Great-West Investments Capital Markets Perspective

Week in Review: June 1st -5th

INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD
Dow Industrials	Lg. Cap Eq.	34,756.39	0.66%	14.40%
S&P 500®	Lg. Cap Eq.	4,229.89	0.61%	13.39%
NASDAQ Comp.	US Equity	13,814.49	0.48%	7.56%
S&P Midcap 400©	Mid-Cap Equity	2,728.67	0.05%	18.30%
Russell 2000®	Sm. Cap Eq.	2,286.41	0.77%	15.55%
Stoxx 50	Europe Eq.	4,089.38	0.46%	14.40%

INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD
FTSE 100	UK Equity	7,069.04	0.66%	9.42%
Nikkei 225	Japan Equity	28,941.52	-0.71%	5.46%
EEM:US	Emkt. Equity	$55.99	2.04%	8.89%
EFA:US	Non-US Equity	$81.68	1.05%	11.89%
UST 10y (yield)	US Treasury	1.56%	-0.04%	0.65%
B/Barc AGG	Fixed Inc.	2,340.14	0.12%	-2.08%

Overheard on a reddit chat yesterday: "…yeah, but *free popcorn*!"

Okay, I didn't really overhear that. I'm not even sure I could tell the difference between a "subreddit" and a subway sandwich, so the idea that I've been prowling reddit boards looking for content for this week's review is pretty outlandish. But whether or not that kind of conversation actually took place between dueling Redditors debating the merits of investing in theater chain AMC is kind of beside the point: **the fact that it's pretty easy to *imagine* such a conversation taking place is reason enough to scratch your head a little and wonder exactly where this all ends**.

For those who don't know, what I'm referring to is last week's announcement by AMC CEO Adam Aron that **shareholders of theater chain AMC could register on the company's Investor Connect website and receive, apparently among other perks, a free large popcorn**[1]. Now, that may be a perfectly legitimate strategy to entice a certain type of shareholder (especially when you consider that the current price for a single share of AMC isn't too far from the price of two tickets, sodas and a large popcorn at one of its venues[2]), and the last thing I want to do is to enter into a debate about the suitability of any individual stock as a potential investment – least of all a meme stock like AMC. But one thing that last week's announcement did for me is make me feel, once again, hopelessly old school: **I guess things like dividends, potential capital gains and the other benefits of being a public company shareholder are starting to look a little old-fashioned**.

So what is it about AMC's free popcorn announcement that gives it top billing in this week's commentary above more fundamentally interesting – and potentially far more consequential – things like still-surging PMIs and a second payrolls miss in as many months? (More about those in a minute…) I suppose it's the unshakable feeling that **listing free popcorn as one of the benefits of share ownership somehow might represent the most strikingly unexpected example of froth** I've seen since that time I mistakenly ordered an iced cappuccino with cold foam at Starbucks. But either way, the free popcorn gambit is enough to **make me wonder exactly how much of the current asset-price**

[1] https://twitter.com/ceoadam?lang=en
[2] Here in the suburbs, matinee tickets run about $14 bucks. Buy two of those (who goes to the movies alone??), add $12 for two sodas and $8.50 for popcorn and you're at $48.50. This morning, AMC was trading around $57 (movie price data: movietheaterprices.com).

euphoria is a result of the easy money policies put in place by virtually every policymaker on the planet in response to COVID, rather than actual fundamentals.

And that matters, because **at some point** (who knows when?) **those policies will end**, and the music will stop. And who knows, when all that liquidity goes away, free popcorn might seem like a pretty good deal.

Okay, that was a little darker than I wanted it to sound. After all, **with foam or without, the market has done just fine** as the US economy continues it's climb-out from the depths of the pandemic, and this week, we had further, ample illustration of those exact points. First, in terms of the pace of recovery, **last week's ISM and PMI data went four-for-four, with the manufacturing and services sectors outperforming expectations pretty much across the board**. The best quote from all four reports may well have been this one, from Markit Economics' services PMI: "**the US economy shifted up a gear," and may register double-digit growth during the second quarter**[3]. Of course, that report (and nearly half a dozen others like it, including the Fed's Beige Book[4],) was rife with mentions of pricing pressure, lagging vendor performance and other supply chain stress, but we don't worry about those anymore, right?

As far as the mood of the market is concerned, last week's best example of investor durability came on Friday, when the Bureau of Labor Statistics' closely-watched **employment situation report missed economist estimates for a second month in a row**. To be clear, this month's payrolls shortfall was nothing like April's, when job creation fell short by 750,000 or so (this time, the miss was a far more palatable ~100k.[5]) The market took the news very much in stride, with **stocks actually having their best day of the week following the release**.

It's tempting to give credit for that seemingly backwards reaction to an improvement in the overall unemployment rate, which actually declined by 0.3% to 5.8% even though payrolls was a miss. But that would probably be a mistake: unemployment likely fell for the "wrong" reason, namely **a drop in the participation rate** – which essentially measures how many workers have a job or are actively looking for work. Alternatively, you might point to the **faster-than-expected 0.5% boost in hourly earnings** as the reason for the market's upbeat reaction. After all, if workers are earning noticeably more for the same amount of work than they were last month, that should goose economic growth even further, right? That, too, would be a mistake: in fact, **the acceleration in wages was probably the *worst* surprise in the release, because it feeds the inflation narrative** that has kept investors on edge for months.

