Jeremy R. Hofer
Hofer & Associates Wealth Management
90 E. Thousand Oaks Blvd #310
Thousand Oaks, CA 91360
(805) 557-8054
www.hoferwm.com

Monthly Market Insights

September 1, 2020

The summary below is provided for educational purposes only. If you have any thoughts or would like to discuss any other matters, please feel free to contact me.

Best 100-Day Rally Since 1933

The Dow Jones Industrial Average just had its best 100-day run since 1933, according to a mid-August article in Barron's. The period in question: the Dow's bottom on March 23, which was followed by a 50% advance over the next 100-trading days.

The S&P 500 Index tacked on 51% during the same period, while the Nasdaq Composite added 62%, logging its best advance since the peak of the dot.com bubble.

The S&P 500 went on to eclipse its February peak on August 18 and racked up six more records before the month ended (St. Louis Federal Reserve). Meanwhile, strong tech performance has fueled stellar gains in the Nasdaq this year. Only the Dow has yet to top its previous high.

Index	MTD* Return %	YTD Return %
DJIA[1]	+7.57	-0.38
Nasdaq Composite[2]	+9.59	+31.24
S&P 500 Index[3]	+7.01	+8.34
The Global Dow[4]	+6.00	-4.77
Bond Yields	**Yield - % a/o Aug 31 & Change***	**Yield - % a/o Dec 31, 2019**
3-month T-bill	0.11 +0.02	1.55
2-year Treasury	0.14 +0.03	1.58
10-year Treasury	0.72 +0.17	1.92
30-year Treasury	1.47 +0.29	2.39
Commodities	**Aug 31 Price & Change***	**Year end 2019**
Oil per barrel[5]	$42.61 +2.34	$61.06
Gold per ounce[6]	$1,978.60 -7.30	$1,523.10

Sources: U.S. Treasury, MarketWatch
**MTD: July 31, 2020 – August 31, 2020*

A question that usually arises: Why has the stock market performed so well against the uncertain economic backdrop? The economy has been in recovery mode, but activity is not back to pre-Covid levels, at least according to most metrics. And the virus has yet to be contained.

We'll never be able to quantify with exact certainty why the major indexes have rallied in such a profound way. But we can review some factors that have aided sentiment.

1. Federal Reserve stimulus and an open-ended commitment of additional support,
2. extraordinarily low interest rates,
3. Fed guidance that low rates will continue for an extended period,
4. an improving economy,
5. a smaller-than-expected drop in Q2 S&P 500 profits (Refinitiv),
6. a rollover in new daily Covid cases (Johns Hopkins) and talk of a vaccine, and
7. investors may simply be looking past 2020.

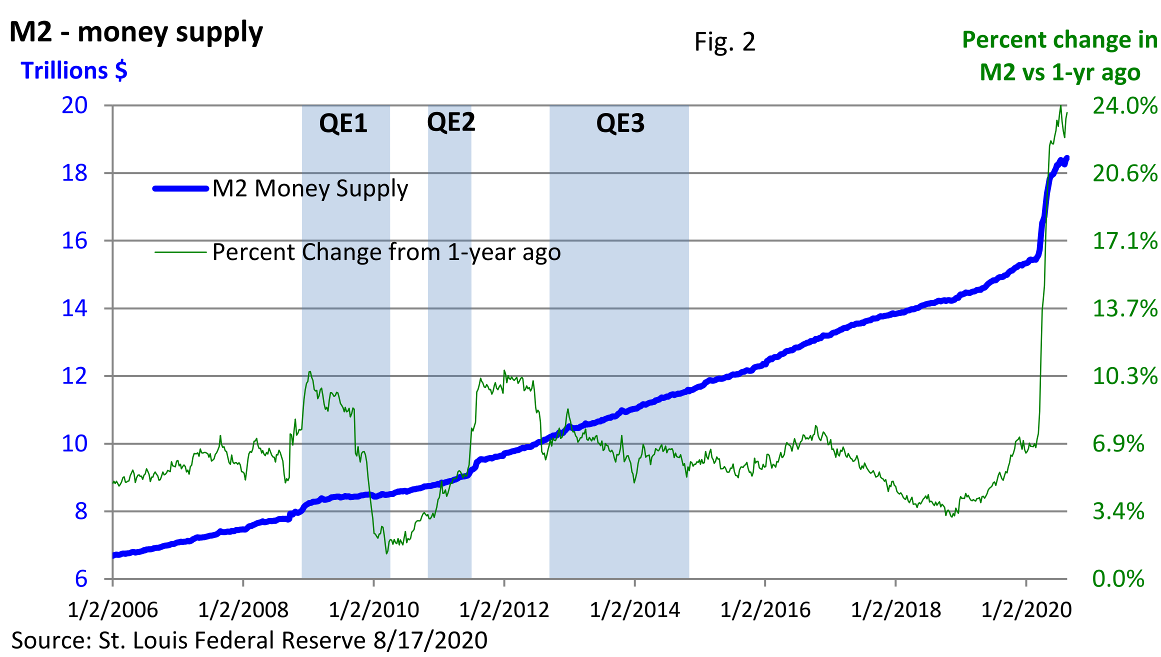
Let's start with the first three, which are tied to the Fed's unprecedented response to the health crisis.

