CORBETT ROAD

MACRO MUSINGS

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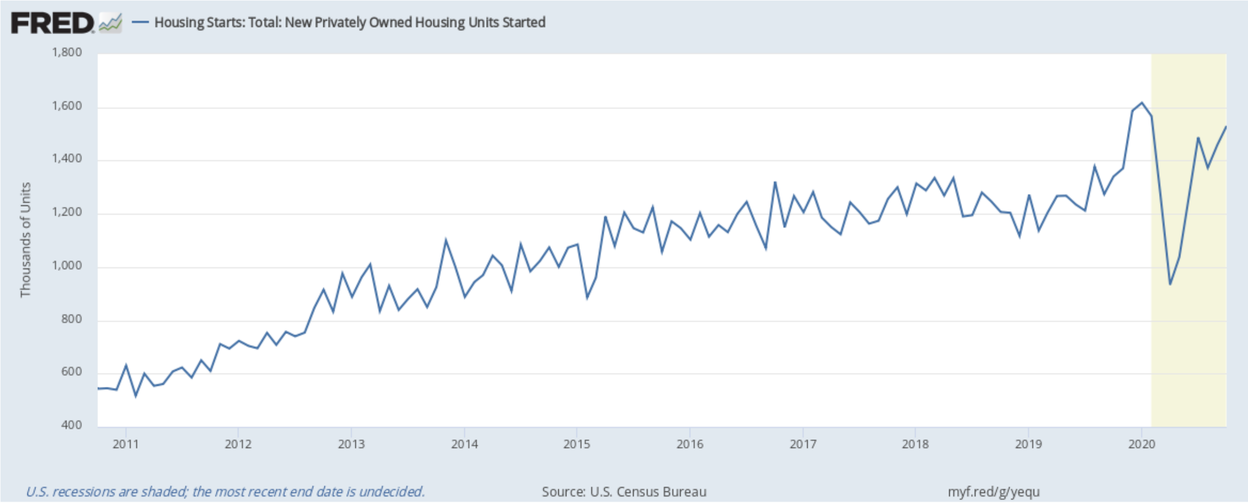
OUR 2021 OUTLOOK

SUMMARY

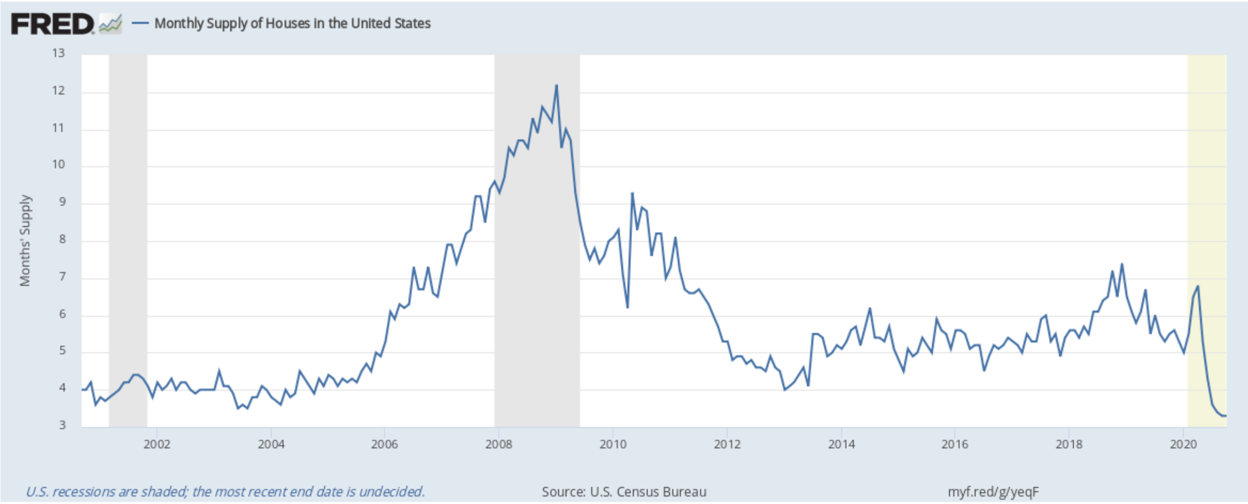
- **Economic growth should rebound in 2021 thanks to a red-hot housing market and strength in the financial positioning of households, which are in much better shape than they were after the last recession.**
- **The Federal Reserve has promised to support the economy as much as possible by keeping rates low until unemployment drops to pre-pandemic levels, even if inflation rises above their stated target of two percent.**
- **November saw some of the best gains ever for the S&P 500, which rose over 10%. In previous years, when we had a double-digit return month, the market was consistently higher six and twelve months later.**

