Regency Financial Group

INVESTMENT & FINANCIAL SERVICES

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RFGMoneyMatters

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"Nothing in life is to be feared, it is only to be understood. Now is the time to understand more,

so that we may fear less." ... Marie Curie

…the WORD.

The November edition of RFGMoneyMatters was published shortly after the election on November 3. At that time, the prolonged ballot counting continued in the midst of the pandemic. As a result, several key races remained undetermined for days. Based on what I knew on November 6, I published my anticipated election outcome:

1. White House control by Democrats;
2. G.O.P. control of the Senate by a 52-48 or 51-49 margin, depending on the outcome of the Georgia runoff election on January 5; and
3. House control by Democrats.

I also observed that this set of outcomes would provide the basis for Washington political gridlock, which has been preferred by investors.

While most investors look forward to the day when elections are not part of the investment equation, I am not quite there yet. The two Senate seats in the Georgia runoff on January 5 will determine control of the Senate for the next two years. While a Democrat sweep of the two races would throw Senate leadership into Democrat hands and open the door to potential tax code changes, I take the view that the probabilities favor at least one of the two seats remaining in G.O.P. hands. This would keep Senate control in the G.O.P. for at least two years. From an investor perspective, this would most likely keep the top corporate income tax rate at 21%, which most investors prefer. I expect the Georgia runoff election to be a textbook base turnout election, and since anything is possible, investors will be following this closely.

In Georgia, given the fact that Senator Perdue was not quite able to reach the 50% threshold for winning in the general election (he received 49.7% vs. 47.9% for Ossoff), and given the fact that Senator Loeffler has her Senate seat as a result of appointment by the Governor, these runoffs are expected to be close elections. I view all outcomes as possible in Georgia and recommend that investors have their asset allocations at the level that matches their personal risk tolerance, given the potential for short-term volatility if a change in Senate leadership occurs. At the same time, even if a change occurs, West Virginia Senator Manchin (D), who describes himself as a “moderate conservative,” says he is not an automatic vote for Senate Democrats. In his Fox interview on November 9, he stated, "If one senator does not vote on the Democratic side, there is no tie and there is no bill." Manchin then added, "I will not vote to end the filibuster." He then went on to say he is "not for all the crazy stuff.”

It is worth noting that history favors the G.O.P. in Georgia runoff elections. In two previous Senate runoffs in Georgia, in 1992 and 2008, the G.O.P. Senate candidate emerged victorious. The 1992 victory margin was 1.3%, while the 2008 margin was 14.9%. Both were low turnout elections at 44% and 43%, respectively, and since Georgia is now the center of the political world, turnout for this runoff could be higher. It is also fair to say that the electorate in the Peach State has undergone considerable change since the most recent Senate runoff election in 2008.

In order for investors to place the 2020 pandemic in the rear-view mirror, vaccine discovery remains the priority. The development of safe and effective vaccines that provide immunity from COVID-19 has been the focus of the pharma and biotech sectors since March. I have discussed several leading vaccine programs in RFGMoneyMatters, and I now have three research efforts that have emerged as the leaders in the vaccine race. The firms involved are Pfizer, in partnership with BioNTech, Moderna Pharmaceuticals, and AstraZeneca, in partnership with the University of Oxford.

The Pfizer vaccine partnership with BioNTech announced successful data from their Phase 3 clinical trial on November 19. The firms stated that their COVID-19 vaccine has an overall effectiveness of 95% and is safe with no serious side effects. This vaccine is based on a novel technology known as messenger RNA (mRNA). This methodology uses a synthetic version of coronavirus genetic material to program cells to make copies of a virus fragment, which then serve as a catalyst within the immune system to attack the virus if COVID-19 exposure occurs. The vaccine requires cold-chain storage at -94F or below. This creates challenges since the vast majority of hospitals lack the facilities to store vaccines at such ultra-low temperatures.

Pfizer and BioNTech submitted the new vaccine to the FDA on November 20. They have also initiated rolling submissions across the globe, including Australia, Canada, Europe, and Japan. The vaccine requires two doses, separated by three to four weeks. The efficacy of the vaccine has been consistent across age, race, and ethnicity in the Phase 3 trial, which involved close to 44,000 volunteers. In a remarkable development, the vaccine appears to be 94% effective in older adults. Pfizer indicated that further study is required to determine the duration of immunity.

Based on current projections, the companies expect to produce globally up to 50 million doses in 2020 and up to 1.3 billion doses by the end of 2021. The United States allocation of total doses is 50% and the companies will be ready to distribute the vaccine within hours of authorization, hopefully by mid-December. The vaccine could be available to the general population by the second quarter of 2021.

In mid-November, Moderna Pharmaceuticals announced an analysis of its Phase 3 clinical trial results for its mRNA COVID-19 vaccine candidate. The initial results were very promising as the placebo group contracted 90 of the 95 total cases, including all 11 severe cases. The vaccine had a 95% effective rate for the prevention of COVID-19. These highly significant results were analyzed by an independent data safety monitoring board.

