

ECONOMY

A 5th Element
of Concern

THINK STRATEGICALLY:



Quintuple Witching Explained

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Quadruple witching is an occurrence on certain dates in which stock options, stock index options, stock index futures and single stock futures all expire at the same time. Typically, stock options contracts and index options expire on the third Friday of every month; however, quadruple witching happens when all four asset classes expire simultaneously on the third Friday of every March, June, September and December.

Quadruple witching on its own did not cause the damage that the markets experienced last Friday. Global stock markets were experiencing significant stock rotations since the Federal Reserve confirmed its position on interest rates, tapering and inflation. The Fed admitted that inflation was no longer temporary; it would change the monetary policy to reduce inflation during the coming quarters to 2 percent. Additionally, the central bank presented projections that there will be no less than three interest rate increases in 2022. For this specific reason, we have named it Quintuple Witching, given that the new monetary policy adds an element of concern for investors.

As we discussed last week, the Fed outlined the changes to its monetary policy as follows:

– **Doubles Down on Tapering:** The Fed will increase the pace to wind down its

bond purchases. It recognizes the rapid increases in the consumer price index that have hampered growth over the last seven months.

– **2022 Monetary Policy:** The Federal Open Market Committee conveyed a more hawkish tone, as it predicted no less than three rate increases during 2022. We are pretty surprised that the market did not react more, given it has become dependent on extraordinarily accommodative monetary policy.

– **Revised Economic Projections:** The revised Fed projection follows.

Variables	2022	2023
Gross Domestic Product	3.6%-4.5%	2.0%-2.5%
Unemployment	3.4%-3.7%	3.2%-3.6%
PCE Inflation	2.2%-3.0%	2.1%-2.5%
Core PCE Inflation	2.5%-3.0%	2.1%-2.4%
Federal Funds Rate	0.6%-0.9%	1.4%-1.9%

When the new Fed policy goes into effect, there will be market behavior changes. So the best advice is to maintain a well-diversified portfolio with the proper balance of stocks, bonds and other instruments that meet your financial goals and criteria is the best protection from any market swings.

Week in Markets: Teutonic shift in Fed policy impacts global markets.

All last week, investors were on a holding pattern awaiting the determinations of the Federal Reserve Bank and other central banks. All policy announcements made by the Fed were widely expected. In my view, the only real surprise was the outlook for three rate increases in 2022.

Even with a global economic recovery full of pandemic-related obstacles, economic and job growth progress has been robust. Inflation has risen the most in nearly 40 years, with most of the Producer Price Index program increases due lower supply levels and excess demand. Meanwhile, energy has risen close to 58 percent since last year, materially impacting everyone.

Before raising rates, the Fed typically has a 2 percent target rate for inflation. Because of the pandemic and the global supply chain disruptions, the Fed

concluded that inflation was temporary, so it did not prevent a derailment of the economic recovery. However, the Fed has pivoted as pandemic relief funding is no longer needed, and it must work to deter inflation.

While the Fed implements its new monetary policy, we think the stock market will continue to grow amid sector rotation, and volatility will continue impacting the markets.

As a comparison, during the previous interest rate increase cycle in December 2015, the Vix Index, which measures volatility, rose above 20 percent.

Also, the interest rate cycle change does not mean that the market will fall into correction mode; while it could happen, we do not envision it occurring just yet.

With interest rate increases taking center stage, what becomes a real threat is the later stages of the interest rate cycle that are prone to impacting economic growth and stock market valuations.

We predict that the bull market will continue during the first half of 2022 and even much longer, all depending on the speed of the interest rate increases combined with the GDP numbers, labor force growth and the solution of the global supply chain disruptions.

Wall Street Weekly Review, Dec. 17

– The Dow Jones Industrial Average closed at 35,365.44, up 605.55 points, or 1.68 percent, for a year-to-date (YTD) return of 15.55 percent.

– The Standard & Poor's 500 closed at 4,620.64, down 91.45 points, or 1.94 percent, for a YTD return of 23.02 percent.

– The Nasdaq Composite Index closed at 15,169.68, down 460.92 points, or 2.95 percent, for a YTD return of 17.7 percent.

– The Birling Capital Puerto Rico Stock Index closed at 2,920.45, down 22.49 points, or 0.76 percent, for a YTD return of 42.81 percent.

– The U.S. Treasury 10-year note closed at 1.41 percent.

– The U.S. Treasury 2-year note closed at 0.66 percent.

Weekly Market Close Comparison	12/17/21	12/10/21	Return	YTD
Dow Jones Industrial Average	35,365.44	35,970.99	-1.68%	15.55%
Standard & Poor's 500	4,620.64	4,712.09	-1.94%	23.02%
Nasdaq Composite	15,169.68	15,630.60	-2.95%	17.70%
Birling Puerto Rico Stock Index	2,920.45	2,942.94	-0.76%	42.81%
U.S. Treasury 10-Year Note	1.41%	1.48%	-4.73%	0.45%
U.S. Treasury 2-Year Note	0.66%	0.67%	-1.49%	0.60%

Final Word: PRSI Outpaces Major Indices

When comparing the Birling Capital Puerto Rico Stock Index's (PRSI) performance from Jan. 1 to Dec. 17 against the Dow, S&P and Nasdaq, the former's results blew the key indices out of the water.

Companies' returns and prices per share:

– **Triple S Management (GTS):** Its 66.14 percent return exceeds the Birling PRSI, the Dow, S&P and Nasdaq, with a closing price of \$35.66.

– **First Bancorp. (FBP):** Its 42.62 percent return exceeds the Dow, S&P and Nasdaq, and is just below the Birling PRSI, with a closing price of \$13.15.

– **OFG Bancorp (OFG):** Its 36.52 percent return exceeds the Dow, S&P and Nasdaq, but is less than the Birling PRSI's, with a closing price of \$25.31.

– **Evertec Inc. (EVTC):** Its 21.69 percent return is lower than the Birling PRSI and S&P's, but greater than the Dow and Nasdaq's, with a closing price of \$47.85.

Focusing on Popular Inc. and the solid year 2021 has turned out to be:

– **Popular Inc. (BPOP)** achieved a 37.25 percent return, exceeding the Dow, S&P and Nasdaq's, but just below the Birling PRSI.

Key Stats for Popular Inc.:

– Total assets: \$74.19 billion, up 12.56 percent

– Total loans: \$28.9 billion, up 6.16 percent

– Nine months' net income: \$728.8 million, up 120.62 percent.

– Stock price: \$77.32, up 37.28 percent

– Common Equity Tier 1 of 17.4 percent

– Credit Ratings: Fitch, BBB- Stable; Moody's, Ba3 stable; and S&P, BB- Positive Outlooks.

The five Puerto Rico public companies in the Birling PRSI have made a comeback from the -52.49 percent return they had on March 18, 2020. The index's 42.81 percent return is an outstanding achievement.

Francisco Rodríguez-Castro is president and CEO of Birling Capital LLC. Think Strategically© is a publication by Birling Capital LLC that summarizes recent geopolitical, economic, market and other developments. This report is intended for general information purposes only and does not represent investment, legal, regulatory, or tax advice. Recipients are cautioned to seek appropriate professional counsel regarding any of the matters discussed.