MARKETS TURN POSITIVE (BRIEFLY) AFTER PANDEMIC LOWS

On Monday, June 8th, the S&P 500—at least temporarily—returned to positive territory for calendar year 2020. This coincided with the announcement from the National Bureau of Economic Research that the U.S. had officially entered a recession in February. U.S. COVID-19 infections surpassed 2 million, the U.S. death toll surpassed 112,000, and riots continue for the 16th consecutive day in response to police brutality and racism in the wake of the murder of George Floyd.

From its all-time high on February 19th, the S&P 500 declined -34% through March 23rd. Off these lows, the subsequent rally for U.S. equities is unprecedented. As of the June 8th market close, the S&P 500 had appreciated over 45% since late March and was within 4% of its peak. Dating back over 50 years, the 40% gain for the Index during the first 50 trading days following March 23rd is unmatched. The only other distinct periods when the 50-day returns exceeded 30% began in March 2009 following the lows of the Great Financial Crisis, which coincided with the start of the most recent bull market, and a rally in October 1982, which was the beginning of a five-year bull market thanks to President Ronald Reagan.

In recent weeks, there has also been a resurgence in so-called value-oriented stocks. A value-stock can be defined as one that is cheap in relation to such basic measures of corporate performance as earnings, sales, book value, and cash flow. The retail, bank, energy, and industrial sectors are typically considered value plays. Prospects for these stocks—which, as a group, had already meaningfully lagged their technology and communication-services growth peers for the three-year period preceding the onset of the pandemic—will likely be determined by how smoothly the reopening goes and the degree to which economic data reverts to pre-pandemic levels.

The sharp rebound for equities has coincided with ongoing concerns about the health of the economy. The Congressional Budget Office now projects the U.S. economy will not recover from the pandemic for a decade. A record decline of -53% is projected for second quarter GDP according to the Atlanta Fed. The GDP downturn for the full calendar year is expected to be the largest in over 70 years.

The equity rally has occurred despite limited visibility on corporate earnings. Many companies have opted not to provide quarterly and full-year expectations and guidance due to uncertainty related to the impact of the pandemic. FactSet recently estimated a -43% decline in second quarter earnings for the S&P 500, which would represent the largest year-over-year decline in earnings since the fourth quarter of 2008. The Institutional Brokers' Estimate System estimates 2020 S&P 500 earnings will decline -23% versus 2019, before rebounding in 2021. Valuations are elevated, with the forward 12-month price-to-earnings ratio for the S&P 500 at 23x. An expected earnings decline this year is no longer reflected in market returns, and follows a year when the S&P Index was up over 30% and earnings grew only 3%.

To be sure, investors have taken solace in the broad range of measures the Federal Reserve has implemented to support the economy and financial markets. In the wake of the Fed's response, its balance sheet rose from $4 trillion in early March to over $7 trillion. But other variables could impact prospects for equities in the near-term. These include a potential second wave of COVID-19 infections, social unrest in the U.S. and globally, the upcoming U.S. presidential election, and the state and federal governments' responses to the elevated unemployment rate.

Extreme market volatility, both on the downside and more recently on the upside, is a reminder of the challenging terrain investors must navigate in their pursuit of strong long-term returns. We understand the concerns this year's extreme market action has caused, and share them. At the time of this writing, today's trading action shows declines of over -4% intraday.

While we believe in the growth of markets and increase in share prices over time, we remain as dedicated as ever to building investment plans that seek to both preserve and grow wealth in a way that transcends short-term market conditions and volatility.

Thank you for your interest in our weekly investment commentary. If you would like to speak personally with a member of our team at any time, please click here.

FIERCE FED ACTION

In yesterday's market-moving decision, the Federal Reserve kept interest rates near zero and indicated they will remain at that level for the next two years as the economy recovers from the coronavirus pandemic.

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