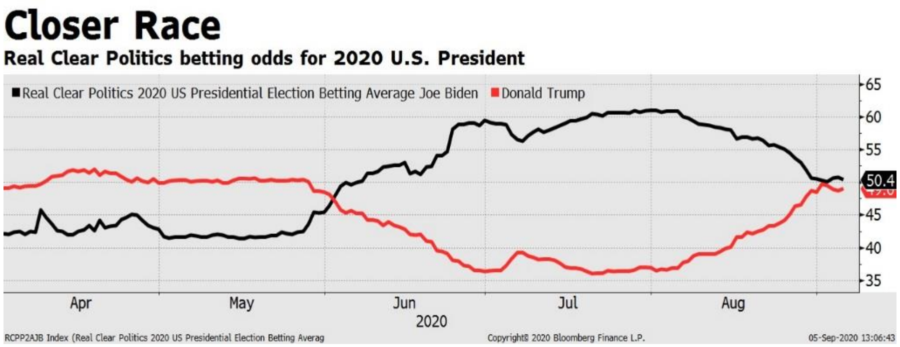
Courier Capital, LLC
Registered Investment Adviser
An affiliate of Five Star Bank

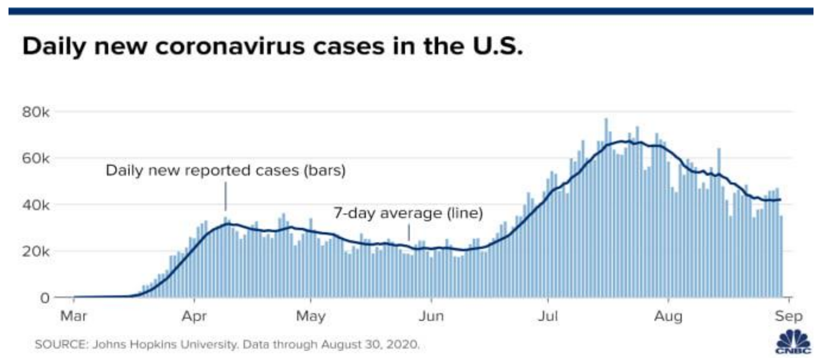
Economic and Market Update – AT A CROSSROADS (08/31/2020)

Latest Developments and Economics

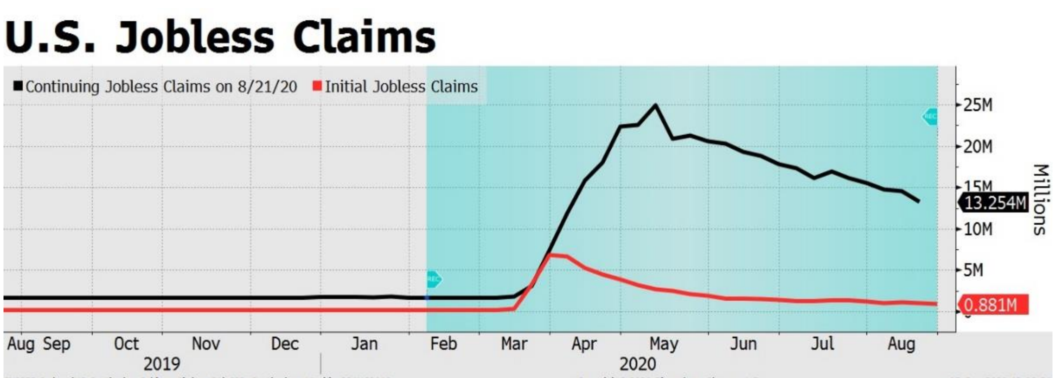
August saw the completion of the virtual (and partially virtual) political party conventions that made Trump/Pence and Biden/Harris the presidential nominees by the Republicans and Democrats for the office of President. We now have the debates on deck (first one scheduled for 9/29) before the elections are held in about 9 weeks. Following the conventions Real Clear politics data shows this to be a race that is getting closer. This election is likely be different than others in that the results may not be known until well after election night (like Bush-Gore in 2000). A contested election does have the potential to create market volatility and many consider this election to be a crossroads in terms of the political direction of the country.