No, the market's willingness to rally on the back of a second consecutive disappointing jobs report was very likely a result of the fact that it **implied the economy has failed to show enough progress on employment to compel the Fed to normalize policy anytime soon**. That means the deluge of liquidity that has likely kept meme stocks like AMC so well-oiled will probably continue for at least another few months. Said another way, risk markets are acting very much like addicts: something that may not be all that healthy from a macroeconomic perspective (i.e. weaker-than-hoped-for employment growth) is nonetheless good for how markets feel. (Come to think of it, that's not altogether unlike the relationship that I have with AMC's buttered popcorn…)

But we need to close this part of our weekly conversation with **one item that very much *is* consistent with a normalization of policy:** the Fed's announcement that it would begin to **unwind the portfolio that it acquired under the Secondary Market Corporate Credit Facility, or SMCCF**[6]. That was the somewhat controversial program begun by the Fed at the start of the pandemic which allowed it to purchase investment grade corporate bonds and ETFs as a way to ensure the smooth functioning of those markets. The program never grew even close to the gargantuan size that critics feared it might (the Fed reportedly holds a mere $14b in the SMCCF portfolio versus it total balance sheet of more than $7 *trillion*,) and it quit buying new assets way back in December. That's probably why **the Fed's announcement that it would begin selling those assets failed to gain much attention**. But make no mistake, the unwinding of the SMCCF **seems very much like the Fed sticking its toe in the water of a post-pandemic normalization of policy**. That, depending on your perspective, can feel like a very good thing, or a very scary thing.

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[3] https://www.markiteconomics.com/Public/Home/PressRelease/1092ca7290b24f8880984fce9ba10698
[4] https://www.federalreserve.gov/monetarypolicy/files/BeigeBook_20210602.pdf
[5] https://www.bls.gov/news.release/empsit.nr0.htm
[6] https://www.federalreserve.gov/newsevents/pressreleases/monetary20210602a.htm.

What to Watch This Week: June 6th – June 12th

Notable economic events (June 6th – 10th)

Monday: *no major releases planned*

Tuesday: NFIB small business sentiment, JOLTS

Wednesday: Wholesale inventories

Thursday: CPI inflation, weekly jobless claims, ECB decision

Friday: UofM consumer sentiment, G7 meeting

It promises to be a relatively quiet week, with **Thursday's consumer price index release perhaps the most interesting thing on the calendar**. CPI has been elevated for several months, and for obvious reasons: in addition to so-called "base effects" (which simply recognize the fact that today's numbers are being compared to last year's unusually depressed figures,) consumers have also had to contend with what feels like legitimately higher prices for things like gasoline, groceries, houses and just about everything else they buy. While **investors have been somewhat more tolerant in recent months given policymakers' repeated assurances that its all temporary**, at some point prices will have to ease if that argument is to remain credible. People will watch this week's CPI for evidence of which way the discussion is breaking.

Next up on the list of things to watch is probably Thursday's announcement by the European Central Bank (ECB.) There seems to be little chance that the ECB will do anything as rash as slow its QE program (it certainly won't move on rates,) but given how tightly central bank policy seems to be coordinated across international boundaries during these pandemic-tinted times, investors will scour the post-meeting announcement and press conference for **any indication that the ECB – and, by extension, it's central bank peers in other regions – is becoming less dovish**.

Similarly, **Friday's convening of the G-7 Summit** in the UK will provide market-watchers with an opportunity to **see if the prevailing wind has shifted with regard to fiscal support as well**. One interesting item likely to be on the agenda is a deeper discussion of a proposed 15% minimum corporate tax – an idea designed to target multinationals who seek low-tax domiciles to reduce their tax bills. The proposal gained support from each of the G7's finance chiefs over the weekend,[7] leaving the various heads-of-state at this week's meeting to discuss the details. Here at home, that kind of a deal could help ease opposition to President Biden's proposed increase in corporate taxes by weakening the argument that higher corporate taxes in the US will simply cause businesses to flee to overseas tax havens. The idea that the G7 luminaries could somehow magically help heal what is a deeply partisan divide here in the US seems like a long shot to me, but the idea will nonetheless probably continue to draw ink this week.

Finally, under the "odds and ends" category, this week will have **two important reads on confidence** – **the NFIB's small business confidence index on Tuesday and the University of Michigan's preliminary read of June consumer sentiment on Friday**. Both business- and consumer confidence have started to waiver amid rising inflation and other stresses, suggesting that this week's data could get some added attention. Likewise for **Tuesday's JOLTS data** (which will provide a deeper look at who's hiring, who's looking for work, and who isn't.) With labor markets very much at the center of today's capital market debate, I'd look for that release to get some play.

Source for index data: Bloomberg.com; GWI calculations.

[7] https://www.reuters.com/business/g7-nations-near-historic-deal-taxing-multinationals-2021-06-05/