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August 3, 2020

Weekly Viewpoint

Market Indices Post Fourth Straight Month of Gains

Performance for Week Ending 7.31.2020

The Dow Jones Industrial Average (Dow) lost 0.16%, the Wilshire 5000 Total Market Index[SM] (Wilshire 5000[SM]) gained 1.80%, the Standard & Poor's 500 Index (S&P 500) added 1.73% and the Nasdaq Composite Index (NASDAQ) tacked on 3.69%. Sector breadth was mixed with 7 of the S&P sector groups closing higher and 4 finishing lower. The Technology (+4.98%) sector was the best performer while Energy (-4.23%) was the worst.

Index*	Closing Price 7/31/2020	Percentage Change for Week Ending 7/31/2020	Year-to-Date Percentage Change Through 7/31/2020
Dow	26428.33	-0.16%	-7.39%
Wilshire 5000	33393.39	+1.80%	+1.54%
S&P 500	3271.12	+1.73%	+1.25%
Nasdaq	10745.27	+3.69%	+19.76%

Market Observations: 7/27/20–7/31/20

The major market indices finished the week mostly higher reflecting another batch of solid earnings reports and a pledge from the Federal Reserve to maintain very accommodative monetary policy for the foreseeable future. The combination helped offset a report that showed the economy contracting at a record pace during the second quarter. On the earnings front, technology bellwethers Apple, Amazon, Facebook and Google reported better than expected quarterly earnings, underscoring how much consumers have come to depend on their products during the coronavirus pandemic. All four of the market indices finished higher during the month of July, marking the fourth consecutive month of gains.

Fed Remains "all in": As expected, the Federal Open Market Committee (FOMC) meeting ended with the central bank leaving rates unchanged near zero, while pledging to use all its tools to support a recovery from the coronavirus pandemic. According to the after-meeting statement, "The path of the economy will depend significantly on the course of the virus. The ongoing public health crisis will weigh heavily on economic activity, employment, and inflation in the near term, and poses considerable risks to the economic outlook over the medium term. In light of these developments, the Committee decided to maintain the target range for the federal funds rate at 0 to 1/4 percent. The Committee expects to maintain this target range until it is confident that the economy has weathered recent events and is on track to achieve its maximum employment and price stability goals."

Q2 Earnings: Second quarter earnings season continues to trend at a better than feared pace. Through Friday, 312 members of the S&P 500 having reported earnings with nearly 85% surprising to the upside. Aggregate earnings growth has fallen by 10.4%, but still well ahead of the forecasted 44% decline at the start of reporting season. Ten of the eleven sectors have reported upside surprises, with the biggest surprises coming from the industrials, financial and materials sectors.

Economy Plunged During Q2: The Commerce Department reported that real GDP during the second quarter plunged at a 32.9% annualized rate, the most in the history of the data. While the report was certainly shocking it was far from surprising. The decline was widely expected as the stay-at-home and lockdown orders in response to the COVID pandemic shut down large parts of the economy in early part of the quarter. Meanwhile, the Labor Department reported that initial claims for unemployment insurance increased 12K in the week ended July 25, its second gain in a row, to 1.434 million. Initial claims peaked in late March at 6.9 million but continue to run at a level more than twice the previous record set during the worst of the Great Recession. Moreover, the pickup in claims in the past couple of weeks suggests the labor market recovery has stalled amid the resurgence of COVID cases in the Sunbelt region.

Market View: Following the 40%-plus gains since the bottomed reached on March 23, it wouldn't be surprising to see a period of consolidation develop. Since the March lows, the S&P 500 has had several pullbacks that have ranged from 5 to 7 percent, a level that seems to be the sweet spot to draw the 'Buy the Dip' crowd back into the market. At the end of the day, the amount of stimulus being pumped into the economy should continue to act as a safety net under the market, and if there is one lesson learned over the past decade, it's you shouldn't "Fight the Fed."

If a cooling off period were to develop in the weeks ahead, we would suggest using the pullback to selectively add to equity positions. The economic situation should continue to get "less bad" and earnings expectations have started to stabilize. The healthcare system seems to be better prepared for the second wave of new cases and paradoxically, the market knows that the worst things get, the more likely the Federal Reserve and policymakers will inject additional stimulus into the economy. While nothing moves in a straight line, we continue to believe the return profile over the next 12 – 24 months should remain asymmetrical, with an upward bias.

The Week Ahead: The focal report in the coming week will be the July payroll report on Friday. According to Bloomberg, nonfarm payrolls are expected to grow by 1.578 million while the unemployment rate is forecast to fall to 10.5% (from 11.1% in June). Other data reports of interest include; the Institute for Supply Management's (ISM) July manufacturing index, the Markit Purchasing Managers' Manufacturing Index (PMI) index, June construction spending, motor vehicle sales for the month of July, the July ADP employment report, and the July ISM non-manufacturing (services) index. Second-quarter earnings season will remain on the front burner, with 130 members of the S&P 500 reporting results. Fed Heads will be out and about with a half dozen speeches scheduled throughout the week.

Definitions

The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally defined as the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

Wilshire 5000 Total Market IndexSM represents the broadest index for the U.S. equity market, measuring the performance of all U.S. equity securities with readily available price data. The index is comprised of virtually every stock that: the firm's headquarters are based in the U.S.; the stock is actively traded on a U.S. exchange; the stock has widely available pricing information (this disqualifies bulletin board or over-the-counter stocks). The index is market cap weighted, meaning that the firms with the highest market value account for a larger portion of the index.

Standard and Poor's 500 Index is a capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The Nasdaq Composite Index is a broad-based capitalization-weighted index of stocks in all three NASDAQ tiers: Global Select, Global Market and Capital Market. The index was developed with a base level of 100 as of February 5, 1971.

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