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SLIMMON'S TAKE > TAKEAWAYS & KEY EXPECTATIONS

Andrew Slimmon December 2020 Equity Market Commentary

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1) After the best November for the S&P 500 since 1950,[1] isn't the market due for a correction? After all, we have seen record inflows,[2] and sentiment seems downright giddy.[3] Seemingly with everyone in the boat, isn't the boat in danger of taking on some water?
   We doubt it.

   A. Market breadth[4] is expanding, suggesting a very healthy environment.
   B. We are in the midst of the Biden "honeymoon period."[5]
   C. Seasonality.[6]

   For these reasons, we expect to see continued strength into early next year.[7]

2) Value cyclicals have performed extraordinarily well lately.[8] Is it time for investors to take profits?
   We doubt it.

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[1] Bloomberg.
[2] Equity ETF inflows posted a monthly record $81 billion. Strategas. December 1, 2020.
[3] Citibank Panic/Euphoria model is at August highs. Helen Meisler. November 28, 2020.
[4] 93% of stocks in the S&P 500 are above their 200 day moving average. Bloomberg.
[5] The period post-election of new Presidents until January 1st has a high positive hit ratio for S&P 500. Strategas. November 2020.
[6] December has been a favorable month for a "Santa Clause rally". Thomas Lee/CNBC. November 12, 2020.
[7] The "honeymoon period" tends to run out in early January. Strategas. November 2020.
[8] Deep value factor outperformed all other factors in the month of November 2020. Factset.

The index performance is provided for illustrative purposes only and is not meant to depict the performance of a specific investment. **Past performance is no guarantee of future results.** See Disclosure section for index definitions.

A. Investors remain heavily overweight in technology stocks.[9] Therefore we suspect that any pullbacks in cyclicals will be quickly bought in the quest to position for 2021.

B. Historically, when value outperforms in November, it is highly likely that pattern will continue in December.[10]

C. Admittedly an anecdotal reason, but when I have mentioned buying the cruise lines (a greatly depressed value area) in any media situation, it has been largely greeted by guffaws….until about a week ago.

3) Does this mean there is a great rotation away from growth and technology stocks?
We doubt it.

A. We believe this is simply a broadening of participation. While the largest mega-cap tech stocks grew to comprise a dangerously high percentage of the S&P 500 by this past summer, that number is already starting to recede.[11]

4) With European financials leading the charge, up nearly 30% for November,[12] are we finally seeing a leadership rotation from the US to Europe?
We doubt it.

A. Global investors are underweight in Europe,[13] particularly in European value stocks, which could lead to some continued performance.

B. However, interest rates in Europe are negative and getting worse,[14] which we do not believe suggests accelerating economic growth.

C. Plus, the European earnings recovery continues to lag the US and Emerging Markets.[15]

Ultimately, fundamentals need to validate the rise in stock prices, or else stocks will fade, as we have seen happen so often in the past.

5) Chinese internet stocks have been hit with a series of issues recently. Is this the end for China tech?
We doubt it.

A. The key driver of Asian performance, in our opinion, is not politics, but the direction of the dollar versus Asian currencies.[16] As long as the dollar is depreciating, in our opinion, flows will continue to be attracted to these reasonably priced Chinese internet giants.

6) Finally, over the summer, the two primary arguments we heard against owning equities were: 1. the risk of a fall re-outbreak of COVID-19, and 2. a contested Presidential election in November.
We doubted both.

A. These were "known" risks that the media discussed daily.

B. Downside corrections tend to occur when "unknown" risks emerge, rather than "known" risks.

C. We think it's best to focus on the "unknown" risks that are not in plain sight.

[9] Technology positioning amongst institutional hedge funds remains in the 90th percentile of exposure since 2010. Nick Savone/ Global Reflections. November 27, 2020.

[10] In the last 27 years, Factset value factor has outperformed the Russell 1000 in November 13 times. Of those 13 times, value outperformed the S&P 500 in December 10 times for a 77% hit ratio. Hannah Garriga, MSIM Applied Equity Advisors, November 17, 2020.

[11] By the end of August, Apple, Microsoft, Amazon, Facebook and Google comprised nearly 25% of the S&P 500. That is down to 21% as of November 30, 2020. Bloomberg.

[12] MSCI Europe Financials rallied 28.75% in November 2020 in USD.

[13] The Flow Show. November 25th, 2020.

[14] The German ten year bond yielded 0.42% at the end of August and as of December 1st, sits at -0.53%.

[15] MS Q3 Scorecard. November 19, 2020.

[16] From March 27, 2018 until October 18, 2018, the MSCI AC Asia ex Japan currency index dropped -6%. MSCI AC Asia ex Japan equity index dropped -17% during that time. Since the MSCI AC Asia ex Japan currency index bottomed this year in March, the index is up 8%. The MSCI AC Asia index is up 52%. Bloomberg.

Slimmon's TAKE - 2021 Outlook, to be distributed later this month, will discuss risks which are rarely mentioned.

Here's one: Geopolitical event risk.

When was the last time you heard anyone mention geopolitical issues as a risk to the market?

Will the market sail through 2021 without some unforeseen geopolitical event?

We doubt it.

Andrew

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