Moderna has requested emergency use authorization from the FDA, and the agency has scheduled an advisory meeting from December 8th to the 10th. This vaccine is likely to be authorized shortly thereafter. Upon approval, immunizations could be administered to health-care workers, first responders, and high-risk individuals. A major positive for the Moderna vaccine is the ease of storage. Unlike the Pfizer vaccine, the Moderna vaccine has a longer shelf-life under refrigeration and at room temperature and does not require cold-chain storage at -94F. The Moderna vaccine can be stored and transported at -4F and should be widely available by spring.

AstraZeneca and the University of Oxford announced on November 23 that their COVID-19 vaccine appears effective. The vaccine is inexpensive and easy-to-produce, and early analysis of Phase 3 trial data found the vaccine up to 90% effective. The initial Phase 3 trial involved less than 2800 subjects, therefore a broad trial of 60,000 subjects in four countries will continue through December. Meanwhile, Phase 3 clinical trials continue on the one-dose Johnson & Johnson COVID-19 vaccine. The approval of multiple vaccines would greatly improve the ability to immunize a large percentage of the population to defeat the coronavirus.

Builder confidence increased to another record level in November as the NAHB housing market index (HMI) jumped five points to 90, breaking the previous high of 85 in October. The NAHB Chairman stated that "historically low rates, favorable demographics, and an ongoing suburban shift for home buyer preferences have spurred demand." Housing remains a stellar bright spot for the economy and the entire industry is largely domestic. HMI readings above 50 indicate positive single-family home builder confidence and the current record readings bode well for the sector into 2021.

All of the HMI components registered record highs in November. The index that measures current sales conditions jumped six points to 96, the component measuring sales expectations over the next six months rose one point to 89, and the gauge charting traffic of prospective buyers rose three points to 77. On a regional basis, the Northeast gained two points to 83, the Midwest jumped six points to 80, the South rose four points to 86, and the West gained four points to 94. I expect the housing sector to remain an integral part of the 2021-2022 economic recovery, bolstered by low rates, strong demand, and tight supply.

Housing starts exceeded expectations in October to a 1.53 million-unit annual rate. The year-over-year gain in starts now stands at 14%. The October increase was driven by a 6.4% gain in single-family starts to a 1.18 million-unit annual rate, the highest since April 2007. Single-family starts have risen for six straight months as home buyers continue to shift from large metro areas in the Northeast and West Coast. Single-family permits edged higher by 0.6% to a 1.12 million-unit annual rate.

The Conference Board Leading Economic Index (LEI) increased by 0.7% in October. This was the sixth straight increase for the LEI and followed gains of 0.7% in September and 1.6% in August. The pace of expansion has moderated following the surge that developed after the initial lockdown during spring. Seven of the ten LEI components made positive contributions, led by new orders and initial jobless claims. On a year-over-year basis, the LEI is down 2.9%.

The economy has displayed a high level of resilience during the worst pandemic in a century. Given the resurgence of COVID-19 during the late autumn and winter seasons, it would make sense for Congress to pass additional stimulus/relief measures to help bridge the next few months until widespread immunization can get underway. Until the deployment of vaccines reaches critical mass, the economy will be challenged by the lack of mobility and engagement throughout the consumer and business community.

The Coincident Economic Index, which measures current economic activity, gained 0.5% in October as it registered its sixth consecutive advance. This index remains 4.6% below its February peak. The development of COVID-19 vaccines remains the most critical influence on the improving economic outlook in 2021 and 2022.

I expect real GDP growth in 2021 to reach the 3% to 4% range. Pent-up demand and the gradual expansion of vaccine immunization should support above-average expansion. I estimate 2021 S&P 500 operating earnings of at least $165, expanding to at least $180 in 2022. In a low-interest rate economy, a price/earnings ratio of 21 times earnings provides the potential for the S&P 500 Index to trade into the 3800s range.

I expect investors to remain focused on the corporate earnings recovery into 2022. Interest rates should stay low indefinitely with Fed accommodation, and COVID-19 vaccines should pave the way to economic normalcy by 2022. While opposition from the seasonal deficit hawks and partisan wrangling hamper stimulus/relief talks, a package in the area of $1 trillion is possible in the first quarter. For those adding to holdings, I recommend a dollar-cost-average approach.

The Federal Open Market Committee (FOMC) reconvenes on December 15 and 16 to review monetary policy. The FOMC has made it clear that their plan to hold short-term interest rates close to zero will remain on track until 2023 to support the economy. The current real year-over-year growth rate of the narrowly defined M-1 monetary aggregate of 41% is historic and unprecedented. The broadly defined M-2 aggregate also shows the rapid growth of 23% year-over-year, adjusted for inflation. Although the FOMC favors the passage of additional fiscal stimulus/relief in Congress, such efforts have been held hostage by partisanship in the Senate.

Always be vigilant about your investments and markets.

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Past performance does not guarantee future results. The value of your investment may stay unchanged, increase, decrease, or result in a total loss of your investment.

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