1st Quarter 2021 Market Overview
The Focus Turns to Inflation

The stock market shrugged off the specter of rising interest rates and posted gains for the first quarter. Investors are mainly encouraged by growing prospects for an economic boom.

During the quarter, the government finally paid out $1.9 trillion in stimulus checks. Another $2t is currently being promised via an infrastructure spending bill and a further $1.5t is being unveiled in the form of an education and healthcare bill. In the meantime, our Federal Reserve continues to buy $120 billion in Treasury bonds each month which serves to keep a steady flow of liquidity sloshing in our banking system.

The economy is responding to this stimulus. Local roads are getting crowded. Restaurants are open. Fans are back for baseball. Disneyland reopened. Trade shows in Vegas are unfolding. We can even look forward to seeing our beloved artists at concerts.

Predictions for GDP growth exceed 6% for 2021and this may be conservative. This expansion promises to be far greater than anything we have experienced in nearly 40 years.

The consequence of this flood of printed money is inflation. Inflation is a dreaded enemy of bonds and stocks. It is a death nell for bonds and it also erodes return-on-investment, which makes equities less attractive. Consequently, we are a juncture where *inflation is the chief worry for the markets*.

Have you seen prices, lately? A trip to the store reveals startling increases for items in our cart. So far, Federal Reserve Chair Jay Powell calls these price increases “transitory”. Powell’s reassurance insinuates current price increases are not systemic and are more the result of temporary supply strains.

For now, this seems to have assuaged the markets, but skeptics are not so sure it will last.

Doubters feel Powell is underestimating the strength of the economy and will be forced to tighten credit and remove the “punch bowl” that has fueled the market. Absent a dovish Fed, the market is sure to protest and react to the downside.

Already this year, the rate on the 10 year US Treasury bond rose from 0.92% at the outset of 2021 to 1.75%, recently and this led to a 12.5% loss in for the first quarter, one of the worst quarterly performance for bonds in history.

If bonds *are* on the precipice of a bear market, what does that mean for stocks? Our last bout with rising interest rates in 2018 led to a 20% drop. If the stage is set for a market correction, inflation will be to be center stage.

The End of the Speculation Craze

The gamification of the stock market seems to have culminated with the Gamestop stock mania in January. Since then, this reckless speculation has largely been quelled.

Not only did Gamestop stock tumble sharply from its peak but speculative investment behavior has been withering. Many of the SPAC stocks have declined 50% or more. Recent notable IPOs have retreated markedly. Even Tesla saw its shares down 28% ytd during the quarter.

Individual investment activity, led by Robinhood brokerage accounts, has fallen over 60% over the past two months. Lately, daily individual investor activity is drying up according to surveys. (WSJ 4/5/2021)

CNBC TV personality, Jim Cramer recently claimed that investment professionals have "taken back the market at the expense of retail day traders." "Money managers … don't want to pay 100 times sales. They would prefer to pay 10 times earnings," he said in his usual colorful fashion.(CNBC 3-26-2021) Mainly he is referring to the end of the gamification of the stock market that we have seen since last fall.

Peregrine Holdings and Strategy

The first quarter was a saga of what noted market technician, Helene Meisler, refers to as an "either-or market." She points out the market either favors large technology stocks (FAANG), or everything else. But, not at the same time. Thus, an either-or market. For example, Microsoft gains at the expense of United Airlines or vice versa, but not both.

Peregrine currently holds investments in both categories. Our intent is to manage accordingly, so that clients gain from holdings in both baskets.

Core holdings for clients in defensive food and household products stocks performed poorly in the quarter until March. While these companies are predictable and relatively impregnable, they are regarded as stodgy businesses with limited growth prospects. This group of stocks has been a drag on client accounts. Finally, in March, there was a modest recovery. Hopefully, this group will gain a perch of eminence in the economic environment since they clearly gain from increasing prices.

Broadly, the market faces sizeable headwinds from inflation threats. We currently look for a retreat in the market that will offer an opportunity to invest in leading stocks at cheaper prices.

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