THE HOUSING MARKET IS ON FIRE, AND THAT'S GREAT FOR THE OVERALL ECONOMY

Housing was one of the first sectors to rebound after the spring lockdowns. The combination of historically low mortgage rates, a pandemic driven exodus from major cities, and the millennial generation entering peak buying years proved to be a positive formula. New and existing home sales rebounded immediately, and both are at decade highs. Housing starts, a leading indicator measuring new residential construction, is also approaching pre-pandemic levels. The chart below depicts this V-shaped recovery:



Housing starts should continue to accelerate in 2021 as the supply of homes has fallen to a multidecade low:



This is great news not only for the housing market but for the economy as a whole. Housing activity leads to more spending and generates all types of additional business. People buy new furniture and appliances. They invest in home improvements like kitchen and bathroom upgrades. A surge in housing starts and building permits can boost demand for contractors, creating new construction jobs and boosting employment.

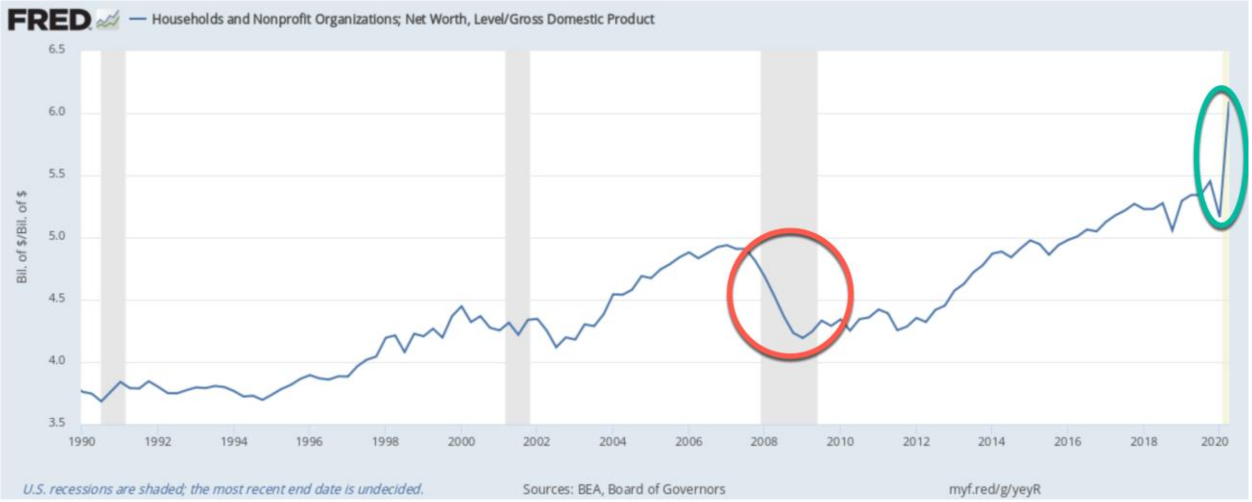
With service industries like restaurants, travel, and entertainment suffering, it is important for other areas of the economy to pick up the slack. The housing market has been doing so all year, and we expect that to continue in 2021.

HOUSEHOLDS ARE IN THE BEST POSITION COMING OUT OF A RECESSION IN DECADES.

The biggest difference between the pandemic recession and the global financial crisis of 2008-2009 is how strong household finances are this time around. In the previous recession, both housing prices and the stock market saw severe drawdowns in value, decimating household balance sheets, which have most of their wealth tied to those two forms of investment. Net worth collapsed and did not meaningfully start recovering until 2012.

