Investor Intelligence Newsletter©

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From the Executive Desk

Dr. Edmundo J. Garza
Chief Executive Officer & President

After a strong start to 2021, most equity markets loss their momentum as January closed. Emerging markets outperformed, up about 3%, but developed market equities ended the month down 1%. Initially, the global roll out of Coronavirus vaccines and the promise of further fiscal and monetary stimulus in the U.S. helped the market overlook concerns about pandemic driven restrictions. However, delays in immunization efforts increased contributing to a sell-off that drove a slump in equities towards the end of the month. Despite continued delays in Europe the vaccine rollout is now progressing well in the UK and US and there was recent positive news about the Novavax and Johnson & Johnson vaccine trials. Overall, the economic data paints a mixed scenario in the U.S., where the manufacturing index rose to 59.1, and housing construction starts continued to rise through December at the fastest pace since 2006, but employment and consumer confidence metrics stayed well below pre-covid levels. The victories in the two Senate races in Georgia handed Democrats control over Congress, boosting further support for the $1.9 trillion "American Rescue Plan", which is in addition to the bi-partisan $900 billion stimulus package approved in December. Even if the bill gets toned down by congress, the macroeconomic impact should be dramatic as the overall stimulus bill for 2021 is likely to be worth close to 10% of GDP. Increased expectations of government spending should put upward pressure on long-dated US Treasury yields and for equities, the improving near-term growth prospects should provide support to value sectors and small cap markets. Finally, President Biden's stance on climate policy should generate opportunities in real assets and renewables that will continue to speed up the U.S. transition to alternative energy and fuels.

Economic Perspectives

Myrna Rivera, CIMA®
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After a decade of US dominance, 2021 could mark the beginning of Asia's reign over global markets. The region has been more successful in containing the pandemic, and it has many growth prospects in its favor. A recovery in both domestic and foreign demand for Chinese goods and services led to accelerated economic growth in the fourth quarter of 2020. Real GDP rose by 6.5% year-over-year, marking a return to pre-covid growth rates. China might very well be the only large economy to achieve positive GDP growth in 2020. As infection rates dropped and domestic economic activity resumed, the hard-hit service sector caught up with industrial sectors during the third quarter. Trade normalization and strong demand for remote work technology has also supported growth. Chinese manufacturers have been able to gain market share as international competitors have been hampered by lockdowns and supply chain disruptions. As a result, Chinese industrial production increased by 7.3% year-on-year in December, and exports rose 18.1% year-on-year, leading to a record trade surplus for the month. Japan, the world's third-largest economy grew by an annualized 12.7% in the fourth quarter of 2020 compared with the previous quarter, marking the second-straight quarter of expansion and exceeding forecasts. A global rebound in manufacturing activity gave Japan's exports a much-needed boost, especially to China, making up for weakness in domestic demand. Lastly, while the International Monetary Fund expects the Indian economy to have contracted by 8% in 2020, it has revised its growth forecast upwards to 11.5% for 2021. The IMF's revision reflects expectations of a vaccine-powered strengthening of activity later in the year, making it the only major economy expected to register double-digit growth amidst the pandemic.

Indicators **(As of January 31, 2021)**

United States:
CPI: +1.4% Chg. from yr. ago
Unemployment Rate: 6.3%
GDP: 4.0% Comp. Annual rate of Chg. on 2020: Q4
Ind.Prod.Index: 0.9% change from previous month
Source: *St. Louis Fed. Res.*

Japan:
CPI: -0.6% Chg. from yr. ago
Unemployment Rate: 2.9%
GDP: 3.3%, Comp. Annual rate of Chg. on 2020: Q3
Ind.Prod.Index: -1.6% change from previous month
Source: *Moody's Analytics*

Euro Zone:
CPI: -0.3% Chg. from yr. ago
Unemployment Rate: 8.3%
GDP: 12.5%, Comp. Annual rate of Chg. on 2020: Q3
Ind.Prod.Index: 2.5% change from previous month
Source: *Moody's Analytics*

Puerto Rico:
CPI: 0.1% Chg. from yr. ago
Unemployment Rate: 9.1%
Payroll Employment: -7.7% Chg. from yr. ago
EDB Econ. Act. Index: -7.1% Chg. from yr. ago
Source: ***P.R.E.D.B.***

Market Recap

Evangeline Dávila, CIMA®
Chief Research & Investment Officer

Stocks: U.S. equity benchmarks ended mixed in January after late-month selling. Active participation by retail investors kept trading volumes elevated throughout the month and reached record levels late in January amid buying partly coordinated on social media website Reddit. The S&P 500 and the Dow Jones Industrial Average recorded modest losses, while the Russell 2000 notched a solid gain. Energy and health care shares outperformed, while consumer staples and industrials stocks fell sharply. Shares in Europe fell as worries intensified about the economic damage caused by the spread of coronavirus variants, the extension of national lockdowns, and delays in vaccination programs. Stocks in Japan posted solid gains in early January but suffered a steep decline at the end of the month. The blue-chip Nikkei 225 Stock Average ended the period with a 0.8% gain, while the broad Japanese market recorded a loss.

Bonds: Stimulus hopes helped push the yield on the benchmark 10-year U.S. Treasury note above 1% for the first time since March, weighing on bond returns. Municipal bonds outperformed, aided by hopes for federal support to shore up state and local finances and solid demand as investors reinvested January coupon payments. Japanese government bond yields rose modestly, with the 10-year bond closing the period yielding 0.06%. The yield on China's 10-year government bond edged up 2 basis points to close at 3.21%.

Alternatives: In currency trading, China's renminbi gained 1.6% against the U.S. dollar, with the USD-RMB exchange rate falling below 6.50 for the first time since 2018. The yen weakened versus the U.S. dollar and traded above JPY 104 at the end of the month.

What to Do?

Democrats "sweeping" of Congress and the White House may seem to assure the passage of another coronavirus relief package, but there's considerable doubt about whether President Joe Biden will be able to secure the full $1.9 trillion in proposed spending. Absent sufficient support from Senate Republicans, Democrats may also have to rely on the "budget reconciliation" process to pass a bill, which would place limits on certain types of spending. U.S. efforts may pale in comparison to China's, who is leading the global economic recovery in 2021. China's economy expanded by 2.3% in 2020, a remarkable recovery from a record contraction in the first quarter. Real gross domestic product growth in the fourth quarter accelerated to 6.5% year over year, making China the only major economy to regain its pre-pandemic momentum. China's strong economic momentum is likely to lead to a broad-based recovery in corporate earnings, but political risk might increase if China's recent trade success comes under scrutiny from the Biden administration. ***Hence, we continue to recommend prudent asset allocation and risk assessment, based on future capital needs for plan sponsors, institutions, and individual investors. We continue to believe that higher quality assets are favored. We believe rebalancing is fundamental to a well-executed long-term investment strategy, and that due diligence reviews and an adherence to a well-developed investment policy remain the most prudent course of action for long-term investors.***