
HedgeFolios Strategy Advisory

“The Big Game-Changer for 2021”

1-11-2021

Our Current View:

For many weeks, we had written in in our short-term trading services and in many issues of our [*Wellington Letter*](#) that political turmoil awaited the markets in January. Investors and traders piled into the markets over the past several days to price in the impact of the chaos in Washington D.C. and the now Democratic-majority Senate.

President Donald Trump, just after Congress certified Democrat Joe Biden’s Electoral College Victory, pledged “an orderly transition.” In a statement released by the White House, he said:

Even though I totally disagree with the outcome of the election, and the facts bear me out, nevertheless there will be an orderly transition on January 20th.

That’s it folks! Biden is your next president until he is dumped onto the trash pile of politicians who have outlived their usefulness.

The markets have interpreted this as more bullish than anything before. Buyers rushed into stocks, sending all the major indices to new all-time highs late last week, while government bond yields continued to extend their run higher on the day following Biden’s confirmation (January 7th).

By the close on Friday (1/8/2021), the Dow, S&P 500, NASDAQ Composite, Russell 2000, NYSE Composite, and most importantly, the VALUG, had all reached new all-time highs on both an intraday and closing basis. The VALUG’s advance helped it to finally overcome the high it achieved in mid-2018. We show this on the weekly chart for the index below:



In this environment, bad news is good news for the markets. The “Blue Wave” trade playing out is based on expectations for incredibly strong fiscal stimulus. The more the economy struggles in the coming months, the greater the government’s stimulus will be.

We saw this play out on Friday after the Bureau of Labor Statistics reported the worst U.S. jobs report since April 2020. In total, 140,000 jobs were lost in the month of December, ending a 7-month long winning streak and confirming that the economic recovery is stalling.

Yet, the markets showed no signs of slowing down. The S&P 500, Dow, and NASDAQ climbed to another new set of all-time highs on 1/8/2021, despite the abysmal jobs report. This confirms our thesis that the markets are now totally driven by stimulus hopes, which are now much more intense than they were last year.

In the past, when our work called for it, we frequently pinpointed “the big game changers” for the market, often to the same day or week. We now have another one.

For investors and money managers, this could be Nirvana. Now, portfolios have to be readjusted for the new reality: **trillions of dollars of new spending financed by new money creation. That money has to go somewhere.**

The long-term negatives, of course, are the diminishing U.S. influence in the world, our politicians becoming tools of communist regimes, the destruction of our value system, much higher taxes, lots of free “stuff” to convince the masses that everything is great, schools that brainwash, censorship of anyone with different views, and social media firms becoming official tools of the socialists, among others.

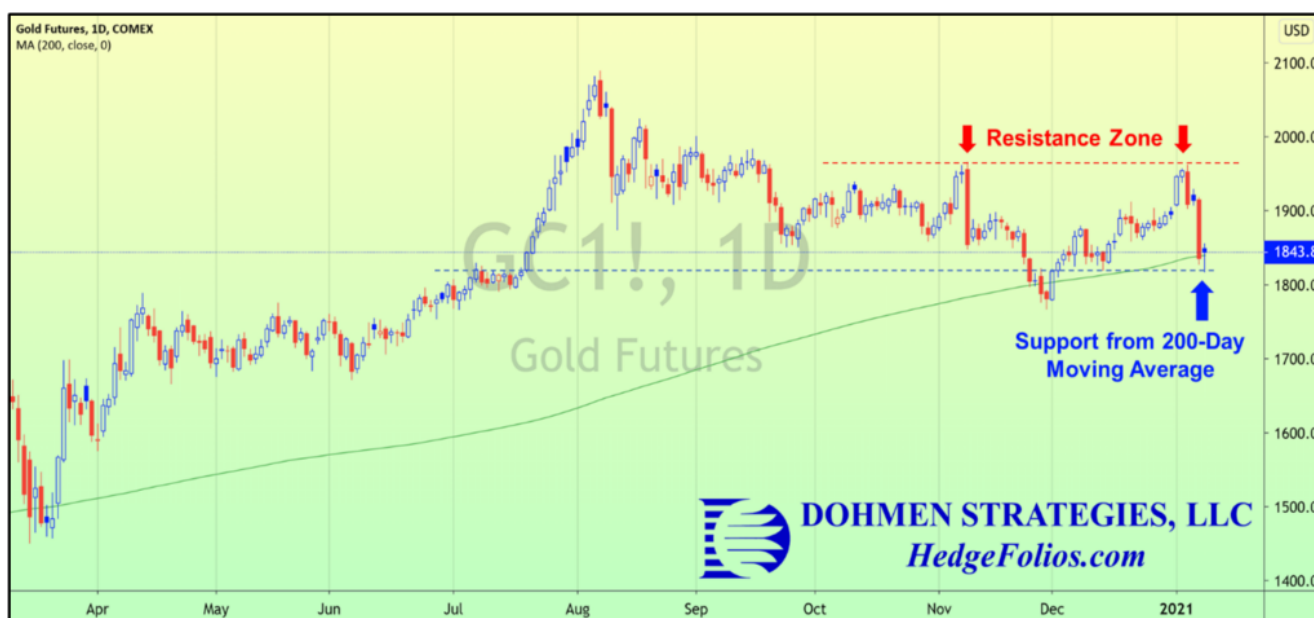
We have an unthinkable \$19 *trillion* of stimulus from the world’s central banks. This liquidity has to go someplace, especially as the economic activity is not absorbing it. That creates great opportunities for prices of assets. The adverse consequences will likely come 18-36 months from now.

