



Market Update – October 2020

October continues to show signs of an economy that continues to improve from its abrupt stop. While the recovery is a welcome addition to this year's historic course, taking a closer look at the health of the economy reveals that although many segments have recovered, others have not fared as well. Further, the future's unknowns, such as the elections and delayed fiscal relief packages, create a significant amount of uncertainty that may not be settled for weeks or even months (or more). Let's unpack the good and bad news of the economy and how they can impact risk in the markets.

The good news: consumer spending accounts for nearly two-thirds of the U.S. GDP (1) and is seen as a helpful indicator of economic growth or contraction. Consumption outside of travel-related services, movies, restaurants & bars, and gyms has seen a strong rebound. Believe it or not, retail sales from September of last year to this year are now up 5.4% (2)! Homebuilding is another area that has seen rapid growth, as residential construction increased due to adverse impacts of the COVID-19 related shutdowns, historically low interest rates, and a super-demographic of millennials moving into their first-time homebuying years. Fears of deflation taking hold has gone away for the moment, as CPI was reported to grow at 0.2% in September for an annualized rate of 2.4%. Expectations for future profits have also grown as companies have trimmed any excess they once had, both hard and payroll, and are positioned to deploy capital to their durable business lines that have proven to be resilient in the new environment. While the stock market has hit its spouts of volatility during September and some in October, it has yet to show signs of weakness like March of this year. Financial stress in the banking system, measured by the St. Louis Federal Reserve Financial Stress Index, has improved from its extreme move at the beginning of the year (3). A similar note can be said for the Chicago Fed National Activity Index, which gauges overall economic activity and related inflation pressures, has also begun to move away from the depths of March's lows (4).

The bad news: although consumption is up, sentiment, or how consumers feel, has not enjoyed the same recovery. The most recent report from the University of Michigan noted that consumer sentiment is still 26.5% below its December 2019 peak (5). While consumers are spending in certain areas of the economy, they have dramatically cut in others. Their drastic behavior change has resulted in entire industries, such as the airline industry, relying on relief from Washington D.C. and their local governments. In addition to consumer sentiment being low, the Economic Sentiment Index by Hamilton Place and CivicScience found that confidence in finding a new job has dropped lower than its previous reading in July, a sign that Americans are not convinced that the worst is behind us (6). Speaking of jobs, initial weekly jobless claims as of October 15th showed that nearly 900k jobs were lost in one week's time, a number that is still much higher than the highs of the Great Financial Collapse and 3.7% higher than the same measurement one month prior. While jobless claims continue to stack up, relief talks our nation's capital have not been able to keep to consistent deadlines, as lawmakers focus their attention on confirming a new Supreme Court Justice, Amy Coney Barrett, as well as their reelection campaigns.

The divergence of attention from passing new relief packages has left many Americans waiting for clarity until after the early November elections. Once the elections are complete, we anticipate that lawmakers will be able to redirect their focus on the immediate needs of those effected by economic impacts of COVID-19.

The bottom line: The S&P 500 continues to climb primarily on expectations of financial support from the Fed (interest rates and balance sheet expansion) as well as Congress (stimulus and relief packages). Consensus expectations for corporate profits in the future are high, but mostly due to budgets cuts and repositioning due to the shutdowns. While the strength of the U.S. economy continues to highlight its resilience through the revitalization of many industries, others have not enjoyed the same rebound. As we head into the final weeks of the election season, headlines have a stronger ability to move markets in a volatile manner, and we will not be surprised if that is the case. We anticipate that once the election is complete, the clarity gained will allow for a much more comprehensive, but still cautious outlook of the future. Investors should be detailed and mindful of their appetite for risk and reward as we head into the final months of the year.

- (1) Eapen, A. (n.d.). Economic Sentiment Steady After Turbulent Two Weeks. HPS-CivicScience Economic Sentiment Index. https://hps-civicscience.com/economic-sentiment-steady-after-turbulent-two-weeks/?utm_source=newsletter&utm_medium=email&utm_campaign=newsletter_axiosmarkets&stream=business
- (2) Personal Consumption Expenditures/Gross Domestic Product | FRED | St. Louis Fed. (n.d.). <https://fred.stlouisfed.org/graph/?g=hh3>
- (3) FRED Economic Data. (n.d.). <https://fred.stlouisfed.org/series/STLFSI2>
- (4) FRED Economic Data. (n.d.-b). <https://fred.stlouisfed.org/series/CFNAI>
- (5) SSSD, Advance Monthly Retail, Monthly Retail, and Quarterly E-Commerce: retail.trade@census.gov,(301)763-2713. SSSD, Annual Retail: sssd.annual.reatil.survey@census.gov, (301)763-2747 or (888)211-5946. (n.d.). Monthly Retail Trade, Main Page - US Census Bureau. <https://www.census.gov/retail/index.html>
- (6) Surveys of Consumers. (n.d.). http://www.sca.isr.umich.edu/?utm_source=newsletter&utm_medium=email&utm_campaign=newsletter_axiosmarkets&stream=business

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