Rochester Financial Services

Fee-Only® Financial Management Services

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December 7, 2021	Dow	S&P		Russell	10 yr			Crude
2 pm	Jones	500	NASDAQ	2000	Treas	Bitcoin	Gold	Oil
	35,748	4,690	15,708	2,266	1.47%	51,056	$1,784	$72.14

Investment Strategy Report

Volatility Is Back as The Fed and Covid Concerns Weigh On Stocks

Stocks climbed steadily during October and as a result, the volatility index (VIX) dropped to a low of about 15. That all changed in November as volatility returned to the stock market, which is another way of saying that there were large price swings, with a good number of them being to the downside. It was actually on Black Friday that the real fireworks began.

After modest up and down price movements for the first part of November, the S&P 500 dropped 2.3% on Black Friday, Friday 11/26, with the Dow dropping 905 points. The S&P recovered 1.2% the following Monday, but resumed its decline on Tuesday and Wednesday, 11/30 and 12/1, dropping 1.8% and 1.3%. This correction, from November 26th through Dec. 1st took the S&P 500 down 4.0%. The small cap Russell 2000 index dropped a much larger 8.0%. During this time, the VIX spiked higher to 31, as will happen when investors get nervous following large market drops.

The reason for this short term sell-off was an over-reaction to news of the Omicron variant on Thanksgiving day, according to JP Morgan's Marko Kolanovic. This was followed by more selling the following Monday based on disappointing news from Moderna. As I write this letter on Tuesday 12/7 (at 2 pm), we are in the midst of the second day of what Josh Brown on CNBC has called a "face ripper" market rally, with all market indexes up 2 to 3%. Kolanovic says yes, we can trust this bounce in the market. The post Thanksgiving Day selling was an over-reaction to the virus news. Investors who were short the market, expecting a repeat of the 4th quarter 2018 sell-off, are being squeezed as the market moves higher. He expects the pandemic to end next year and also is not convinced that the Fed will be as restrictive as some fear, so we can see the US market rise 10% in 2022. He expects even higher gains next year of 20% in both Europe and emerging markets.

Stephanie Link, chief investment strategist at Hightower, is very optimistic about the economy and thus, the prospects for the stock market. The economy is at all systems go, with unemployment now down at 4.2%. Home prices are up 19% and the ISM services index is at record highs, as is New Orders, which bodes well for next year's earnings and capital expenditures. She points out that the Atlanta Fed is forecasting 4th quarter GDP to come in at 9.7%, well above the 2% rate for the 3rd quarter. This will translate into 18% earnings growth. She stated that she is "long and staying long".

Louis Navellier, in his podcast today, stated that today's short covering rally, coming after yesterday's market surge, might very well mark the end of the market sell-off. He feels that some of this week's recovery is due to comments made over the weekend by world health organizations and Dr. Faucci stating that the Omicron variant may not be that dangerous. He also feels that investor fears of Fed tightening are overblown, especially since the 10 year Treasury yield is still below 1.5%. With the strong dollar, foreign money will continue to flow to US markets. Bank of America reported that $7 billion flowed into US markets last week, the biggest inflow since 2017.

The market technicians I follow also are sounding more optimistic based on the current rally. Charles Nenner (CharlesNenner.com) who has been negative on this market for several weeks, sees this rally pushing the indexes above market trend lines and thus has cancelled his sell signals. Jason Goepfert (sentimentrader.com) tracks the spread between what he calls the "Smart Money and Dumb Money", and it is currently at its widest value since April 2020. "The S&P 500's annualized return when the spread is above 45% (currently it's at 47%) was +52.6%, nearly 10 times the return when sentiment was neutral.

Of course, sentiment always turns ebullient on days like today and yesterday when all sectors of the market are rallying. I can guarantee that challenges will lie ahead for us next year. The key for 2022 might very well be to determine which sectors of the markets, US vs. foreign, developed countries vs. emerging markets, growth vs. value, large cap vs. small cap, will present us with the most promising opportunities. *Jeff Feldman*

Happy Holidays and A Very Safe and Healthy New Year!

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