This could fuel incredible speculation. For that reason, assets that may have appeared too risky in the past may now be viable investment opportunities.

One development that emerged on Friday was a sharp turnaround in gold and silver bullion prices. This is a counter-trend move and goes in the opposite direction of what the fundamentals suggest. With higher stimulus on the horizon, inflationary pressures and uncertainty will build, driving up gold and silver demand.

The downturn in the precious metals we saw over the past few days was more likely prompted by investors moving into higher-risk inflation hedging vehicles, including commodity stocks and cryptocurrencies, now that the risk of such assets plunging is significantly lower. This shouldn't impact the higher demand for gold, which should still be the inflation hedge of choice for less speculative investors.

Gold prices have also rallied off support since their decline on Friday. We show the latest price action on the daily chart for gold futures below:



In today's trading, we saw prices rally off lows near support (dashed blue line) and close above the 200-day moving average (green line). If the decline goes any further, stronger support is nearby at the recent November low. The sudden move from risk-off into risk-on assets may have jolted gold investors, but we nonetheless remain bullish on the sector.

As we discussed previously, however, in the new stimulative environment we're in, with trillions of new dollars in stimulus likely to come in over the course of 2021, it will be important to participate in other sectors besides gold and silver.

Our HedgeFolios:

Our latest update to our HedgeFolios (1/8/2021) will help us capitalize on a continued rise, driven

primarily by stimulus and speculation. With Democrats in control of both houses of Congress, the outlook has improved significantly for companies offering solutions in clean energy. Thus, we gained some exposure to ETFs like PBW, PBD, and TAN within our models.

Mega-cap tech stocks may face additional antitrust scrutiny under a Democratic administration, but the growth-favoring impact of high stimulus will keep the tech sector attractive. We re-entered small positions in a few of ARK's disruptive innovation ETFs, as well as the "next generation" NASDAQ ETF, QQQJ.

For better or for worse, the incoming administration will likely be more amicable towards China, making the prospects of their stock securities more attractive. We've added a small position in the ASHR ETF to our Global Equity portfolio to gain exposure.

With a potentially hyper-bullish environment ahead of us, places that will likely underperform are the classically defensive areas like Utilities and Real Estate. We have therefore exited our positions in these sectors across all our HedgeFolios.

We are holding onto our positions in the mining sector, namely GDX and SIL, to provide diversification and to hedge against the inflationary impact of all the incoming stimulus. We still have a good amount of cash on hand, which we may distribute across our current bullish positions once we have further confirmation of the up-move.

Our Conclusion:

In the wake of recent events, the outlook for 2021 has shifted. This year may have some of the best opportunities for active investors who are smart, knowledgeable, and have experienced, professional guidance. The current environment is very similar to the one of the late 1970s, except now the creation of money will be larger by many magnitudes.

Of course, this cannot last forever. Easy money and government spending cannot be used as a substitute for genuine economic growth forever. But it may be a long time before the negative consequences are realized. A possible trigger may be a rise in prices, which would be a big shock to the U.S. economy, where inflation has been dormant for almost 40 years.

We will, of course, watch closely and anticipate such developments before they begin to take hold in the markets. In the meantime, however, you can be sure champagne corks are popping on Wall Street, and it would be foolish not to participate.

Wishing you successful investing,

Bert Dohmen and team