The Type 2 Investor

June 10, 2021

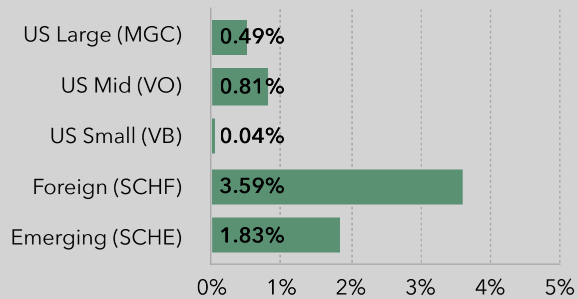
May 2021

Economic Data

- The number of US workers on payroll rose 559,000 in May, with most of that coming from bartenders and waitstaff
- Retail sales were flat for the month of April, following a 10.7% rise the previous month
- Y/y inflation (CPI) came in hotter than expected at 4.2% in April—the highest since 2008—with Energy and Used Car prices exploding
- Existing home sales fell 2.7% in April, the third decline in a row, with a record high median home price of $341,600

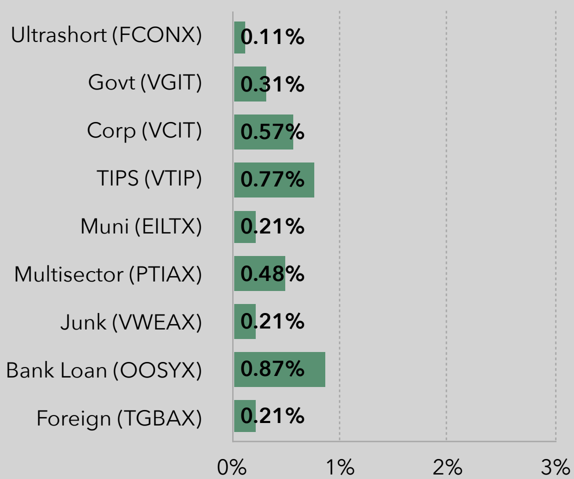
Stocks

May Returns



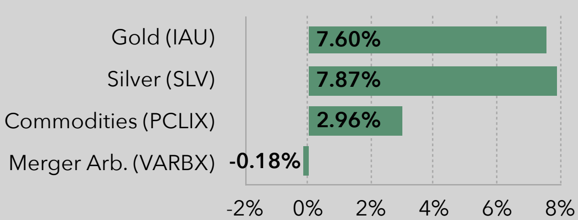
Bonds

May Returns



Alternatives

May Returns

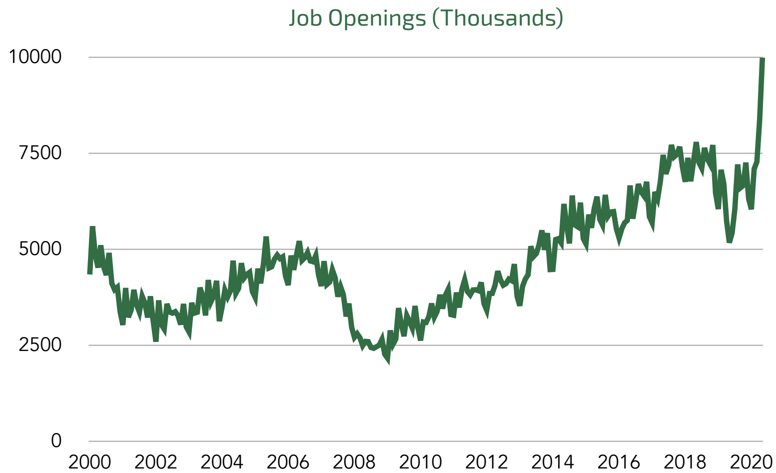


Performance data provided by Morningstar.

The brain uses two systems to process information. The first type is intuitive but lazy, rapidly forming judgements with no conscious input. The second system is slow, reflective, and is not guided by emotions. It is that second system — type 2 — that we want in control of our investment portfolios.

Work or Free Money?

