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ECONOMIC UPDATE MAY 2020

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Stocks mounted an impressive rally in April. Large Cap stocks in the S&P 500 were up 12.8% for the month reducing their year-to-date loss to -9.3%. Small Cap stocks in the Russell 2000 were up 20% in month but are still down -21.1% in 2020. International stocks in the MSCI EAFE are still down -18.0% for the year even though they gained 8.2% in April. Emerging markets stocks were also up 9.2% for the month but down -16.6% on a year-to-date basis. Bond yields declined which helped the Barclays US Aggregate Bond Index climb 1.8% for the month bringing its year-to-date return to 5.0%.

The economy saw good growth the first two and a half months of the year. However, lockdowns across most of the country beginning in mid-March resulted in negative first quarter GDP growth of -4.8%. Expectations for 2nd quarter GDP growth are around -25%. As the restrictions are lifted, JPMorgan is expecting GDP growth of positive 5% in the third and fourth quarters.

Earnings are also being revised down. Of the S&P 500 companies that have reported so far, first quarter earnings are down about -17%. Estimates for second quarter are for a decline of -34% and -19% in third quarter. According to Zack's, full year 2020 earnings are expected to be down -19% (about what they declined in 2008).

As of April 30, about 30 million people have filed for unemployment in six weeks even with the Payroll Protection Program that is helping small businesses keep and pay employees. The unemployment rate is expected to jump into the high teens from 4.4% in March (3.5% in February). It peaked at 25% during the Great Depression and was 10% in the Great Recession.

Investors seem to be looking past all the dismal projections for 2020 and focusing on a recovery in 2021. Stocks have rallied strongly and seem to be trading at elevated valuations considering much of the US is still shut down. Hopes are high that the US will be able to "reopen" and get back to "normal" soon. To get fully back to "normal", we'll likely need a vaccine or treatment so that people are not scared to be in crowds or travel. If businesses are not able to come back on-line as quickly as expected or if we see a second wave of infections, we could see another downward move in stock prices.

The Federal Reserve and the government actions are significant and should help to support financial markets and the economy in the short run. So far, the $2.4 trillion in spending is 12% of GDP which is twice as much stimulus as used in the Great Recession. Our fiscal deficit is expected to be almost 20% of GDP which will be the most it has been since coming out of World War II. This increase in debt and expansion of the Fed's balance sheet is likely to result in Treasury bond yields staying below 1% for many years. At the end of April, the U.S. 10-year Treasury bond was yielding 0.62% compared to 0.69% at the end of the first quarter. The Federal Funds Rate is expected to also stay at 0.00%-0.25%.

Markets are likely to remain volatile as news related to the coronavirus and the reopening of the economy continues to be reported. It's important that investment changes you make at times like this are in-line with your long-term goals. If you have any questions about your account, please do not hesitate to contact us.