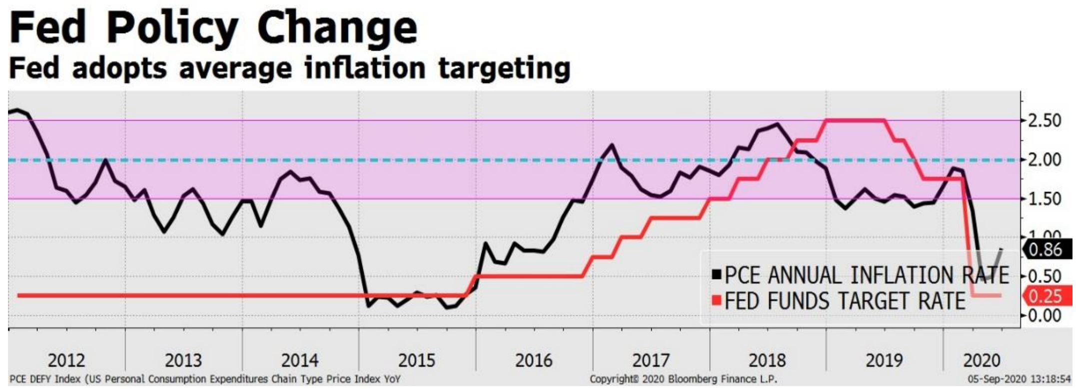
This isn't the only topic facing a crossroads. While the U.S. was experiencing a decrease in the cases of COVID-19 the numbers have started to level off and there is concern that the start of the school year and upcoming flu season could cause more problems. After 6 months of dealing with the virus there is fatigue in the country but also a resiliency to try to return to some sort of normalcy until a vaccine arrives on the scene (which is increasingly expected to be available within the next six months) which will still take time to manufacture and distribute to willing patients.



A third topic seemingly at a crossroads is the near-term direction of the U.S. economy. While the $600 supplement to unemployment insurance ended on July 31 and the PPP payroll requirements end on September 30, the economy has made significant improvements in key economic data, though, by most measures we are still not out of the recession that started earlier this year. Initial Jobless claims finally broke below the 1 million weekly mark (red line) and the continuing claims continue to fall, which have caused the unemployment rate to come down from 14.7% in April to 8.4% at the end of August. This past surprise reading of a net 1.37 million new jobs continues to provide evidence that recovery continues. In other good economic news, the ISM Purchasing Manager's Index continues to rise (latest reading of 56) indicating a rebound in manufacturing, retail sales jumped 1.2% in July from the previous month and were 2.7% ahead of July 2019. Finally, Q2 earnings in the S&P were astonishingly better than expected with 84% of companies reporting positive earnings surprises and 65% with positive revenue surprises. Factset reports that this "marked the highest percentage of S&P 500 companies reporting a positive EPS surprise" since they began tracking this in 2008. This news was also followed by upcoming announcements totaling 115,000