In May of last year I mused that when the economy did start to open up many would find the enhanced unemployment benefits—as much as $74k per year in Massachusetts—exceeded what they would earn going back to their menial jobs. So instead they would decide not to return until the benefits ran out, which is basically what is happening now. And I don't blame them. If you're getting paid relatively the same amount or even more to stay at home, that's the rational thing to do. And that's why we have the highest number of job openings since the government started tracking the data back in 2000.



Source: U.S. Bureau of Labor Statistics

There are over 15 million Americans on the dole right now, with over 11 million of those on some sort of pandemic-specific unemployment benefits. The labor force participation rate—the percentage of the working-age population that is working or looking for work— is only 61.6%; almost two percentage points below its pre-pandemic level. About 7.4 million fewer people are working today than at the beginning of last year, yet companies are desperate to find employees. President Biden extended the enhanced benefits to September 6, but 23 states have since opted to cut those benefits this month to encourage people to get back to work.

On top of that, the tight labor market is emboldening many to seek out greener pastures. The rate of people quitting their jobs rose to 2.8% in April, according to the U.S. Bureau of Labor Statistics. That's the highest quit rate for that month since they started tracking the data back in 2000, and just one-tenth shy of the record high for any month. If you take out government employees—who seemingly never quit regardless of the job market—the number rises to 3.2%. In fact, the number or people quitting their jobs in the private sector was almost double that of a year ago.

With almost half the states cutting benefits this month, one more next month, and the rest in just three months, this will likely be short-lived. In the meantime, it does create some bargaining power for those looking to jump ship or get off the couch. Those who wait too long may find the job environment not as target-rich by the end of the year.

"Transitory" Inflation

We talked about inflation a little bit last month, and how there was seemingly a disconnect between rapidly rising raw materials prices and home prices and what we were actually seeing in the CPI report and what the Fed was telling us. CPI is deliberately designed to underreport true inflation, but that's a topic for another time. Anyway, the next day the latest CPI report came out and it was a big one, with year-over-year inflation jumping to 4.2% on dramatically higher energy and used car prices. This morning, the May CPI report showed year-over-year inflation heating up further to 5.0%. That's red hot at a time when you're lucky to get 0.50% interest on your deposits.

Rising inflation is tied to many factors, including increased demand, supply-chain disruptions, and shortages of labor and materials. Generally, equities act as a good hedge against inflation. However, this relationship tends to break down and can even turn negative when inflation gets too high. There is not a hard rule, but 4% is often cited as the line. If inflation is in fact "transitory" as the Fed would have us believe, this won't be an issue. If, however, we see a sustained period of inflation above 4%—which I think is a real possibility—equities might have more mixed results.

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Tactical Asset Allocation

Asset Class	Heavy Under-weight	Under-weight	Neutral	Over-weight	Heavy Over-weight
Fixed Income		●			
Duration	●				
Inflation				●	
Credit	●				
Foreign				●	
Equities		●			
Large Cap	●				
Mid Cap		●			
Small Cap	●				
Developed Intl.		●			
Emerging			●		
Alternatives					●
Commodities					●
Hedging					●

Binge Box

Mighty Ducks: Game Changers (Disney+)

Mighty Ducks: Game Changers reunites Gordon Bombay (Emelio Estevez) with his one true love…single hockey moms. Er, I mean coaching peewee hockey. Admittedly, Estevez's acting seems a bit more rigid and uninspired than I remember from the original films. Also, Dylan Playfair, who is comedically brilliant in *Letterkenny*, puts on a performance so bad it would get him cut from a middle school play. So why am I recommending it. Because I loved the Mighty Ducks trilogy growing up and the show gives the fans what they want: a formulaic and highly unrealistic underdog story, plus an episode of callbacks. Stream the whole season on Disney+.

About EmeraldSpark

EmeraldSpark Investments, LLC is a Registered Investment Adviser based in Chicago, IL. We were founded by Ryan P. Layton, CFA in 2015 to provide personalized financial planning and fiduciary investment management services to select clients. Our investment process blends the foundations of Modern Portfolio Theory with the latest research in the field of behavioral finance. We specialize in asset allocation and investment due diligence to help provide our clients with investment strategies personalized to match their specific goals and risk comfort zone.