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Market Update: June 7, 2020

Stocks had yet another huge week. Global stock markets advanced nearly 6% over the past five days and are now up over 22% quarter-to-date. U.S. stocks have now erased most of their "coronavirus losses" and are now down less than 1% for the year.

The U.S. is managing through the effects of a pandemic, economic recession, tensions with China, and riots … but the markets seem to be betting that these are only short-term concerns.

> **The U.S. is being rocked by protests of a scale not seen for half a century and Washington and Beijing are facing off over Hong Kong, all amid a raging pandemic. Markets have often shrugged off geopolitical stress … but the gap between what's happening in the world and in the market seems extreme even by those standards.**
>
> **Mike Bird – WSJ 6/3/20**

The markets are responding to data suggesting the economic downturn has bottomed, as well as hopes that the pandemic will be kept under control. In fact, four of the best-performing days for the Dow Industrials have come on days that had significant announcements regarding virus treatments or vaccines:

- April 17 – Gilead's drug Remdesivir (+705)
- April 29 – Remdesivir's positive trials (+532)
- May 18 – Moderna's early stage human trials (+912)
- May 26 – Novavax's phase one clinical trial (+530)

Investing is – and always has been – a process over time. It should never be about moments in time ... In today's environment, the stock market may also be high on *hopium* with regard to the expected success of the economy, now that it's reopening; but also, with regard to finding therapeutics and/or a vaccine for the virus itself.

Liz Ann Sonders, Charles Schwab – Advisor Perspectives 6/2/20

The jobs report for May came out on Friday, and it was a blockbuster. The jobless rate fell to 13.3% and employers added 2.5 million jobs … the biggest one-month increase in civilian employment since the end of World War II.

Investors are forward looking, I keep hearing, and I've been looking forward to seeing what everyone's looking at. On Friday, I got a glimpse.

Jack Hough – Barron's 6/5/20

The report blew away expectations that were forecasting the unemployment rate to reach 19.8% on a loss of 7 million jobs.

I've been at this for roughly only four decades, but I can't recall an economic report that was so wide of what everybody expected …

Randall W. Forsyth – Barron's 6/5/20

Instead of a bottoming of employment in May and a rebound in June, we apparently hit bottom in April and began to rebound in May.

It appears that businesses began rehiring workers earlier and in greater numbers than expected, a trend that is likely to continue as lockdowns ease around the country. To be clear: things are very far from normal in the labor market. But the pace of improvement, if sustained, suggests more reason for hope in the

> **second half of the year than we have seen from any previous data release.**
>
> **Eric Winograd, CNBC – 6/5/20**

The Labor Department reported on Thursday that 1.9 million Americans applied for unemployment benefits last week. That is the first time since mid-March that weekly claims were below 2 million. Continuing claims, Americans drawing benefits, were up slightly to 21.5 million for the week ended May 23.

> **The ongoing retreat in the level of initial claims is welcome news. We still expect the recovery in the labor market to be painfully slow.**
>
> **Nancy Vanden Houten, Oxford Economics – WSJ 6/4/20**

Vanguard forecasts a moderate recovery for the global economy in the second half of this year. They also expect U.S. economic growth to decline by "high single digits" for all of 2020. Here are some additional insights from their June 2020 - Market Perspectives:

- Activity should resume in a staggered fashion, with some segments of the economy gearing up more quickly than others.
- The main challenge, regardless of whether lockdown measures can be eased, is the extent to which consumers are willing or have the money to engage with face-to-face service sectors.
- Weak global demand will prohibit a strong bounce-back for China.
- The pandemic has emphatically reinforced the value of supply-chain diversification. Mexico and Southeast Asia will benefit as companies diversify.
- The likelihood grows that U.S.-China tensions will weigh on the markets.

The Congressional Budget Office has adjusted its economic forecast for 2020-2030 to reflect the sharp contractions triggered by the coronavirus. According to their updated forecast, U.S. GDP will not catch up to previous projections until the end of 2029. In other words, it will take a full 10 years to recover from the effects of the pandemic.

> **While the economy is expected to resume growing after this year, the pace of growth likely won't be fast enough to quickly make up for the ground lost during the coronavirus pandemic. The difference between the CBO's latest projection for GDP and its January forecast *roughly disappears by 2030* adjusted for inflation.**

Hannon/Kiernan – WSJ 6/1/20

China's economic rebound may already be stalling because of falling orders from overseas customers. Although formally abandoning annual economic growth targets, Beijing is still focused on job creation and the eradication of poverty. Both goals, however, are under pressure from continuing weakness in exports.

> **I'm afraid the fastest pace of recovery is already behind us. Weak demand is indeed the biggest problem.**

Yang Weixiao, Kaiyuan Securities – WSJ 6/1/20

The World Bank, based in Washington, is owned collectively by 189 countries. It lends to the world's poorest countries, helping them to develop their economies. Most emerging economies do not have the ability to borrow heavily, like the U.S. and the European Union, to support stimulus programs.

Over the past few months, the World Bank has provided $160 billion of pandemic relief loans to struggling countries. The World Bank believes the pandemic will leave lasting scars for these low-income and emerging-market economies, and they will probably remain deeply damaged over the next five years or so.

> **The bottom line is that most emerging market and developing economies started this crisis in a weak position, with a lot of vulnerabilities, and it's the biggest shock since World War II.**
>
> **Ceyla Pazarbasioglu, World Bank VP – WSJ 6/2/20**

When the year started, analysts expected corporate earnings to grow by 10% … analysts now expect earnings for companies in the S&P 500 over the next four quarters to decline 20% from a year earlier. That forecast would put current stock values at 21.6 times expected earnings.

Everyone knows that valuations have been distorted by the pandemic, and earnings declines are hopefully just temporary. Still, the recent stock market rebound has left the S&P 500 at levels last seen in late 2019, when expected earnings were 25% higher, and S&P 500 stocks were valued at 17.4 times earnings.

> **Earnings expectations aren't the only driver of stocks, of course. The collapse in long-term interest rates since the crisis struck probably has left many investors with the feeling that there is nowhere else to stick their savings … But as the expected collapse in earnings over the next year starts to become reality, investors' faith in the stock market could be put to the test.**
>
> **Justin Lahart – WSJ 6/1/20**

Growth stocks have considerably outperformed value stocks since 2017. For the 13 quarters through March of this year, growth stocks are up over 46% against a 5% decline by value stocks. Almost all of this differential has come from the spread in valuations … not corporate earnings. In other words, growth stocks have become much more expensive over the past few years.

> **Studious observers of market history know that value faced similar death sentences previously, only to undergo a rapid reincarnation and deliver spectacular returns. Valuation spreads – while they are not perfect predictors of the future and cannot be used to time factors or asset classes – are the best predictors of future returns.**

Larry Swedroe, Buckingham Strategic Wealth – Advisor Perspectives 6/1/20

The Leuthold Group broke the market down into two groups, one containing the top 25% by valuation and the other with the remaining 75% of companies. While the most expensive stocks have continued to get more expensive, valuations in the remainder group were basically unchanged. The takeaway:

> **The broad market is not overvalued.**

Jim Paulsen, The Leuthold Group – Barron's 6/5/20

The stock market has always been a leading indicator, and Friday's jobs report seemed to confirm why the markets have been on a tear over the past 11 weeks.

Thoughts of a V-shaped recovery have resurfaced, but disciplined investors never get caught up in the euphoria ... they stay calm and unemotional. It should take some time before the global economy gets back to pre-pandemic levels.

Daniel G. Corrigan, CPA/PFS, CFP®