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BLBB Advisors, LLC – Market Update

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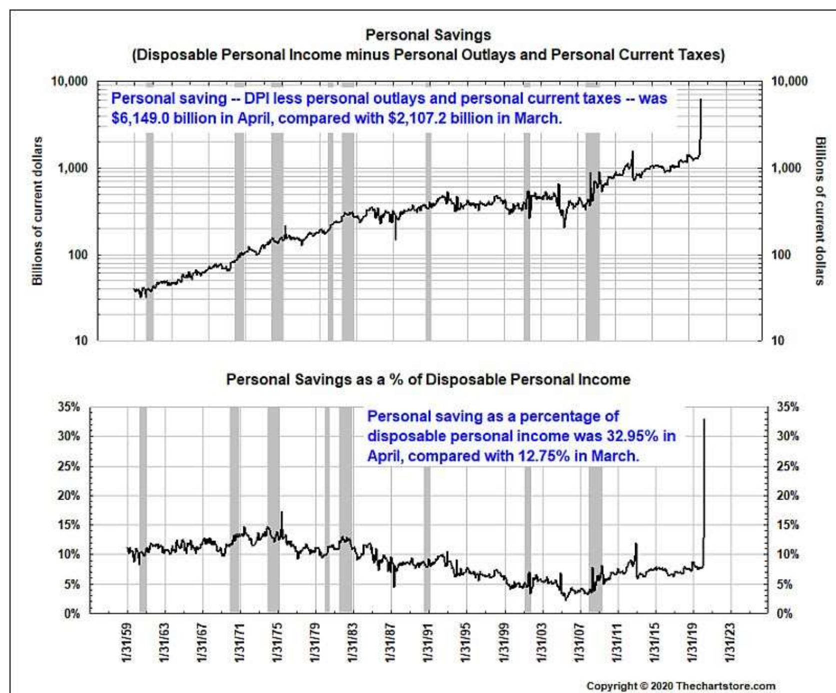
After a 40% surge in the S&P 500 since the March 23rd lows, US equity markets finally look like they are getting ready to take a breather and enter a consolidation period. To the surprise of many, the major US equity indices have appeared to defy gravity over the last couple of months – pushing ahead by leaps and bounds even in the face of numerous and significant uncertainties and a wide variety of troubling news in the US and overseas. In the first 10 days of June alone (8 trading days) the S&P 500 was up 4.4%.

Coincidentally, there has also been a noticeable uptick in retail investors trading stocks on commission-free platforms like Robinhood. In fact, adding to savings and trading stocks were two of the most common uses for the stimulus checks many received over the last few months (Link here). The personal savings chart below illustrates the sudden and dramatic increase in the savings rate – most likely caused by people banking their stimulus checks, cutting way back on spending, and banking some of their unemployment benefits as some people are now receiving more than they usually earn because of temporarily more generous unemployment benefits.



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We have some concern, however, that the heightened savings rate is also a result of people opting to take advantage of temporarily relaxed payment rules and deferral options for their mortgages, credit cards, student loans, and other debt. Recent data indicates the numbers of mortgages, credit cards, and other loans now in hardship status have increased 7-fold from about 0.05% to 3.5% (Link here). While it may make good financial sense for some to conserve funds over the short-term and temporarily reduce or eliminate debt payments, it is quite possible, however, that unemployment and economic distress will last far longer than the several months reprieve now being offered by many lenders. Also, for some loans, the interest due continues to mount. Hopefully, we will continue to see improvement in the unemployment and job creation data, as the sooner people are able to return to work, the more likely it is they will be able to resume their usual debt repayments.

In stark contrast to recent equity market activity, this morning (Thursday, June 11), the Dow Jones Industrial Average opened down about 900 points. So far today, the DJIA and S&P 500 are experiencing their largest one-day drops since early April. The NASDAQ is also down – for the first time in nine days. It has been a while since we experienced such a sharp downward move in equities. There are several reasons why this is happening today. First, the Federal Reserve Open Market Committee (FOMC) met this week and then issued its monetary policy statement yesterday afternoon. While that statement noted the Fed "*is committed to using its full range of tools to support the U.S. economy in this challenging time, thereby promoting its maximum employment and price stability goals*" it also contains some rather gloomy commentary regarding the prospects for the US economy:

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 (Link here).

The Fed also released its US economic projections for the remainder of this year and 2021-22. You can find those here. As expected, the Fed's projections for the US economy have changed drastically since December 2019. For example, in December, the Fed posited US GDP for 2020 would be 2.0%. Now they predict -6.5%. The Fed also opined it will need to keep the fed funds rate at its current level of 0% - 0.25% through 2022 and will continue to offer additional monetary support through regular purchases of treasury bonds and mortgage-backed securities.

Recently, some economists have suggested the US economic recovery will be "V" shaped. In other words, the economy sharply and swiftly contracted as strict quarantines were imposed simultaneously around the country and world. This is the left side of the "V". Then, the economy bottoms (low point of the "V"; possibly occurred in April) before beginning to recover almost as quickly as it declined (right side of the "V") (Link here). Others suggest we might be in for a "U" shaped recovery wherein the economy takes longer to turnaround (bottom portion of the "U") but eventually returns to its prior growth trajectory. While it remains to be seen how the recovery will play out, and it may not be a "V" or "U" shaped recovery, the Fed is predicting a meaningful rebound in GDP growth for 2021 (from -6.5% in 2020 to a +5.0% in 2021) and a decent but not complete recovery in the unemployment rate (9.3% in 2020 and 6.5% in 2021). By comparison, in December 2019, the Fed predicted unemployment would range from 3.5% to 3.7% from 2020 through 2022.

US equity markets are also falling today on some recent covid-19 data indicating increases in positive tests in some areas of the country including the portions of California, Texas, and Arizona near the border with Mexico, as well as Florida, and South Carolina. There is also growing concern the recent protests in numerous cities around the country may result in a second wave of infections. The protests began in Minneapolis on May 26th – the day after George Floyd's death – and quickly spread to many other cities and towns throughout the US in the ensuing days. It is now June 11th which is 17 days since the initial protests began and about 12 days since many of the larger protests were held. A key question is whether or not we will see a major coronavirus spike attributable to these mass public events. Given the up to 14-day incubation period for the virus, we probably have at least a few more days to go before understanding what the public health ramifications of these protests might be. Also, as protests continue in some areas, it may take longer to realize what impact, if any, these protests will have on coronavirus infection rates (Link here).

Unfortunately, we are in a highly unusual period where prior economic playbooks do not necessarily seem to apply. Also, the economic issues brought on by the quarantines are exacerbated by the numerous uncertainties associated with the coronavirus. In addition, this is also a period of great social unrest. And, to further complicate matters, China appears to be taking advantage of the global pandemic and associated economic distress to push its own agenda upon Hong Kong. The economic and social ramifications of this could be tremendous. The US recently threatened to remove the preferred trade status Hong Kong receives. Also, Britain recently offered the right to live and work in Britain to the 3 million Hong Kong citizens who are eligible for a British National Overseas passport (Link here).

As you can imagine, this is a highly unsettled period, not just in the US, but around the globe. It remains to be seen how these important issues will evolve and eventually resolve. But, until the level of uncertainty falls, it is likely we will continue to have heightened volatility and that financial markets and investors will swing from extreme to extreme. We will do our best to continue to keep you apprised of important developments. Please look for our next update towards the end of the month.