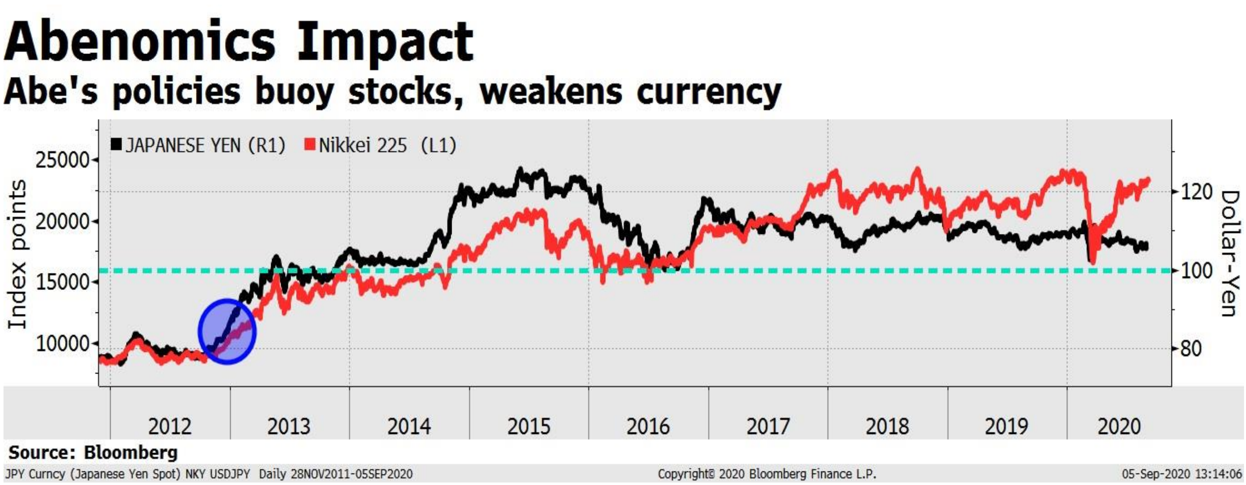


job cuts led by airline, transportation, hotel, restaurant and leisure companies. This bifurcated data has contributed to the impasse in another round of stimulus by both parties. The Democrats have offered to come down from the $3.5 trillion HEROES Act passed by the House in May while Republicans have offered $1 trillion as the next round (arguing there are still funds from the CARES Act not fully utilized). The Republicans in the Senate have also made a few attempts at clean bills addressing only an extension of unemployment benefits but they were rejected by the House. Currently no talks are even scheduled until after Labor Day. The sticking points seem to be the total cost as well as particular elements of the HEROES Act. One such point is Federal aid to states and municipalities – the HEROES Act includes approximately $900 billion for that alone and New York subsequently has sent a request to Congress for $59 billion solely for their state. The impasse caused President Trump to use available funds to extend unemployment supplement of $300 for a few weeks but states need to cooperate to receive the funds and he plana to delay payroll taxes for anyone earning $104,000 or less per year for the rest of 2020.



FOMC Chairman Jerome Powell announced significant changes to Fed policy by changing their price stability mandate from a target of 2% inflation to targeting an "average" of 2% inflation which means they will let the economy run hot if inflation gets past 2%. This was also done partly to support the creation of jobs as, over the last couple years, historically low unemployment did not generate inflation the way it had historically. The announcement is a bit moot as the Fed has not been able to generate inflation near 2% consistently since 2008. The average inflation over the last 10 years has been about 1.5%. This has been caused by low productivity, low potential growth (some due to demographics) and general deflationary pressures on goods and services (think Amazon). Although this is the case with goods and services there has been significant inflation in the price of assets – financial (stocks, bonds), real (housing, precious metals, etc) and even digital (cryptocurrencies) have seen significant price appreciation recently.

In international developments this month Shinzo Abe, Japan's longest serving Prime Minister decided to step down due to declining health. He leaves office with what many consider to be a mixed record of achievement. He is known for the reforms he made to Japan's economy to combat decades of low interest rates and stagnation and to counter China's growing world influence. This leaves Japan at a crossroads as he declined to comment on who would replace him. Though his party remains in power the possibilities range in policy positions. The leading candidates are Taro Aso, (right wing Finance Minister), Shigeru Ishiba (a longtime critic), Fumio Kishida and Taro Kono.



Financial Markets

Despite the mixed economic signals and rising virus cases the financial markets have continued their historic climb since the March lows. The tech-heavy NASDAQ and the S&P 500 set a new closing record highs at the end of August while the Dow Jones Industrial Average turned positive for the year. Although the equity market news has been good, going almost unnoticed is that the volatility index (VIX), sometimes called the "fear gage" has been rising again. In March it was at a historic high of 82 and had steadily declined since to the low 20's but, over the last month it has risen back to 33.

