THE PERSONAL WEALTH COACH®

An SEC Registered Investment Adviser

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TPWC Market and Economic Update – Special Edition

The Markets

Had an observer looked at the S&P 500 stock index (SPX) at the beginning of this month and then again today they would have seen a very pleasant rise in the index values. On the other hand, watching daily we have seen rises and falls in days that we have not seen over months in previous years. The SPX closed today at 3124.74, up 2.74% from Friday, but still not quite as high as it was last week at this time. It is now down 3.02% year-to-date, down 7.72% from its top in February and up almost 40% from its bottom in March. Perhaps most importantly to longer-term investors, the SPX is up 7.09% from where it was a year ago. The surges and falls we have seen in the stock market over the last several months and even over the last several days have a simple cause, *uncertainty*. In more normal times most of the variables that are likely to cause market moves remain more or less constant with small moves month-to-month or even from quarter to quarter. When one of those variables moves a little, it causes an oversized movement in the market. In this time of pandemic, the gauges that investors use to determine whether the market is over or underpriced have swung massively. Some of them indicate the market is dramatically underpriced while others indicate the market is dramatically overpriced. The answer is more appropriately, "We just don't know."

Some very vocal investors have proclaimed that this is the worst set of economic numbers we have seen since the Great Depression; therefore, the market should be down, way down. Others look at the quantity of cash that is sitting on the sidelines and their confidence that a vaccine will be developed within the next year and conclude that the market is very underpriced because things will not only return to normal in a year or so, but the surge in pent-up demand will cause a boom in the economy and in corporate earnings. We believe the prudent thing to do, presuming a well-diversified and well allocated portfolio was what you started with, is to do nothing. The future is always uncertain, we just are very much aware of it right now.

The U.S. 10 Year Treasury note was in lockstep with the stock market and closed at 0.746%; higher than it was on Friday but lower than it was at this time last week, with the yield curve remaining solidly positive. West Texas Intermediate crude oil (WTI) agreed with both the stock market and the bond market and ended the business day at $37.84 a barrel, like the other indicators, higher than it was on Friday but a bit lower than it was last week at this time.

The Economy

According to the Commerce Department, U.S. retail sales rose a record 17.7% in May from a month earlier but were still down 6.1% from where they were a year ago and 7.9% below their pre-COVID-19 level. May's results were in stark contrast with the 14.7% decline in retail sales we saw in April and the 8.2% drop we saw in March. The question is where they go from here. No one has a good handle on how much of the increase in sales was rebound and how much of it will be sustainable. More, a 6.1% drop in retail sales in a years' time is a big hit. In an economy where two thirds of GDP is consumer spending, a market that is up over 7% for one year is hard to explain in light of retail sales being down over 6% for that same year. One camp of investors believes the best is yet to come while the other one believes this makes no sense.

There is evidence supporting both arguments. Assets held in money market funds that normally would be invested in stocks and bonds have risen to about $1 trillion since February. That money came out of the market and primarily came from stock sales. The argument is that at some point all that money will go back into the market and drive stock prices higher as soon as the coronavirus threat is behind us. Those seeing the glass as half empty note that corporate earnings in the United States and around the globe have dropped dramatically both currently and in corporate forecasts. If we look at trailing and current earnings, the stock market appears to be priced as high as it was in 2000 just before the 50% drop in value that lasted until 2002.

Another positive for the bulls is that the Federal Reserve appears to be determined to prevent the monetary system from causing damage to the economy. It announced today that the facility it has created to purchase corporate bonds is open and ready to do business. In essence, it is saying that it is willing to loan money at rock-bottom interest rates to corporations indirectly through the market. At the same time, Chairman Powell in his testimony before Congress made a statement that is both obvious and easily forgotten. "Until the public is confident that the disease is contained, a full recovery is unlikely." He also warned of significant uncertainty surrounding the timing and strength of the US economic recovery. He went on to testify that the Fed is providing a cushion and a backstop against further shocks.

Brace yourself for some really bad news in July. Moody's Analytics is now forecasting second-quarter GDP to come in at an annualized rate of -39.8% if that forecast is correct, it will be the worst quarter since GDP has been measured in the United States. Remember too that that number is annualized so the real decline for the quarter will be about 10% and the bottom was probably hit around the end of May.

We remain convinced of a couple of things. First, we will recover from this and go on to better times ahead. Unlike other recessions we have seen in our 40 years of observing the markets and the economy, this event has a single cause and once that cause is behind us, we will recover. The timing though is uncertain. Coronavirus infections are rising, particularly across the southern and western states, and this is still the first wave. History suggests, if we allow infections to get out of control, a second wave will probably arrive this fall and possibly be worse than the first one. Still, by this time next year we fully expect that a vaccine will be available and widely used. That vaccine and its widespread dissemination will mark the end of this crisis. Rebuilding will be necessary in a lot of areas, but we continue to believe that that rebuilding will herald a period of economic prosperity as great as any we have seen in the history of our country. Meanwhile it is critical that we remain patient and persistent in pursuing a prudent investment strategy.

Until Friday we remain alert and aware of the situation and ready to answer your questions and discuss your concerns.

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