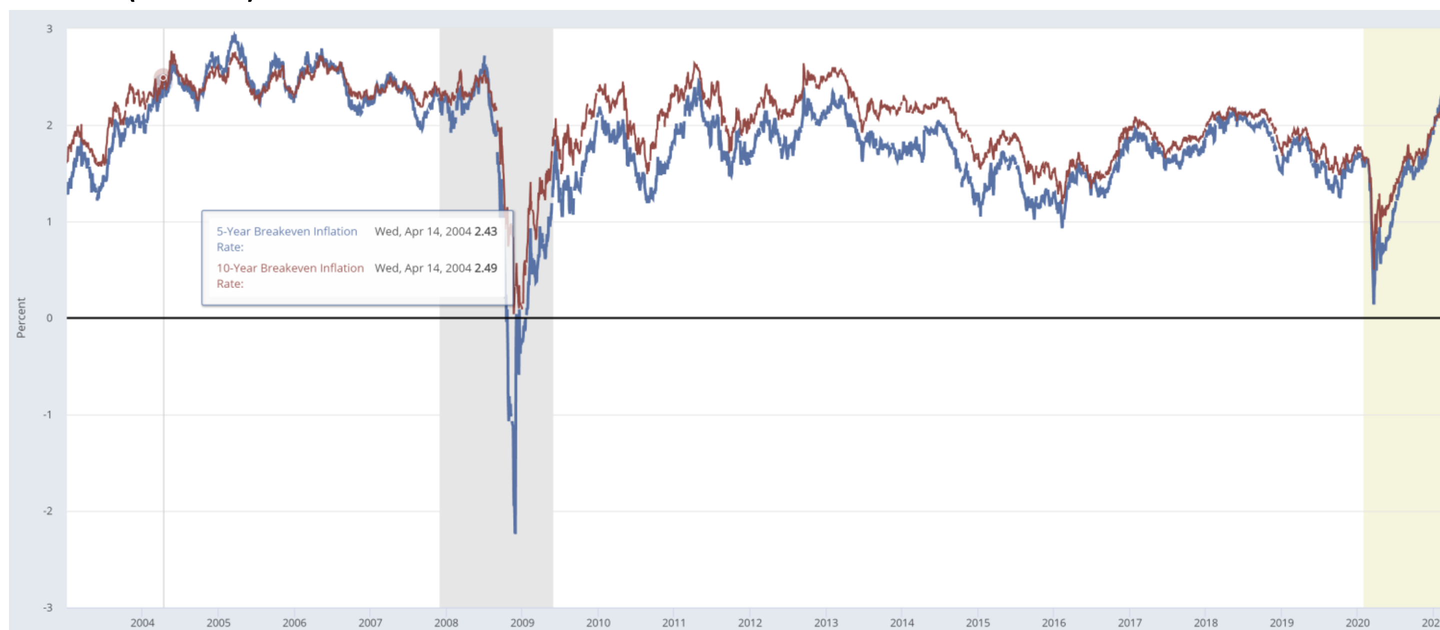
Jerome Powell: (01:18:35)

Well, when you and I studied economics a million years ago, that M2 and monetary aggregates generally seem to have a relationship to economic growth. Right now, I would say the growth of M2, which is quite substantial, doesn't really have important implications for the economic outlook. M2 was removed some years ago from the standard list of leading indicators, and just that classic relationship between monetary aggregates and economic growth in the size of the economy, it just no longer holds. We've had big growth of monetary aggregates at various times without inflation, so something we have to unlearn, I guess.

We would love to have Chairman's Powell confidence in dismissing the problem with M2's growth, but with commodity prices also rising (crude is up from less than $43/barrel three months ago to almost $62 for example) forward expectations for inflation have also spiked dramatically, and now are pricing 2.5% inflation five to 10 years in the future, up from 0.5% a year ago.

We are stumped to accept that this time things will be different. If the long end of the yield of the curve continues to "misbehave", the consequences for the markets will not be pretty, and the Fed's easy money will prove to no longer be the solution, but the problem.

