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TPWC Market and Economic Update – Special Edition

The Markets

The S&P 500 stock index (SPX) added another 1.08% since Friday as it continued to inch ahead on less-bad news. It closed on Tuesday at 3131.29 moving towards the top of its recent trading range. The SPX is now down 7.53% from its top in February, down 2.8% year to date, up 39.95% from its bottom in March, and up 7.33% from where it was last year at this time. The good news about this recent rally is that the number of stocks participating as a percentage of the S&P 500 appears to be rising. We were concerned previously that only a relatively few stocks were participating in the bull market while many others were definitely in a bear market. The good news appears to have been transmitted to some of the previously bear market stocks and they are beginning to rise too.

The 10-year U.S. Treasury note yield climbed a bit to close at 0.719% and like stocks, stayed within its recent trading range. West Texas Intermediate crude oil (WTI) rose to the top of its trading range as oil investors raised their bets on a good recovery with a surge in demand on the horizon, as it closed out the business day here in the U.S. at $40.02, up 5.76% since Friday.

The Economy

There are several interesting facets of this odd coronavirus economy that are becoming obvious. The first is one we have talked about before, that less-bad news is taken as good news. One of the prime indicators about the future that we have paid attention to in the past is the Purchasing Managers Index (PMI). IHS Markit publishes two PMIs each month, one for manufacturing and the other for services. Their indexes use 50 as the basepoint with numbers above 50 indicating growth and below 50 indicating contraction. The US purchasing managers index for manufacturing for June came in at 49.6. In better times that would be alarming as anything below 50 indicates contraction but in light of how low the numbers have been for the past several months a 49.6 is positively buoyant. The services index did not come in quite as high at 46.7. The composite of the two was at 46.8, still indicating that the economy was contracting in June, but not as fast as it has been for the last four months. The bottom line, according to IHS Markit, is that output and employment were falling at far more modest rates in both the manufacturing and service sectors. The problem now appears to be shifting from the mandatory restrictions placed on businesses by government to the public's fear of contracting COVID-19. Oddly, the areas where the most restrictive lockdowns occurred seem to be rebounding the fastest once the lockdowns ended.

Another thing that has changed is the savings rate. According to the Bureau of Economic Analysis, the U.S. personal savings rate rose to 33% in April and while more recent numbers are not available, anecdotal information suggests that it is remaining high. The savings rate is the difference between income and expenses including taxes for people in the United States. Prior to the Corona pandemic the savings rate was single-digit, averaging about 8.2% recently. In short, people are hoarding money. Some of that is going into money market funds, and the rest is going into savings accounts and CDs. The result is we have a glut of money, but it is not doing anything. It is not being spent and is not being invested. A high savings rate equates to a low spending rate. A low spending rate means a lower GDP in the future. With the threat of a second wave in the coronavirus pandemic it is unlikely that people will reduce those savings positions or spend more of their income, which means that until we get a vaccine economic growth is likely to be slow. The same pattern is showing up in China, Japan, Korea, and in Europe.

Meanwhile Texas reported the highest number of COVID-19 hospitalizations to date on Monday with 2,326 confirmed. For the month of June so far, the seven-day average of new cases diagnosed has doubled. Houston has gone to a condition orange for the disease, indicating that the infections are growing at an uncontrolled rate. This is still the first wave, and the growth rate remains around 3.6% per day in Bell County and in Texas. We are reporting this not to raise undue alarm but as a warning that if the infection and hospitalization rates continue to rise this fast, it is going to have an economic impact. Contrary to what many had hoped, warmer, and even hot weather appears to not be slowing the infection rates.

We know we have said this before, and more than once, but it is growing more and more apparent that a return to a normal economy and the same level of activity we used to call "normal" will have to await a vaccine and its widespread use. Between now and then the road is likely to be bumpy. The good news remains that both history and what we know of economics tells us that this dark time may mark the beginning of an economic and market boom as good or better than any we have seen. The hard part is being patient until it arrives.

Finally, we need some input about this special edition of what was our weekly letter. We got some comments last week that it is becoming a bit repetitive. The initial phrase of this crisis is over. As a result, the quantity of information we have to report on that is likely to move the economy or the markets is becoming limited. If you want us to continue to publish twice a week, let us know. Otherwise we will go back to just the Friday edition.

Until Friday, we remain your faithful managers, observers, and analysts.

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