The Fed has cut its key lending rate – the Fed funds rate – to zero. It has announced unlimited purchases of Treasury bonds and mortgage-backed securities. The Fed is buying corporate bonds, including bonds that have fallen below investment grade status, i.e., junk bonds.

It announced a facility to support credit to consumers and businesses, including student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration.

Its Municipal Liquidity Facility can purchase muni bonds of state and local governments.

The response has been far greater than what we saw in the 2008 financial crisis, and Figure 1 illustrates the unprecedented surge in the money supply that has occurred in its wake.

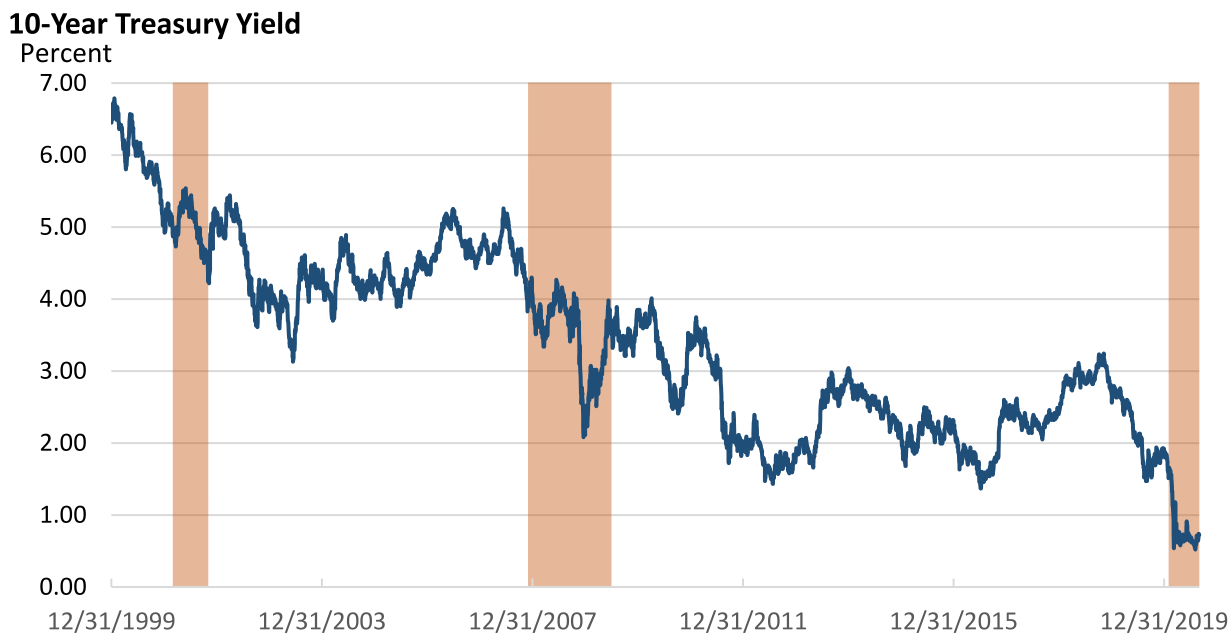


QE1, QE2, QE3 (quantitative easing) were more limited Treasury & mortgage-backed bond purchases initiated by the Fed during and after the financial crisis to support credit conditions and economic growth.

Some of the jump in the money supply can also be traced to fiscal stimulus, including generous jobless benefits and the $1,200 checks that were first mailed in April.

While fiscal stimulus has supported consumer spending, massive amounts of liquidity poured into the economy by the Fed may also be finding its way into stocks.

Rock bottom interest rates encourage savers to consider stocks as an alternative to low-yielding bonds – see Figure 2. Further, the Fed has pledged to keep the fed funds rate low for a long time.



Data Source: St. Louis Federal Reserve, NBER Shaded areas mark recessions 8/31/2020

Next, let's look at the fourth point, the improving economy. In Q2, U.S. Gross Domestic Product (GDP) fell at an annualized rate of 31.7%.

While the worst on record (St. Louis Federal Reserve, quarterly records back to 1947), we've witnessed a sharp economic rebound in May and June, and continued but more moderate growth in July.