Five Year (Blue Line) and 10 Year Breakeven Inflation Rates



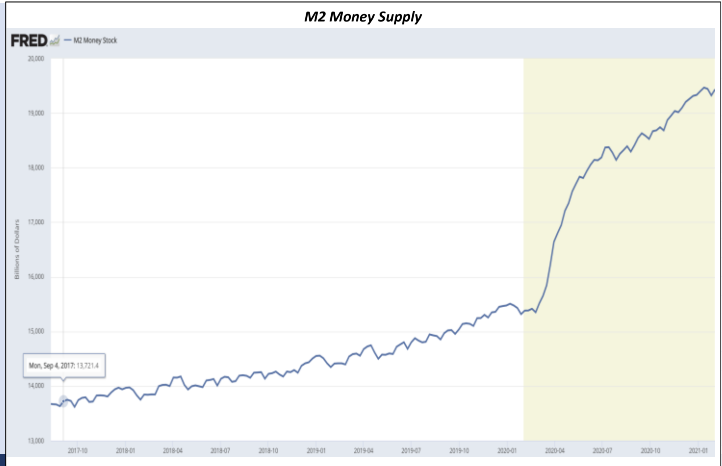
Source: https://fred.stlouisfed.org/series/T5YIE#0

Sixty Guilders Monthly Market Dashboard

3/1/2021
Dimitri Triantafyllides, CFA

Total Return By Asset Class	1 Month	3 Months	1 Year
Oil	16.8%	43.7%	20.1%
S&P 500	***2.3%***	***8.4%***	***32.8%***
60/40 Stock/Bonds	0.7%	4.5%	21.4%
High Yield	0.4%	2.8%	8.7%
Dollar Index	0.1%	-1.2%	-5.5%
International (MSCI) Index	-0.1%	4.3%	19.8%
Barclays Agg. Bond Index	-1.9%	-1.3%	4.3%
Gold	-5.9%	-7.8%	6.1%

Sector Performance (Total Return)	1 Month	3 Months	1 Year
Energy	21.2%	34.7%	10.7%
Financials	12.2%	19.8%	23.0%
Communication Services	7.1%	14.7%	46.7%
Industrials	6.7%	8.6%	29.3%
Materials	4.9%	8.3%	41.8%
S&P 500 Total Return	***2.3%***	***8.4%***	***32.8%***
Real Estate	2.0%	5.3%	-1.2%
Information Technology	1.3%	11.7%	53.1%
Consumer Discretionary	0.2%	12.5%	62.8%
Health Care	-1.8%	6.3%	27.9%
Consumer Staples	-2.3%	-1.9%	10.9%
Utilities	-4.9%	-5.5%	-6.8%



		Latest		1 Month Ago		3 Months Ago		1 Year Ago
Economy								
Economic Growth (Real GDP)	↓	4.1%	↓	4.0%	↑	33.1%	↓	2.1%
Inflation (Ex. Food & Energy)	↓	1.4%	↓	1.6%	↓	1.6%	↑	2.3%
Nominal GDP	↓	5.5%	↓	5.6%	↑	34.7%	↓	4.4%
Unemployment Rate	↑	6.3%	↑	6.7%	↑	6.9%	↓	3.6%
Money & Commodities								
Gold ($/Troy ounce)	→	1,743	↑	1,853	↑	1,891	↓	1,643
Oil (WTI Crude, $/barre)	↑	61.67	→	52.78	↓	42.91	→	51.36
TIPS (breakeven rate)	↑	2.2%	↓	0.0%	↓	0.0%	↓	0.0%
Rates								
3 Month T-Bill	↓	0.05%	↓	0.08%	↓	0.09%	↑	1.27%
5 Yr US Treas.	→	0.71%	↓	0.41%	↓	0.37%	↑	0.89%
10 Yr US Treas.	↑	1.45%	↓	1.04%	↓	0.84%	→	1.13%
30 Yr US Treas.	↑	2.23%	↑	1.79%	↑	1.57%	↑	1.65%
Credit Markets								
3 Month LIBOR		LID INDICATOR	↓	0.2%	↓	0.2%	↓	1.6%
Inv. Grade (Single A rated) Index	→	1.9%	↓	1.6%	↓	1.6%	↑	2.3%
HY (Single B) Index	↓	4.6%	↓	4.7%	→	5.1%	↑	5.9%
Equity Market								
S&P 500	↑	3,902	↑	3,819	↑	3,615	↓	2,991
Price/Book	↑	4.0x	↑	4.1x	↓	3.6x	↓	3.6x
P/E	↑	26.0x	↑	25.5x	↑	25.4x	↓	21.8x
Earnings Yield (E/P)	↓	3.8%	↓	3.9%	↑	3.9%	↑	4.6%
Volatility (VIX)	↓	27%	↑	31%	↓	25%	↑	29%
International Snapshot								
MSCI	↑	2,169	↑	2,170	↑	2,080	↓	1,810
Dollar/Yen	↑	106.6	↑	103.8	↑	103.8	↑	111.7
EUR/Dollar	↓	1.21	↓	1.21	↓	1.19	↓	1.10
10 Japanese Bond Yield	↑	0.17%	↓	0.000%	↓	0.00%	↓	0.00%

