

CORE Comments

ON PLANNING AND INVESTING FOR THE TWENTY-FIRST CENTURY

January 4, 2021

Into the New Year

Optimism about vaccines and about abatement of the death and destruction from the Coronavirus continue to buoy stock markets. More significant, I submit, is the ongoing monetary support provided by the Federal Reserve. Having speedily increased the Fed's holdings from \$4 trillion before the onset of Covid to \$7 trillion, Jerome Powell, the Fed chair, has assured us that the Fed will continue its very easy policies for a long time to come. The money supply has risen far faster than what is needed to operate the economy and the excess liquidity has found its way into various assets, notably stocks and housing. Mr. Powell has told us that the interest rates it controls directly will be held close to 0% for the next three years, even if the unemployment rate falls below 4% and inflation rises above 2% and stays above that level.

As we have remarked in previous letters, the Fed's monetary support and its vast injections of money into the system have been more important to financial markets than the weakness or strength of the economy and, indeed, more important than the health or illness of Americans.

The bond market tells a different story from that of the stock market. Whereas stocks trade at valuations that far exceed historical norms and that are associated with periods of strong economic growth, the bond market tells us that the economy is weak now and will remain weak into the future. The ten-year Treasury bond yields 0.92%, up only modestly from its lowest levels in August. The different stories told by stocks and by bonds are quite reconcilable: the economy is relatively weak, as the bond market tells us. Because of the weakness, the Fed has undertaken--and promises to continue--extraordinary measures to counteract the economic weakness. The Fed's actions cause stock prices to rise to levels inconsistent with underlying economic weakness. Ostensibly the Fed's policies are to support economic activity, but one may be forgiven for thinking that the effect on asset prices--and the stock market, especially--is something the Fed considers. The Fed's promise to continue its policies for the years ahead gives equity investors confidence.

The combination of vaccine hope and easy monetary conditions far overcomes uncertainties in American politics and the desperately awful news of infection and death. For example, since the election, it has been uncertain which party will control the Senate, a matter to be decided on Tuesday's run-off elections in Georgia. This is consequential: should the Republicans retain the Senate majority, the likelihood of further federal disaster relief is quite low, whereas if the Democrats take the two Georgian Senate seats, the Biden administration will have a smoother pathway to accomplish its aims. This political uncertainty has not troubled the stock market. The vaccination roll out has been rather befuddled, to say the least. This suggests that the task of vaccinating all Americans who want the vaccine may not be accomplished anytime soon. Moreover, the more transmissible variant of the Coronavirus, identified recently in the UK, spreads round the world, presumably making things for us more risky than we had thought. Have these problems troubled the stock market? Nope. The

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Fed's promises and vaccine hope have been sufficient to keep stocks pushing higher. Core's investments are working well now and may be expected to perform well in the months ahead.

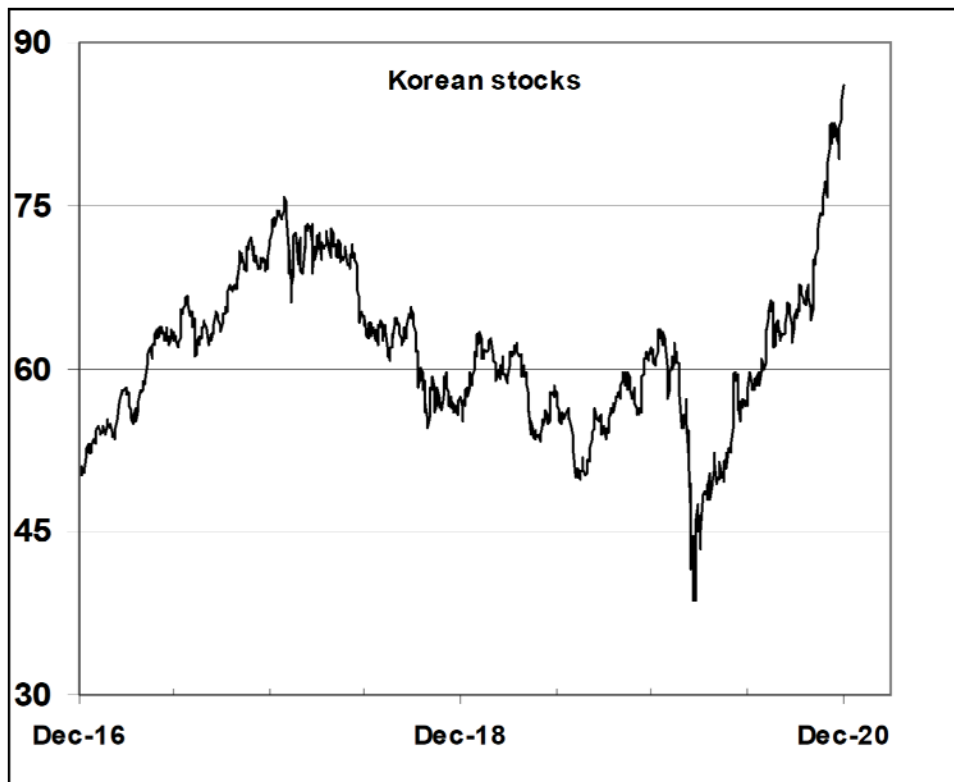
We began 2020 with large investments in bonds (mostly long-term US Treasuries), gold and cash, but with no stocks. That served us very well when the Coronavirus introduced itself and the stock market, as measured by the S&P 500 index fell by 35% in February and March. Came the Fed cavalry and the huge federal disaster relief program (the CARES act) and stocks found their footing. In the second half of the year, Core made a series of stock investments, mostly in East Asian countries. Those countries--Taiwan, Korea, Japan and others--handled the virus far better than did America and Europe and our positions there have gained ground. By avoiding stocks for much of the year while holding large investments in US Treasury bonds (securities without default risk), the risk

in Core's portfolios was quite low. But while incurring very little investment risk, Core's accounts overall returned 19% after fees. (There is variation among individual accounts for various reasons.)

What the new year holds for us investors is, of course, unknown and unknowable. The Fed has made its promise, but will it keep it? What will be the course of the Coronavirus this year? Will effective vaccines be available around the world and successfully administered? What new unknown lies ahead? (Remember that, at the beginning of 2020, the existence of the new Coronavirus was essentially unknown outside of China.) What damage might be wrought by fires and storms this year as the effects of climate

change worsen? What might the Russians be up to with their extensive hacking of American information systems? Against these risks is our experience with chance and mischance: America's and the world's economic engines keep turning over and the many trillions of dollars in financial markets make progress. Good investment returns remain a reasonable expectation. We aim to be alert with the capital you have entrusted to Core's supervision. Warmest wishes for a healthy and safe time this year. May we all be able to resume some of our pre-Covid activities.

The chart below shows the investment results of the Korean stock investment we hold. The remarkable returns since the plague-time low in the spring has far exceeded that our American markets. It is likely that such out-performance will continue.



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