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JANUARY 2021 REVIEW & COMMENTARY

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2021 Equity Market Focus

The January Short Squeeze and 2021 Market Outlook

After starting strong and rising 2.5% in three weeks, the S&P 500® index ended January with a thud due to one of the most unusual events in modern equity market history and ended the month down. The unusual event, of course, was the war between short-sellers and short-squeezers that developed at the end of the month and resulted in extreme volatility for a handful of stocks, the poster child of which is Gamestop.

Gamestop (GME) is a retailer of gaming software and equipment. It began January with a stock price of $18.84, 69 million shares outstanding and market cap of $1.3 billion. Like many retailers, business has been hurt by the Covid pandemic. Through October 31st, sales fell 30% from 2019's level and analysts' expect losses for 2020. Short-interest (betting that the stock will fall in price) was an astounding 61 million shares – or 88% of total shares. On January 11, an online community called wallstreetbets on a social media site called Reddit began saying there was profit to be made in buying Gamestop shares and forcing those short the stock to buy to cover positions. The rest is history. At its peak on January 28th, Gamestop sold for $483 per share and had a market cap of $33 billion. By February 2nd, it fell to $95 per share giving it a market cap of $6.5 billion. Similar moves occurred in several other stocks, including theatre chain AMC Entertainment (AMC), and retailers Bed, Bath & Beyond (BBBY) and Express Inc. (EXPR).

As a result, probably, of this market mayhem, the S&P 500® index lost 3.7% in the last week of January leading to the 1.01% drop for the month. That leads us to the question of the day – where do we go from here?

Historically, "down" Januarys change the outlook for the full year substantially. Historically, markets rise about 70% of the time. According to the Stock Market Almanac, a useful and interesting guide of market statistics published since 1967, when the market is down in January, the chances of the full year being up are basically 50-50. Their data shows that since 1950 the market was down in January 28 times (through 2020). It then went on to post gains for the full year 14 times and losses for the full year 14 times. Scarier still is the fact that the S&P 500® index continued to fall after every down January, in some cases a little, in some cases (2008; -45.4%) a lot. So even though we are in six months of the year historically most favorable to equities (Nov. – April), it behooves us all to think a little more conservatively now.

The year could, of course, turn out like 2020. After a Covid-induced plunge in February and March, thoughts of vaccines and economic stimulus packages resulted in a 70% percent rise in the S&P 500® index between its March low and year-end. It is likely the Biden Administration and Congress will pass another economic stimulus measure, maybe giving $1,400 per person to those who qualify. Federal Reserve bankers are also intent on keeping interest rates low, probably into 2022. With liquidity plentiful and rates low, equities could still be the investment of choice for the year.

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There are other positive and negative things to consider now as well:

Fourth quarter earnings have been stronger than expected, but 2021 guidance is still conservative for many companies.

There are several Covid vaccines now and more people are getting vaccinated daily, suggesting some normalization of the economy this year.

At 23.1x times estimated 2021 earnings, markets are expensive compared to historical averages, but remain attractive due to low interest rates on bonds and cash.

Lastly, a lot can happen between now and December 31st. We've seen two strong days in February and markets are now up again for the year (S&P 500 +1.87%).

Stay tuned.