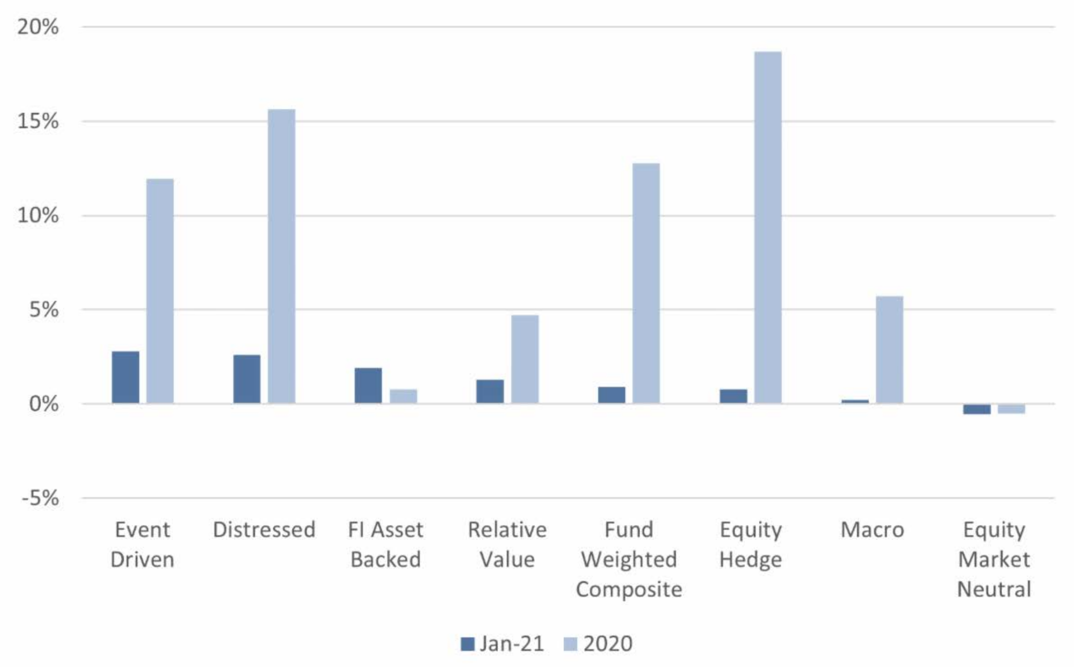
View as Webpage

Market Comment:

Retail v. Wall Street, and other false narratives

Fig. 1: Hedge fund performance, 2020 and January 2021



Source: Bloomberg, Mill Creek. Performance is based on HFRX Hedge Fund Indices.

There have been many narratives put forward about the meme stock short squeeze (e.g. GME, AMC, etc) that occurred in January. One of the worst "hot takes" was that the event signified some sort of battle between retail investors and Wall Street or retail investors and hedge funds. When the dust settles it will be clear that there were institutional investors (mainly hedge funds) on both sides of the meme stock trade. Some profited, others experienced losses, but such is the nature of trading and speculation.

More importantly, the meme stock short squeeze was not a meaningful business event for most of Wall Street. It wasn't even a meaningful event for most hedge funds. The hedge fund universe is comprised of hundreds — if not thousands — of unique strategies. Some hedge funds are focused on stock selection in equity markets, but others trade around corporate events like mergers, deal in distressed debt, or make discretionary global macro trades. Outside of a shared legal structure (most US hedge funds are set up as limited partnerships and are regulated by the SEC and CFTC[1]), individual hedge funds are usually more different than they are alike.

While a few hedge funds found themselves on the wrong side of a short squeeze in January, the impact on a well-diversified hedge fund portfolio was negligible (Fig. 1). Equity hedge strategies, which includes managers that would have been directionally involved in the meme stock trade, returned +0.8% in January[2]. Several other strategies, including event driven, distressed, and FI asset backed also performed quite well. Overall, the HFRI Fund Weighted Composite Index was up 0.92% last month.

We consider ourselves investors, not speculators, at Mill Creek. At the same time, our belief that our clients, when they are able, should allocate a portion of their investible assets to hedge funds means we are allowing traders — speculators — into their portfolios. The events of the last few weeks have not changed our view regarding the value of doing so. Instead, they have revalidated the prudency of our multi-manager, multi-strategy approach for implementation.

[1] Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC)
[2] The average monthly fluctuation for equity hedge managers since 2000 has been 1.5%, making January's results entirely unremarkable.

Updated Benchmark Performance:

Benchmark Performance by Asset Class	Week-to-Date	Month-to-Date	Year-to-Date
U.S. Large Cap Equities	4.92%	4.92%	4.06%
U.S. Small Cap Equities	7.72%	7.72%	13.14%
International Developed Equities	2.75%	2.75%	1.66%
Emerging Markets Equities	4.96%	4.96%	8.18%
Global Equities	4.32%	4.32%	3.84%
U.S. Bonds	-0.39%	-0.39%	-1.11%
Intermediate Municipal Bonds	0.06%	0.06%	0.44%
High Yield Bonds	0.70%	0.70%	1.04%
Oil	7.79%	7.79%	14.59%
Gold	-2.01%	-2.01%	-4.53%
Key Rates	**2/5/2021**	**12/31/2020**	**2/5/2020**
U.S. 2 Year Treasury Note	0.09	0.13	1.44
U.S. 10 Year Treasury Note	1.19	0.93	1.66

Week in Review:

The January jobs report in the US showed some weakness in the labor market, but the economy did create jobs in the month following a decline in December.

- Total nonfarm payrolls increased by 49,000 jobs in January. December payrolls, initially estimated at 140,000 jobs lost, were revised to 227,000 losses.
- The unemployment rate dropped from 6.7% in December to 6.3% in January – largely due to a decline in the labor force participation rate. Labor force participation stood at 61.5% in December, down from 63.3% before the pandemic struck.
- In a sign that layoffs are beginning to ease, weekly first-time unemployment claims fell for a third straight week to 779,000. However, the number remains above the pre-pandemic peak of 695,000.

Following a meeting of the Federal Reserve, the Central Bank has decided to keep interest rates and asset purchases unchanged. The benchmark interest rate will remain near zero and the Fed will continue purchasing $120 billion of bonds each month. "The economy is a long way from our monetary policy and inflation goals, and it's likely to take some time for substantial further progress to be achieved," Fed Chairman Jerome Powell said. In a post-meeting note, the Federal Open Market Committee added that economic growth had moderated and that the future path for the economy depended on the progression of the virus, and more specifically, the progress on vaccinations.

Economic Calendar:

- Consumer Price Index – Wednesday, February 10th
- Weekly Unemployment Claims – Thursday, February 11th

This week's contributors: Michael Crook, CAIA and Dusko Jankovic, CFA, CAIA

Indices Used: U.S. Large Cap equities: Russell 1000 Index, U.S. Small Cap Equities: Russell 2000 Index, International Developed Equities: MSCI EAFE Index, Emerging Market Equities: MSCI Emerging Markets Index, U.S. Bonds: Barclays Aggregate Bond Index, U.S. 10 Year Treasury Note: Bloomberg 10 Yr. Treasury Note, Municipal Bonds: Barclays Intermediate Municipal Bond Total Return Index, High Yield Bonds: Barclays U.S. High Yield Total Return Index, Oil: Bloomberg WTI Crude Sub-Index Total Return Index, Gold: Bloomberg Gold Sub-Index Total Return Index