MV CAPITAL MANAGEMENT

Weekly Market Flash

Ignore the Rumor, Ignore the News

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One of the many old chestnuts of Wall Street wisdom in days of yore went thus: sell the rumor, buy the news. The thinking was that once some idea gained enough traction to be relatively plausible, all the price action would play out well before the thing actually came to pass. Is the Fed going to raise interest rates? Sell now. By the time the formal announcement comes out, the price will probably be low enough from all that selling to merit a buying opportunity. Sounds perfectly rational, but – like many other perfectly rational notions – it doesn't seem to be particularly suited to today's wacky world of equities. On a wide range of typically market-sensitive topics from inflation to interest rates and pandemic trends, investors seem inclined to ignore both the rumor and the news, assuming that whatever happens, the Fed will be there to backstop any fallout. The moral hazard generated by eleven years of unconventional central bank interventions would seem fully baked into assumptions and expectations. Why pay attention to details if there's only one direction the market can go?

Taper, Schmaper

The Fed meets next week for the last 2021 meeting of the Federal Open Market Committee. Observers expect that the FOMC will formally announce a decision to accelerate the pace of tapering its bond-buying program, with the monthly bond purchases likely wind down to zero by March or so of next year. There is also likely to be some tougher talk around inflation, with the Consumer Price Index today posting its highest level in 40 years. Fed Chair Powell gave a preview of this during a Congressional testimony session last week with a hawkish bent, sounding very different from the man who airily dismissed any talk of inflation being anything more than a passing flight of fancy for much of this year.

Expectations of stickier inflation have already brought forward the calendar many investors have in their heads for interest rate increases, with the consensus now being for at least two hikes sometime in the second half of 2022. The rumor – to go back to that old Wall Street adage – has gained enough traction to become conventional wisdom. Each piece of actual news, such as today's CPI release, would seem to confirm the rumor. Yet neither rumor nor news seem to move the sentiment needle much one way or the other. Will the new omicron variant of Covid make an already dicey inflation scenario even worse? Who cares – while medical experts claim they still know very little about this new variant with all its perplexingly advanced mutations, Mr. Market has already decided that omicron (which Mr. Market can neither spell nor pronounce) is of no consequence.

Too Big To Fail

With many seasoned money professionals calling today's environment even more frothy and speculative than 1999 or 1929, it would seem that investors' faith that it will always remain ever thus might be misplaced. Or is it? When central banks started their unconventional monetary experiments in the aftermath of the 2008 financial crisis, part of their aim was to encourage liquid conditions in credit markets that would in turn stimulate economic growth. The practical effect of their efforts was to push traditional safe-asset investors like insurance companies and pension funds further out the risk horizon into lower-grade fixed income and equity markets. This environment is now in its second decade. Every time financial markets have seized up, for whatever reason, central banks have responded by turning on the liquidity taps. In late 2018, when the Fed made clear that it really did intend to stick with its program of raising

rates back to something approximating historical norms, the stock market pulled back sharply and ultimately forced the Fed to pivot.

Small wonder, then, that few people seem to think that anything will be different this time. Small wonder that periodic pullbacks, which are part of any growth market cycle, have gotten successively shallower and briefer. The Fed, it would seem, is a prisoner of its own design. If it were to just let markets be markets, no matter the consequences, then all those pension funds and insurance companies would be at risk – an unacceptable pain point for the economy. By this rationale the S&P 500 is simply too big to fail.

But there wasn't any inflation to speak of in 2018, and there was not much in the way of a real-world impact when the Fed did its legendary pivot in January 2019. That might not be the case this time. Ignoring the news, with the assumption that this best-of-all-possible market worlds will live forever, may not be the best way to think about the year to come.

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