Retail sales have returned to pre-Covid levels thanks to pent-up demand and stimulus money (U.S. Census), housing activity has soared (U.S. Census, Natl Assoc of Realtors), and employment is up sharply, though well shy of pre-Covid levels.

But gains have been uneven. First-time claims for unemployment insurance continue to hover near 1 million per week, the unemployment rate remains just above 10% (U.S. BLS as of July), and the uncertainty regarding the virus translates into enormous uncertainty regarding economic forecasts.

Meanwhile, Q2 profits fell far less than expected, according to Refinitiv. As of July 1, Q2 S&P 500 profits were forecast to decline by 43% versus a year ago. As August came to close, Q2 profits were down just under 30%. Yes, it's a huge decline, but the number easily exceeded conservative estimates.

Finally, talk of a vaccine and the idea that investors are looking past 2020 are lending some support to shares. There are a number of vaccines that are being tested, and we may see something later this year or by early 2021.

Risks to the rally

Risks never completely disappear, and the stellar rally leaves shares vulnerable to the unexpected.

Strong performance in tech stocks has supported the Nasdaq, and outperformance by a few large tech stocks has aided the S&P 500 Index. A reversal of fortunes could leave the major indexes vulnerable to volatility.

While the economy is in recovery mode and the end of the recession probably occurred in April (as key economic reports turned higher in May), the U.S. economy isn't immune to another downturn. Fiscal stimulus measures have stalled in Congress, and the outlook remains unusually uncertain.

In addition, the path of the virus as we head into fall and winter is unknown. Might we have a second wave that raises the death rate and stifles economic growth? Or, will we see a wave of new cases now that school has opened in many states? These are tough questions to answer.

Elsewhere, the upcoming election is a headline risk, while tensions between the U.S. and China lurk near the surface.

Yet, while uncertainty persists, the Fed has pulled out all the stops. In addition, the rally in the stock market suggests that the collective wisdom of all investors points to continued economic improvement, though the pace is uncertain.

If you have any concerns, my door is always open. Please continue to adhere to social distancing and safety protocols and stay safe.

Warmest Regards,

Jeremy R. Hofer

Share!

It's OK with us if you would like to share the Market Insights with your friends, family and neighbors. We love meeting new folks!

It is important that you do not use this e-mail to request or authorize the purchase or sale of any security or commodity, or to request any other transactions. Any such request, orders or instructions will not be accepted and will not be processed.

All items discussed in this report are for informational purposes only, are not advice of any kind, and are not intended as a solicitation to buy, hold, or sell any securities. Nothing contained herein constitutes tax, legal, insurance, or investment advice.

Stocks and bonds and commodities are not FDIC insured and can fall in value, and any investment information, securities and commodities mentioned in this report may not be suitable for everyone.

U.S. Treasury bonds and Treasury bills are guaranteed by the U.S. government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. U.S. government bonds are issued and guaranteed as to the timely payment of principal and interest by the federal government. Treasury bills are certificates reflecting short-term (less than one year) obligations of the U.S. government.

Past performance is not a guarantee of future performance.

Different investments involve different degrees of risk, and there can be no assurance that the future performance of any investment, security, commodity or investment strategy that is referenced will be profitable or be suitable for your portfolio. The information has been obtained from sources considered to be reliable, but we do not guarantee that the foregoing material is accurate or complete. The information contained in this report does not purport to be a complete description of the securities, markets, or developments referred to in this material.

The information contained is not a complete summary or statement of all available data necessary for making an investment decision and does not constitute a recommendation.

Before making any investments or making any type of investment decision, please consult with your financial advisor and determine how a security may fit into your investment portfolio, how a decision may affect your financial position and how it may impact your financial goals.

All opinions are subject to change without notice in response to changing market and/or economic conditions.

[1] The Dow Jones Industrials Average is an unmanaged index of 30 major companies which cannot be invested into directly. Past performance does not guarantee future results.
[2] The NASDAQ Composite is an unmanaged index of companies which cannot be invested into directly. Past performance does not guarantee future results.
[3] The S&P 500 Index is an unmanaged index of 500 larger companies which cannot be invested into directly. Past performance does not guarantee future results.
[4] The Global Dow is an unmanaged index composed of stocks of 150 top companies. It cannot be invested into directly. Past performance does not guarantee future results.
[5] CME Group front-month contract; Prices can and do vary; past performance does not guarantee future results.
[6] CME Group continuous contract; Prices can and do vary; past performance does not guarantee future results.

Content was provided by an independent third-party journalist. Index returns do not represent the performance of Hofer & Associates or any of its advisory clients. Historical performance results for investment indexes and/or categories, generally do not reflect the deduction of transaction and/or custodial charges or the deduction of an investment-management fee, the incurrence of which would have the effect of decreasing historical performance results. There are no assurances that a portfolio will match or outperform any particular benchmark.