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# Important changes in stock sector leadership—masked by an overall dip

By Brian Cayon
Chief Investment Officer
Waukesha State Bank Wealth Management

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The overall slide in stock prices—as investors grapple with the implications of a rising-rate environment—is masking a continuation of the significant rotation going on in the various stock sectors.

We all know that this past decade has been dominated by growth—tech and the FAANG stocks, in particular. Well thus far in 2021, energy and financials have led the charge. As you'll see in the table below, they're leading by a pretty wide margin. And in the second half of February, there was a decided move away from tech and healthcare and into the more cyclically sensitive stock sectors.

**Year to date performance: S&P 500 Index & specific sectors**

| | **YTD** | **Rel. to S&P 500** |
|---|---|---|
| S&P 500 | 1.7% | |
| Energy (XLE) | 27.0% | **25.3%** |
| Financials (XLF) | 9.6% | **7.9%** |
| Communication Services (XLC) | 6.1% | **4.3%** |
| Industrials (XLI) | 2.3% | **0.6%** |
| Real Estate (XLRE) | 2.1% | **0.4%** |
| Basic Materials (XLB) | 1.6% | **-0.1%** |
| Technology (XLK) | 0.5% | **-1.2%** |
| Discretionary (XLY) | 0.2% | **-1.5%** |
| Health Care (XLV) | -0.7% | **-2.5%** |
| Staples (XLP) | -6.2% | **-7.9%** |
| Utilities (XLU) | -6.9% | **-8.6%** |

*Source: yCharts; sectors as measured by the iShares Sector SPDR ETFs; as of February 26, 2021.*

Because of their market leadership and huge weightings in the various indices, technology and healthcare stocks' weakness seems to have brought out a chorus of "top callers," many of whom argue that valuations have reached extreme levels.

In our view, the overall market is NOT extremely overvalued despite some areas showing a bit of froth. Don't get me wrong, there is some crazy investor behavior going on in the likes of Tesla, Bitcoin, Gamestop, pot stocks, etc. But we would argue that, in general, investor sentiment is far from "euphoric."

Though recent American Association of Individual Investor surveys show that sentiment has turned more bullish of late, there is still over $4 trillion in cash on the sidelines, and far more money has been flowing into bond mutual funds than stock mutual funds.

Cyclical stocks are clearly being bought, so if there is any kind of meaningful correction, it would likely be limited to some of the growth and big-tech names, much like we experienced when the dot-com bubble burst. Those of you that were investors then will remember that it was a complete tech-wreck. But do you also remember that financials, energy, industrials and materials all did quite well while tech was rolling over?

Even if we are seeing a top for growth stocks in the short-term, they're certainly not going away. And that wouldn't necessarily spell doom for the entire stock market—the fundamentals are still in place for a robust economic re-opening, and that should bode well for most stocks.

Though there's currently an elevated level of fear among investors, Fed Chairman Powell is likely to continue to ooze dovishness, thus alleviating the fears of a taper tantrum and the potential for runaway inflation.

While both the stock and bond markets may be nervous about interest rates, equity investors should note that that Fed prefers flat to rising asset prices, which is generally supportive of stocks.

Thus, it is wise to remember the adage "Don't fight the Fed."

*Brian Cayon is vice president – chief investment officer for Waukesha State Bank Wealth Management. He leads the investment services platform that includes directing investment and financial planning strategy and policies, asset allocation, and portfolio positioning.*