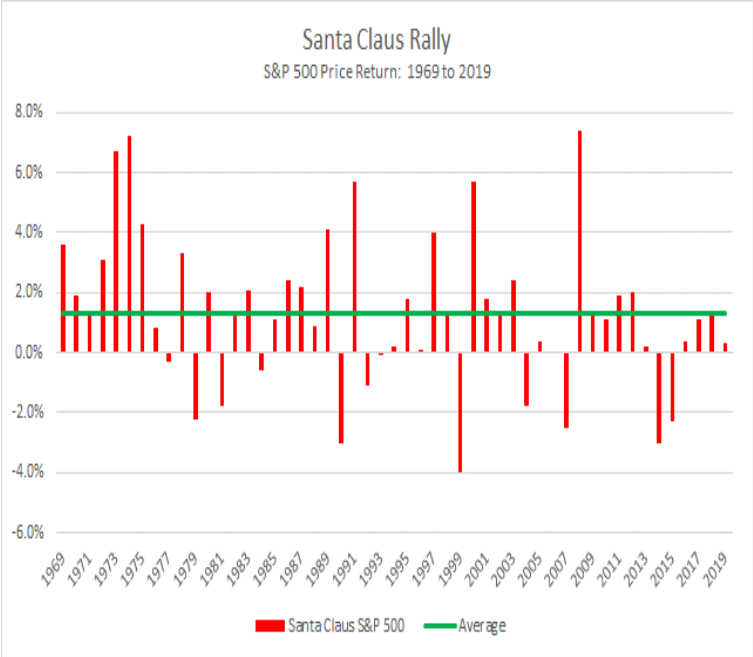
STONE INVESTMENT PARTNERS LLC

Weekly Market Guide | December 21, 2020

CHART OF THE WEEK – HERE COMES SANTA CLAUS



Source: Stone Investment Partners, Stock Trader's Almanac, Bloomberg as of 12/21/2020

An old Wall Street maxim states: "If Santa Claus should fail to call, bears may come to Broad and Wall." The Santa Claus indicator, as defined by the Stock Trader's Almanac, consists of the last five trading days of the current year and the first two days of the new year. Despite this well-turned phrase, our analysis shows that Santa seems to have limited forecasting ability. In the twelve years with a negative S&P 500 return for the Santa Claus indicator, the market was down only five times in the following year, a hit rate of almost 42%. While Santa's crystal ball is cloudy, he does seem to bring good cheer most years with the S&P 500 rising an average of 1.3% during those seven trading days since 1969 (see chart). In addition, the S&P 500 is higher during the Santa Claus rally period over 76% of the time which is much higher than any normal period. In 2020, the Santa Claus period runs from December 24 through January 5. Time will tell if the seasonal market blessings arrive in 2020 or if the news of the vaccine approvals, fiscal stimulus and the resultant elevated investor sentiment caused investors to open their gifts early. In the short-term, economic data has slowed with the increased infections. This will be our last weekly report for 2020 as data winds down for the holidays. Our **U.S. Reopening Monitor** will be updated next week and can be viewed on our website in the blog section. On behalf of Stone Investment Partners, wishing you and your families a very Merry Christmas and a healthy and prosperous New Year. Stone Investment Partners looks forward to sharing an exciting announcement with our readers in early 2021.

