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Stocks were mixed in October. Large cap stocks in the S&P 500 were down -2.7% for the month but are still up 2.8% year-to-date. Small cap stocks in the Russell 2000 were up 2.1% in October but are still down -6.8% year-to-date. International stocks in the MSCI EAFE index were lower by -2.2% in the month resulting in a -7.2% year-to-date return. Emerging markets stocks were up 2.1% for the month and 1.2% so far in 2020. The Barclays US Aggregate Bond Index was down -0.5% for the month bringing its year-to-date return to 6.3%.

The third quarter posted its highest quarterly GDP growth since World War II with a 33.1% bounce off the decline of -31.1% in the second quarter. Although the strength is encouraging, fourth quarter is likely to be more subdued with analysts expecting around 5%. Real GDP is still down 3.5% from its peak in 2019 and isn't expected to reach a new high until the second half of 2021.

The economic strength is being reflected in the earnings reports that have started to come in for third quarter. Of the S&P 500 companies that have reported so far, 83.5% have beaten their earnings estimates and 78.2% have beaten their revenue estimates. These are higher percentages than normal. Total S&P 500 earnings are still expected to be down though by about -15% compared to third quarter last year.

As COVID numbers have been rising, investors have become more concerned about another shutdown. Europe has already seen a new wave of lockdowns in France and Germany. The shutdowns are especially hard on small businesses. Many that close temporarily will not be able to reopen. In the Russell 2000, almost half the small cap stocks are unprofitable right now.

The election has also been partly responsible for the volatility in the market. Another stimulus package is expected to be passed which will help the people who are struggling from the pandemic. The unemployment rate is currently around 8% which is about half of what it was at the peak. However, further job growth will be slower as jobs in leisure and travel are not likely to be coming back soon.

The Fed is leaving short-term rates at 0%-0.25% for the foreseeable future. Even if inflation goes above their 2% target, they will look at a longer-term average before raising rates. The 10-year Treasury yield was at 0.86% at the end of October.

The policy moves of the Fed and of Congress have helped the markets rebound from their lows but in the future, investors will likely begin to worry about the long-term impact of these policies. The most likely impact will be some combination of slower long-term economic growth as we deal with the budgetary impact of much higher national debt and higher inflation which could flow out of the sharp increase in the size of the Fed balance sheet.

Analysts warn about making investment decisions based on elections as stock returns have usually been positive the first year following the election. Diversification and maintaining an allocation in line with your risk tolerance are good strategies for investors. If you have any questions about your account, please do not hesitate to contact us.

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