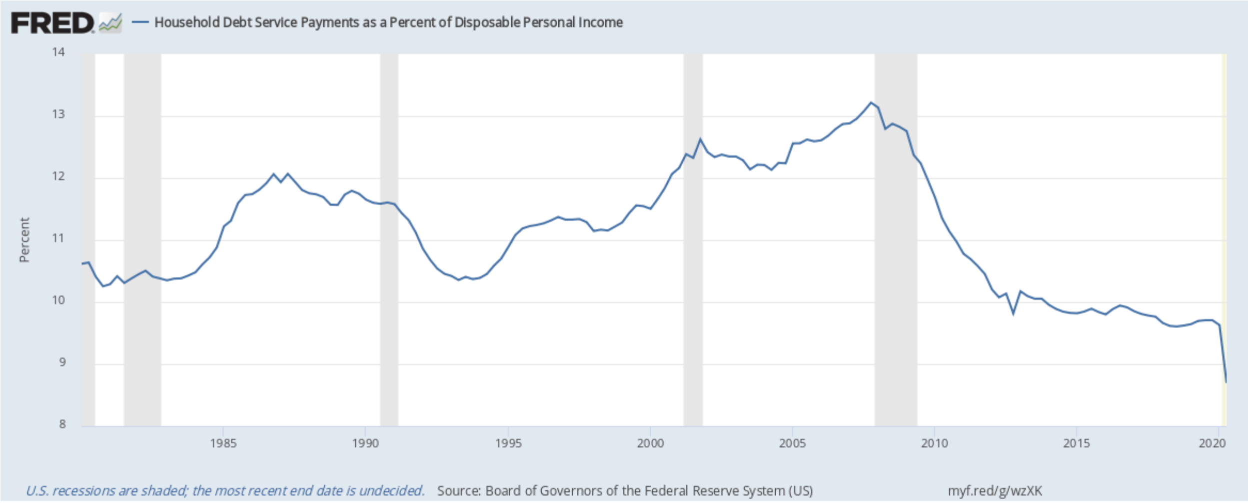
Contrast that with today, where a hot housing market and a quick market rebound have left households in a much stronger position. Part of this was due to the recession's short-term nature, but credit is also owed to the fiscal and monetary policy responses. The CARES Act, passed by Congress, provided direct income to the unemployed and financial support to businesses, while the Fed's unprecedented actions helped stabilize the credit markets.

The following chart shows the drastic difference. It looks at the net worth of households compared to GDP:

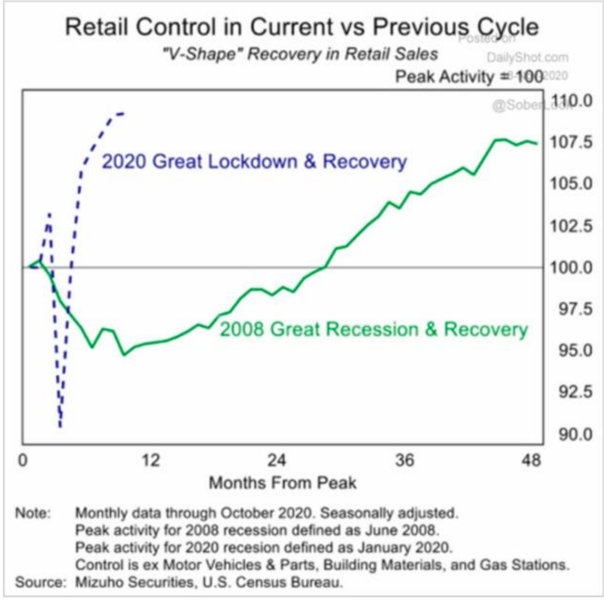


In 2008-2009 this ratio collapsed, and in 2020, it has spiked to new all-time highs.

Further, interest rates continue to remain at record lows. This is great news for anyone who needs to borrow money (not so great for savers who only hold cash), and the lower interest payments owed on debt leaves consumers with more disposable income to spend on goods and services:



These trends support an increased capacity for consumer spending, which is clearly reflected in the chart below (from WSJ) that shows how quickly retail sales recovered to their previous highs in 2020 compared to 2008:



