The economy:

The following economic data points, unemployment claims, consumer spending, industrial production, non-farm payrolls, are known and more importantly *expected.* Because the following is expected it is already reflected in stock prices. It is the *unexpected* or surprise outcomes that significantly impact stock prices positively or negatively.

We see a possible disconnect between stock prices and the economy. This disconnect has been explained by the enormous and rapid federal financial support to the economy through loans and payments to individuals and businesses to get through this period. Corporations have successfully issued additional debt and even equity to raise needed cash. A vaccine gets closer and closer with every passing day. Finally, the market looks out 6-12 months. In May 2021 clearly there are expectations that the economy will be much stronger than today.

Earnings for the S&P 500 for 2020 are currently expected to be $147 and $164 for 2021. At 2900 the S&P 500 is trading at 19x 2020 earnings and 18x 2021 earnings. These are high multiples. Given that interest rates are around zero the cash flow from earnings or dividends become more attractive and are valued at higher levels.

If news comes out that is unexpected and unforeseen the market will correct because uncertainty has entered the picture again. Right now, investors appear to have settled down and agreed on the optimistic future reflected in stock prices.

Data Points

Over a six-week period, there have been 30 million first-time claims for unemployment insurance (through April 25) (https://fred.stlouisfed.org/series/ICSA). It's by far the worst number of layoffs we've ever seen, and it is disheartening to see. However, this has been expected.

A 7.5% decline in consumer spending in March (https://fred.stlouisfed.org/series/PCE) is the biggest decline on record. Industrial production slid 5.4% in March), the worst decline since the end of World War II. https://fred.stlouisfed.org/series/INDPRO# This has been expected.

Nonfarm payrolls for April showed 20.5 million jobs lost and the unemployment rate came in at 14.7%. Also expected.

"Many standard economic statistics have yet to catch up with the reality we are experiencing," Powell said at his end-of-April press conference. "Manufacturing output fell sharply in March and is likely to drop more rapidly (in April) as many factories have temporarily closed."

Put simply, a health crisis has morphed into an economic crisis, with the economy contracting at depression-like speed. "The severity of the downturn will depend on the policy actions taken at all levels of government to cushion the blow and support recovery when the crisis passes," Powell said.

The Market

During April, the Dow Jones Industrial Average and the S&P 500 recorded their best monthly

gains since 1987 (https://www.marketwatch.com/story/after-a-blockbuster-april-for-the-dow-and-sp-500-is-sell-in-may-in-the-coronavirus-era-a-smart-strategy-2020-04-30)
The move in the S&P 500 has been primarily technology, healthcare and consumer staples. Much of technology is subscription based so their cashflows have been little affected. Consumer staples always outperform in a recession as a safe place. Healthcare is a recession resistant sector but especially now with COVID-19 biotech, healthcare providers and healthcare equipment have been winners.
As of May 8, 2020 sector-wise, 10 out of 11 sectors are down YTD with the top two, Technology (XLK) up 2.5% and HealthCare (XLV) off just -2.7%. Microsoft comprises 22% and Apple comprises 20% of XLK. In Healthcare sector Johnson & Johnson comprises 11%, United health 7%, Pfizer 6% and Merck 5%. At the bottom, Energy (XLE) is getting crushed down -36%; Chevron comprises 24% and Exxon 21%. Financials (XLF) have melted -28%; Berkshire Hathaway comprises 14%, JP Morgan 12%, and BankAmerica 8%. Industrials are down -24%. Consumer Discretionary (XLY) is down -7.8%; 38% of Consumer discretionary Sector is in Amazon 25% and Home Depot 13%. When a limited number of names become larger weights in sectors, they can move the performance heavily.
For example, Technology is up 2.5% YTD and the 2 names that are responsible for the move are Microsoft at 22% and Apple at 20%. The tech sector has 72 names in it but MSFT and AAPL account for 42% of the sector.
But the rally over the last month has been nothing short of astonishing given today's dire economic environment as the table below illustrates.

Key Index Returns

	MTD%	**YTD%**
Dow Jones Industrial Average	11.1	-14.7
NASDAQ Composite	15.5	-0.9
S&P 500 Index	12.7	-9.9
Russell 2000 Index	13.7	-21.4
MSCI World ex-USA*	6.8	-18.7
MSCI Emerging Markets*	9.0	-17.0
Bloomberg Barclays US Aggregate Bond TR	1.8	5.0

Source: *Wall Street Journal*, MSCI.com, Morningstar, MarketWatch
MTD: returns: Mar 31, 2020-Apr 30, 2020
YTD returns: Dec 31, 2019-Apr 30, 2020
*in US dollars

How might we explain the disconnect?

The Fed's unlimited firepower has not been enough to prevent a debilitating economic decline, but its unprecedented steps have kept an economic crisis from morphing into another financial crisis, with a massive amount of liquidity and a promise of more support aiding stocks.
Further, government stimulus of over $2.5 trillion is helping sentiment. Talk of a vaccine or treatment that would end the pandemic has been a factor. And, I believe, investors are looking to 2021, when there is the anticipation that corporate profits will turn around.

In January public companies issued additional equity of 10.9 billion; February 15.5 billion; March only 2.8 billion and April 8.9 billion. In total for the first 4 months of the year 38.1 billion dollars were raised in permanent equity capital.
In January corporations issued 130 billion in fixed income; 82 billion in February and 218 billion in March for a total of 430 billion raised in corporate debt. And these figures do not include bank loans or lines of credit available to corporations
Of course, the outlook is very uncertain. Have investors been too optimistic?
Additional government spending and support may be needed to jumpstart economic activity, as Powell alluded to in his press conference. Deficit hawks may cringe at talk of new spending and new programs haven't been problem-free. So far, fiscal stimulus has received strong bipartisan support.
Meanwhile, the reopening of large swaths of the economy *may or may not* go as planned.
This is where we see the biggest possible disconnect. The market action suggests that we will see a very strong rebound in the economy beginning in the 4th quarter 2020.
Another wildcard will be consumer behavior. Prior patterns are unlikely to return to pre-crisis behavior, at least right away, and social distancing at restaurants, airlines, and industries that require person-to-person interactions could limit activity and sales.

Bottom in sight?

Recent market action suggests some type of economic bottom is in sight. Think of it like this: the level and the direction of stocks is the equivalent of the collective wisdom of millions of small and large investors.
They are not simply opinions, but real people and institutions that buy and sell equities, effectively putting their money where their mouth is, as they say.
No one has a crystal ball. No one can tell you where stocks might be at the end of the year. There are too many unknown variables. Those who make forecasts are simply offering opinions.
We understand the uncertainty facing all of us. We are grappling with an economic and a health care crisis. It's something none of us have ever faced.
We are watching the data closely and reviewing asset allocation in accordance with your plan.
We hope you've found this review to be helpful and educational.