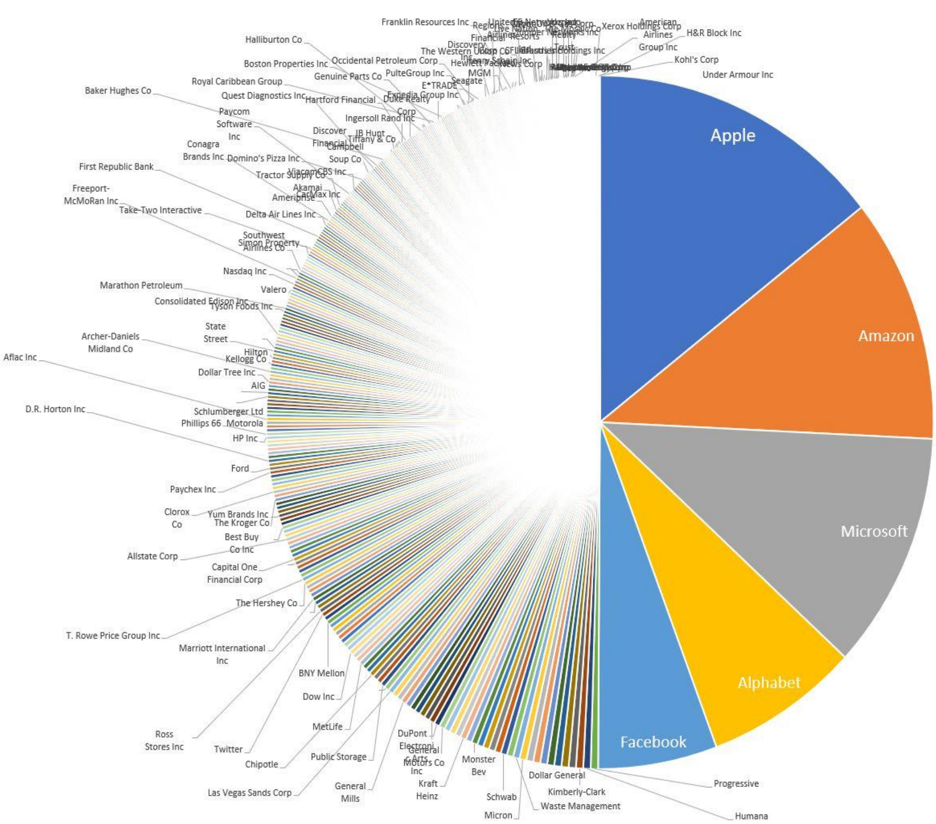
Also, the equity markets are still being driven by information technology (about 6 stocks specifically) and, to a lesser extent, the "stay-at-home" stocks. As you can see in the chart to the left the total return of the Information Technology and Consumer Discretionary returns of 29.66% and 23.90% respectively have contributed 7.96% and 2.73% of the total S&P 500 return of 6.47% due to their weights in the index. Most other sectors had either a minor, or adverse, effect on the S&P 500 total return.

S&P Dow Jones Indices
S&P 500 Total Return Sector Contributions
Year-to-Date as of August 21, 2020

Sector	Total Return	Sector Contribution
Information Technology	29.66%	7.96%
Consumer Discretionary	23.90%	2.73%
Communication Services	11.25%	1.27%
Health Care	5.82%	0.98%
Materials	2.18%	0.08%
Consumer Staples	3.54%	0.05%
Real Estate	-5.83%	-0.41%
Utilities	-6.51%	-0.46%
Industrials	-5.06%	-0.71%
Energy	-38.61%	-1.78%
Financials	-19.85%	-3.24%
S&P 500	**6.47%**	**6.47%**