WEEK IN PREVIEW

- Geopolitical: The U.S. Congress is poised to pass a $900 billion pandemic relief bill which includes small business support, a direct payment to most individuals, supplemental unemployment benefits and funding for vaccine distribution. Another deadline for the Brexit trade negotiations between the European Union (E.U.) and U.K. has passed but the calendar is conspiring to bring it to a close soon with a narrow trade deal the most likely outcome. Increased restrictions continue in many parts of the globe to combat the resurgence in COVID infections, and the impact on economic activity will be closely monitored but revisiting the economic collapse of wholesale lockdowns during Lockdown 2.0 remains unlikely. Moderna's vaccine for COVID-19 received emergency authorization by the U.S. Food and Drug Administration (FDA) last week. A mutated strain of COVID-19 has been identified in the U.K., but the World Health Organization (WHO) says there is no indication that the vaccines will not be effective against it. U.S. markets close early on Thursday and remain closed on Friday for the Christmas holiday with many global markets closed as well.
- U.S.: It is a surprisingly busy economic calendar for a holiday-shortened week, but all eyes will be on the addition of Tesla (TSLA) to the S&P 500 index on Monday. TSLA will be the largest company to ever join the S&P 500 and will be the sixth-biggest market capitalization weight in the index, ahead of Berkshire Hathaway (BRKA, BRKB). The Russell 1000 index and the widely used ETFs (ITOT & VTI) from iShares and Vanguard tracking the broad U.S. stock market already contain TSLA. An excellent analysis by Research Affiliates looks at the outlook for TSLA and notes that an average stock added to the S&P 500 outperforms prior then underperforms in the year following addition. November housing data is expected to soften a bit but remain at robust levels underscoring the strength of the sector. November durable goods orders should continue to rise, but personal income and spending are likely to reflect some weakness. Following a second round of stress tests, the Federal Reserve announced that banks can restart stock buybacks while dividend policy remains unchanged. The Atlanta and NY Fed's estimate of 4Q GDP growth is 11.1% and 2.4%, respectively. Readings for our **U.S. Reopening Monitor** bounced back a bit despite tightening restrictions under Lockdown 2.0 as COVID cases and deaths rose. Underlying high frequency economic data showed improving mobility, airline travel and retail sales while consumer sentiment, jobs and dining showed softening.
- S&P 500 Earnings: 3 S&P 500 companies are scheduled to report earnings: CarMax (KMX), Cintas (CTAS) and Paychex (PAYX). 4Q 2020 earnings and sales estimates are now -9.7% and 0.1% year-over-year (Y/Y), respectively. 2020 calendar year earnings are expected to be -13.6% Y/Y, while sales are -1.8%. A strong rebound is forecast for 2021 with earning 22.1% and sales 7.9% Y/Y. Consensus earnings estimates for 2020 and 2021 increased again last week.
- Europe: The rate of growth in Eurozone COVID cases retreated again slightly. Restrictions across much of the globe continue to impact dining with a -58% decline from the global baseline. Germany and Italy saw a decline in the weekly infection pace, while France and Spain saw an uptick. Consumer confidence readings for the Eurozone and Germany are likely to be depressed by the lockdowns. The U.K. pace of infections marched higher, while U.K. dining fell to -37.4% Y/Y versus baseline. The U.K. economic calendar is quiet with Brexit trade negotiations as the primary focus. Please see our **U.S. Reopening Monitor** for international COVID charts.
- Asia: China's economic calendar is empty. The weekly pace of COVID infections in Japan rose for the twelfth straight week and hit another all-time high. Japan monthly employment data for November is on tap with both the unemployment rate and job-to-applicant ratio expected to hold steady at 3.1% and 1.04, respectively. November Japan retail sales are expected to decline by -0.8% for the month which would drag the Y/Y rate down to 1.7% from 6.4%.
- Central Banks: The central banks of Thailand, Uruguay and Egypt are scheduled to meet with no major banks expected to change their policy rate.

WEEK IN REVIEW

- Stocks rose by 1.3% for the S&P 500 with nine of eleven sectors higher for the week. Technology (3.2%), consumer discretionary (2.3%) and materials (1.9%) outperformed the S&P 500, while energy (-4.3%), communication services (-0.5%) and industrials (0.1%) were the biggest laggards. WTI (5.4%) and Brent (4.6%) oil were higher with MLPs (-3.9%) and the energy sector (-4.3%) weak.
- Large cap value as measured by the Russell 1000 Value underperformed at 0.2%. Banks underperformed with the Invesco KBW Bank ETF (KBWB) lower by -0.7%. High dividend strategies underperformed the S&P 500 with the iShares Select Dividend ETF (DVY) falling -1.5%. Momentum outperformed with the iShares MSCI Momentum ETF (MTUM) rising by 3.4% for the week. Small-cap stocks outperformed relative to the S&P 500 with the Russell 2000 higher by 3.1% but small-cap value stocks underperforming at 1.3%. The 10-year and 30-year U.S. Treasury yields were higher at 0.95% and 1.69%, respectively.
- High yield credit spreads narrowed reflecting increased risk appetite. AAA municipal bond yields as a percentage of Treasuries fell, causing municipal bonds to outperform.
- The U.S. dollar was weaker against both developed currencies and emerging market currencies. Developed international stocks as measured by MSCI EAFE outperformed the S&P 500 returns in U.S. dollar terms (2.0%) but underperformed on a hedged-currency basis (1.0%). MSCI Japan kept pace with the S&P 500 returns in U.S. dollar terms (1.3%) but underperformed on a hedged-currency basis (0.7%). Emerging market stocks underperformed the S&P 500 with a non-hedged return of 0.9% for MSCI EM.
- The 10-2 yield curve widened to +82 basis points. Another curve measure of three-month yield six quarters forward minus the current three-month yield decreased to +8 basis points. The yield curve has historically provided an accurate forecast of future recessions when the difference in these measures turns negative, also known as inversion. Yield curves are one of the major indicators that we monitor to judge recession risk, but these inversions typically happen more than a year in advance of an economic recession. External shocks like the current coronavirus-induced recession might not be accompanied by inversion. Stocks have historically had significant advances post-inversion.

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Disclosures

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