Weekly Markets Commentary
July 13, 2020

Investors Appear Unfazed by the Surge in Coronavirus Cases – Are They Becoming Complacent?

After their strongest quarter since 1998 in the second quarter, U.S. stocks have picked up right where they left off to start the third. After climbing 1.8 percent last week, the S&P® 500 index is higher by 2.7 percent since June 30, with positive returns in five of the seven trading days. After reaching a recovery high of 3232 on June 8, the index stumbled badly on June 11, falling 7.1 percent that day alone. But the renewed strength of the past two weeks has erased most of that damage, and the index closed on Friday at 3185, just 1.5 percent below that recovery high. And futures are pointing to a higher opening to start the week.

While it may come as a surprise to some, investors apparently are unfazed by the surge in coronavirus cases across the country, especially the south. Despite new daily records being set, stocks prices seem to be responding to improved economic data and government support, including the promise of a fourth round after the July congressional recess. In just the last two weeks, job growth in June, both ISM manufacturing and service sector reports, consumer confidence, pending home sales, motor vehicle sales and factory orders have all been better than expected.

There may come a tipping point at which the health crisis takes precedence in the minds of investors, but we are not there yet.

The European Union Seeks an Agreement on the Pandemic Recovery; Investors Await Economic Data out of China

This is an important week for the economy of the European Union (EU) as well. Members are meeting in Brussels at the end of the week to try and reach an agreement on a pandemic recovery fund that includes grants as well as loans, the former representing a significant departure from previous practice and a step closer to fiscal integration. Germany and France have championed the idea, as has the president of the European Commission. But the so-called “frugal four” countries have balked. The Netherlands, Denmark, Austria and Sweden have expressed their skepticism, as has Finland. Approval of the package and the next seven-year EU budget must be unanimous, and extensive diplomacy has taken place ahead of this week’s summit. But reaching a deal will not be easy.
This is also an important week for the latest information on the Chinese economy. Second quarter GDP is scheduled for release and expected to evidence a return to growth. After posting a year-over-year decline of 6.8 percent in the first quarter, second quarter results are forecast to show growth of 2.2 percent. Also scheduled are reports on trade, industrial production, retail sales and fixed investment. It is worth noting that China is the only major economy worldwide that is forecast by the International Monetary Fund (IMF) to actually grow this year.

*What Should Investors Make of the Upcoming Earnings Season?*

Back home, attention will shift to second quarter earnings this week. According to Factset, earnings are expected to fall by almost 45 percent. The question is, what are we to make of that? It is clear that investors have moved on, content to relegate the second quarter to the history bin. Like rubbernecksers on the highway, we may slow down briefly to take a quick look, but soon refocus on the open road ahead and move on. Maybe the best that can be said is that forward P/Es will look a lot better once the second quarter is behind us. But just how informative the quarter will be is difficult to say. It is not expected to be repeated, although the virus has persisted.

Signs of recovery are encouraging, but just how the economy evolves from here remains uncertain. How companies have fortified their balance sheets during the quarter and whether they navigated through the turmoil better than expected will provide some insight into the quality of execution. But how much this tells us about the expected operating environment of the next several quarters is unclear.

*Important Disclosures:*

Sources: Factset, Bloomberg

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