Longer Term Trends

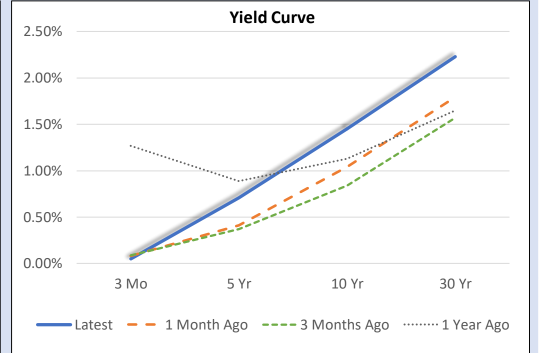
* The US economy is expanded 33% in Q3, bouncing back from Corona virus lock-down impacting of Q1 and Q2.

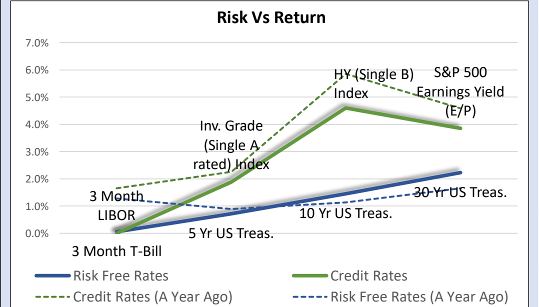
* Gold has pulled in the last 3 months, but is still the best performing asset in the last 12 months.

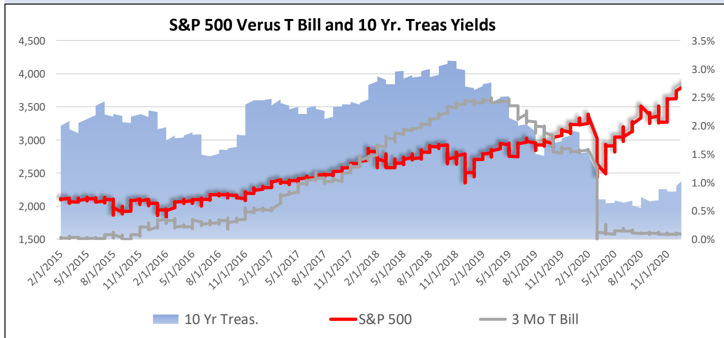
* The yield curve has steepened in the last three months as the Fed has become more "inflation welcoming" (TIPs are now at a 1.8% breakeven rate).

* Similarly, corporate spreads have tighened, with the high yield index trading at a 5.1% yield, down from almost 12% in late March.

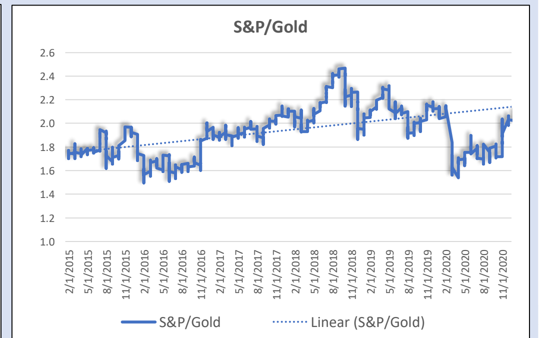
* The VIX (volatility index) at 24%, is down from 76% a its peak in late March.







* The equity market has performed an about face from its lows in late March, exiting its bear market, about as quickly as it got there.
* The flight from cash, has also fueled hard assets and cash alternatives such as gold. As a matter of fact, the S&P, in gold terms, has barely moved in four years.



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