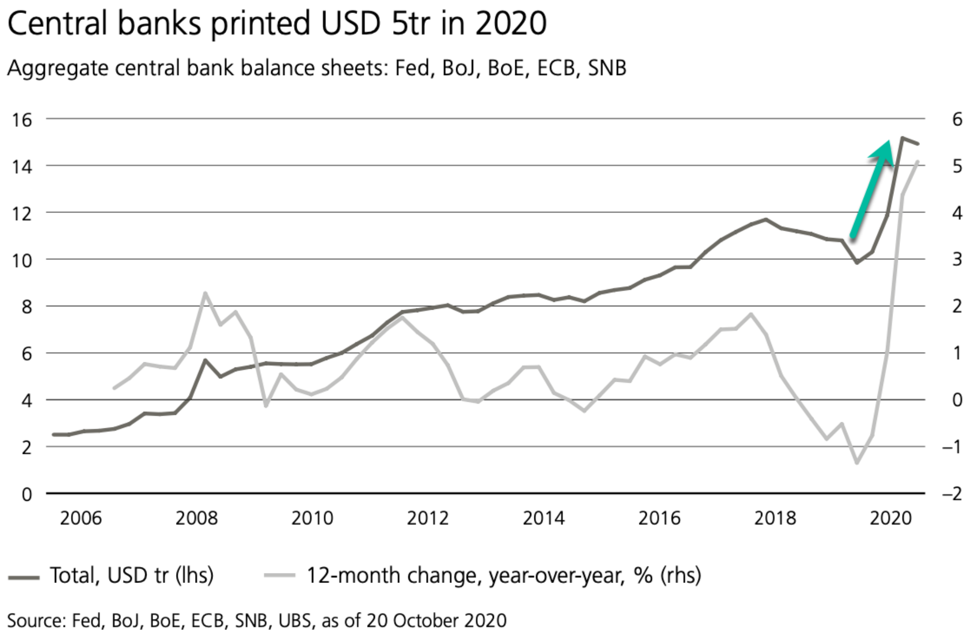
Strong consumers and households will be key to sustaining the economic recovery in 2021.

THE FED HAS PROMISED TO KEEP RATES LOW UNTIL UNEMPLOYMENT DROPS FURTHER

Even with a strong recovery, the Fed has signaled it will not be raising rates until unemployment falls closer to pre-pandemic levels. This is the Fed's position even if inflation exceeds their target of two percent.

Meanwhile, central banks around the world have flooded the credit markets with liquidity to ensure that the banking system does not freeze up.

The following chart shows just how significant that support was. The Fed and its counterparts across the globe were not going to repeat the mistakes of the past, and they took quick, aggressive action in expanding their balance sheets (chart from UBS):



STOCKS WERE UP OVER 10% LAST MONTH. HISTORICALLY, THAT HAS LED TO FURTHER GAINS.

The positive vaccine news helped trigger massive inflows into stocks. This drove stocks to record highs, and the S&P 500 rose over ten percent in November (table from LPL):

What Happens After 10% Monthly Gains? Bulls Smile

Historic S&P 500 Index Gains Have Led To Continued Strong Returns

		S&P 500 Index Return			
Date	**S&P 500 % Change**	**Next Month**	**3 Month**	**6 Month**	**12 Month**
October 1974	16.3%	-5.3%	4.2%	18.1%	20.5%
January 1987	13.2%	3.7%	5.2%	16.3%	-6.2%
April 2020	12.7%	4.5%	12.3%	12.3%	?
January 1975	12.3%	6.0%	13.4%	15.3%	31.0%
January 1976	11.8%	-1.1%	0.8%	2.6%	1.2%
August 1982	11.6%	0.8%	15.9%	23.9%	37.3%
December 1991	11.2%	-2.0%	-3.2%	-2.1%	4.5%
October 1982	11.0%	3.6%	8.7%	23.0%	22.3%
October 2011	10.8%	-0.5%	4.7%	11.5%	12.7%
November 2020	**10.8%**	?	?	?	?
August 1984	10.6%	-0.3%	-1.9%	8.7%	13.2%
November 1980	10.2%	-3.4%	-6.6%	-5.6%	-10.1%
November 1962	10.2%	1.3%	3.3%	13.7%	17.6%
	Average	0.6%	4.7%	11.5%	13.1%
	Median	0.2%	4.4%	13.0%	13.2%
	% Positive	50.0%	75.0%	83.3%	81.8%

Source: LPL Research, FactSet 11/30/2020 (1950 - Current)
All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.
The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

It was the tenth highest return in a calendar month since 1950. In previous cases, when the market was up double-digits in one month, returns were mixed in the short term but higher six or twelve months later in all but two instances. Big rallies like we had in November have historically been a sign of optimism and not "the beginning of the end" of the bull market.

THE BASE CASE FOR 2021: MOVING TOWARD NORMAL

Thanks to a strong housing market, Fed support, and a well-positioned consumer, we believe that the economy is poised to continue its rebound in 2021. We view the successful deployment of vaccines as the catalyst that triggers additional growth in areas of the economy that have been hurt the most by the pandemic.

This is the final Macro Musings of the year. We will publish our 2020 Year in Review late next month.

HAPPY HOLIDAYS

We at Corbett Road would like to thank all of our clients and partners during this extremely challenging year. While the markets and economy have rebounded, we know what a difficult several months it has been for many of you. We want to wish you a happy and safe holiday season and a successful New Year. Thank you for your continued trust and business.