STONEBRIDGE
Capital Advisors

The Stonebridge Market Commentary

February 2, 2021

Equity Commentary provided by David A. Eckenrode
Director of Equity Management

Fixed Income Commentary provided by Jon F. Lynn
Senior Analyst & Portfolio Manager

Equity Commentary

So, we are off to the races in another year. As has been the case for many months, we have approached month's end with a dollop of price volatility. So far, the market has been flat, oil has risen, and all seems right with the way things are generally. The economy has moderated but reported earnings have been good versus expectations. That said, everything seems to be hanging by a thread as we await further lockdowns and or stimulus payments from the government. So, it is a normal January.

Spring awaits and everything will be better...right? What seems real at this point is that the vaccinating of 333 million continues and may point us toward exiting our current malaise, or not. We have not quite figured out what conditions are needed to get the country to a more comfortable level, or even to a point where we do not have to wear masks or be in lockdown.

On the other hand, I would be remiss if I did not acknowledge the short squeezes happening in Game Stop, Bed Bath and Beyond, AMC and others. Seems like the Reddit crowd attacked the high short interest hedge funds by buying heavily shorted names. The hedge funds responded by hemorrhaging cash and then complaining loudly that the plebes were taking advantage and need to be stopped. This will be very interesting to watch and could last for more time than people are assuming. Thankfully, Stonebridge does not gamble on these "Reindeer Games".

As for January, what would a month be without the requisite end of month freak out (EOMFO)? Nothing new I guess. It seems that every month ends with a big surge in volatility and of course, the EOMFO. This month, along with a new administration, protests in Washington, an impeachment and a guarded Fed Chair, not to mention the ongoing COVID battle, we had the big squeeze as noted above.

So, for the month, things were going swimmingly until the squeeze put the kibosh on sentiment until further notice. The EOMFO shaved some 3.58% off the month's total making January a wash. Yes, there were other factors like the potential of a new tax plan. For our part we will wait to see what happens rather than speculate on trial balloons out of Washington. We figure taxes are going up but where and by how much? Wait for a bill so we can see what we have to adapt to if it passes.

The beginning of 2021 was going well until the last week where we shaved off over 3.5% from the S&P. The big loser was the Dow, off 2.04%, the big winner was the NASDAQ which gained 1.42%, leaving the S&P 500 in the middle having lost 1.11%. Markets thrive on confidence and we have just witnessed how rough it can get when confidence is shaken.

After all of this going on the S&P 500 finished the month only 156 points from the all-time high.

Fixed Income Commentary

Fixed income assets performed remarkably well in 2020. The Fed's hand in the markets helped corporate bond spreads tighten and low yields to persist as income seekers were lured into either stretching duration, lowering credit quality or both to pick up yield. That helped to keep high yield or junk bond spreads relatively tight, despite increasing distress and bankruptcy filings in several sectors, which typically might cause caution and put pressure on yields. The largest moves in rates took place on the short end of the curve. The yield on 2-year Treasuries plummeted from around 1.60% at the beginning of the year to around 0.12% at year end. During the same time period 10-year yields shed around 1% to end the year around 0.93%. Moving into 2021, the yield on 10-year Treasuries bumped up above 1% and have consistently stayed there.

Short-term rates remained low for much of the last year and are expected to continue to be anchored there by central banks for an extended period. Longer U.S. rates have inched higher, leading to speculation the Fed may eventually shift its bond buying further out the yield curve in its efforts to keep yields in check. Corporate bonds, both investment grade and junk continue to find strong demand with some of the riskiest borrowers having little trouble finding investors willing to loan them money.

In the coming months with a new administration and shift in power in congress, we could see the SALT deduction cap lifted and perhaps a reintroduction of tax-exempt advanced refundings in the municipal market. Either of which has the potential to help to break municipals out of the very low yield ratios compared to taxable bonds, making them more attractive on a relative value basis, by either easing demand or increasing supply.

Finally, as the Reddit-Robinhood saga has captivated the attention of equity markets, it also has had some interesting side effects on the credit markets as well. It seems the run up in the stock price of AMC Entertainment may have saved it from bankruptcy. The higher stock price allowed it to raise additional capital by selling new shares and converting a portion of its bond debt to stock, lowering its leverage. It reminds me of the adage, "markets can remain irrational longer than you can stay solvent". Or in this case maybe an irrational market helped a company stay solvent.

Sources: Data sourced through Bloomberg, Morningstar and StockCharts