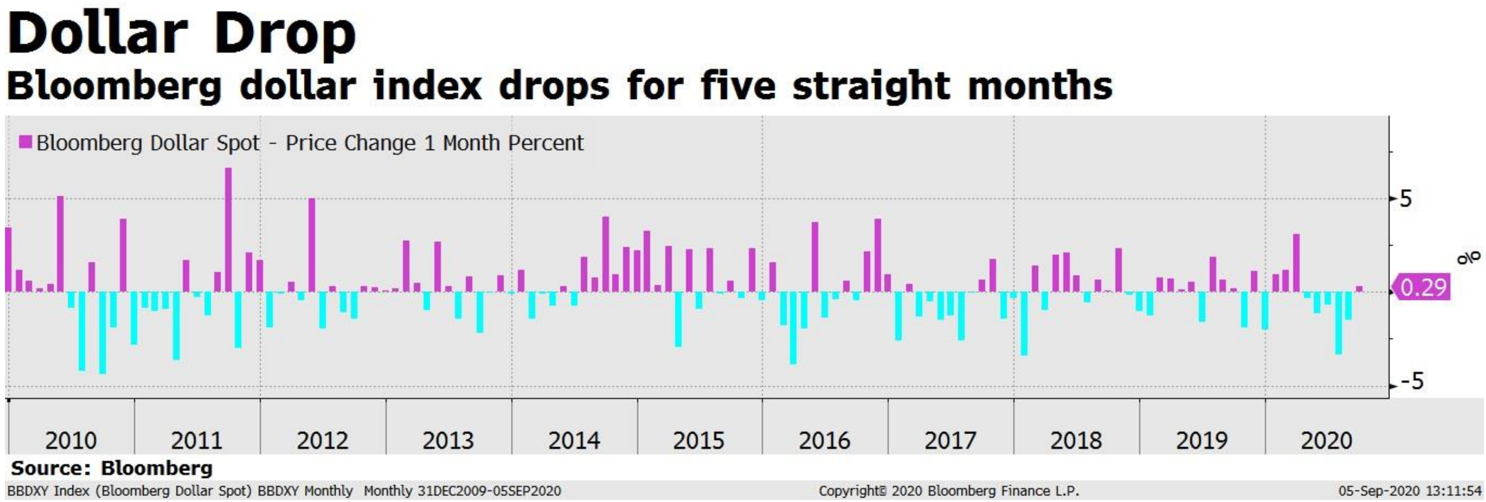
Stocks like Tesla, which has increased tenfold in less than one year) and Apple (about 2.5 times greater than the one year low) have grown so large that they both announced rare stock splits in August (5 for 1 and 4 for 1 respectively). The market capitalization of Tesla is so large due to the stock movement that it is 4 times larger than GM, Ford and Chrysler-Fiat COMBINED (yes, 4 times larger a company than the entire U.S. auto industry). In fact the mega stocks dominate the S&P 500 as well.

The dominance of the 5 big tech companies cannot be overstated. These 5 now make up 26% of the $29 trillion S&P 500. The top 4 are larger than Japan's entire stock market and Apple is larger than the FTSE 100 – the 100 largest companies in the United Kingdom. The chart to the right assembled by Michael Batnick from Ritholtz Wealth Management shows that these 5 are as large as a combined 282 other companies in the S&P 500.



In other U.S. equity market happenings the Dow Jones Industrial Average replaced three stocks (10% of its total) with three new stocks. The committee decided to drop old economy stocks of ExxonMobil, Pfizer and Raytheon Technologies and replace them with Salesforce, Amgen and Honeywell. This was mainly due to the Apple 4 for 1 split. The DJIA is a price-weighted index and the new lower price of Apple, post-split, means that technology representation was underweight. The changes are meant to ensure tech stays about the same weight in the index.

Finally, the currency market movements deserve attention as the direction of the dollar has been changing. There are many reasons for currency changes, which are all relative to other currencies, but the dollar has been slipping lately. There could be many reasons which could include concern about the recovery of the U.S. economy, to political and civil uncertainty to the level of debt the country is taking on. This could also have economic and market implications which we will be watching.



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