Beacon Trust
INNOVATING WEALTH STRATEGY

Market Outlook 2Q 2020 Review **July 6, 2020**

Second Quarter Summary

To transpose a famous quote from Charles Dickens' *A Tale of Two Cities*, it was the worst of times, it was the best of times. Stocks in the U.S. had their best second quarter since 1998, with S&P 500 rising 20.5%. Of course, this dramatic rally must be framed by what happened in Q1, the worst first quarter on record, with the S&P falling 20% as the COVID-19 pandemic swept the globe. The pandemic is far from over, with new cases continuing to increase throughout the U.S. and the rest of the world, thrusting the global economy into a recession.

The apparent disconnect between the severe economic impact of COVID-19 and the stock market, now down very modestly on a year-to-date basis, is not easy to reconcile. In our view, a confluence of factors is driving this disconnect. First, the stock market is a forward-looking mechanism. As long as investors see "light at the end of the tunnel" they will price in a temporary, albeit very painful, period of bad news. The Federal Reserve has come out with "guns blazing", releasing a torrent of liquidity that expanded its balance sheet from less than $4 trillion to $7 trillion, and it is likely on its way to $10 trillion. Fed Chair Jay Powell has stated he will do whatever it takes to prevent the economy from falling into a deeper recession, throwing in the proverbial kitchen sink. Congress, acting in parallel, has unleashed a substantial fiscal stimulus program, including sending direct checks in the mail of $1,200 to most American adults. At least one more stimulus check is likely forthcoming this summer. The unemployment rate fell to 11.1% in June, continuing its downward trend from its peak of 14.4% just two months prior, as furloughed workers return to their jobs. Substantial progress has also been made on vaccine development, pharmaceutical treatment, and the production of ventilators and personal protection equipment. Businesses continue to reopen across the country, albeit in stop-and-start fashion.

Equity performance has been very uneven, with Growth stocks, especially those in the Technology and Healthcare sectors, outperforming Value stocks by a double-digit margin. In fact, the technology laden Nasdaq index recently hit an all-time high. However, not everything is golden. A spate of bankruptcies has occurred in the corporate space, with once vaunted names, such as Neiman Marcus, Hertz, and J.C. Penney now grappling with the Chapter 11 bankruptcy process. Bonds continued to serve as ballast for portfolios, an extremely important role as equity volatility remains more than 50% higher than its historical levels. The Bloomberg Barclays Aggregate Index has returned an impressive 6.3% year-to-date, with returns roughly equal across the first two quarters.

Market Outlook

The economy will not be back to "normal" until there is an effective vaccine, or the virus runs its longer-term course through a "herd immunity" process. There are dozens of COVID-19 vaccines being tested through an accelerated FDA review process. We remain hopeful, given the number of "shots on goal," but are realistic in our assessment that a successful vaccine, and its wide scale manufacturing and inoculation processes are probably at least a year away.

Given the apparent disconnect between the economy and stock market that we previously cited, we expect continued turbulence through the November elections and remain somewhat cautious about near term stock market returns. Our view is further tempered by the likelihood of a "phase 2" return of the virus occurring near the latter part of 2020 and into early 2021. However, looking out over a 2-3 year period, we continue to favor equities over fixed income. Our views are supported by the gradually improving economic fundamentals and the statement by the Federal Reserve that short-term interest rates are expected to remain at or close to 0% through 2022. Long-term interest rates are expected to remain subdued with the benchmark 10-Year U.S. Treasury Note at a paltry 0.67%, as of this writing. As fear dissipates, and continued progress on the economic and healthcare fronts take hold, we expect long-term capital to return to equities. We always recommend clients hold diversified portfolios to reduce risk but want to reiterate the importance of this fundamental wealth management principle at this time.

Although the future path of the COVID-19 pandemic remains the paramount risk, other concerns continue to loom in the background. These include tensions between the U.S. and China, additional geopolitical risks, policy risk change after the November elections, and a very high unemployment rate and its unknown ramifications. COVID-19 has upended how traditional industries operate, such as retail sales, travel, and commercial real estate. It is not clear what the “new normal” will look like for these affected industries, as well as new areas that have dramatically accelerated, such as telehealth and “Zoom-like” meetings. Even things as mundane as a simple handshake may be at risk of disappearing from our everyday norms.

On an operational note, Beacon remains fully functional. The bulk of Beacon employees are now back in their offices. We also have a robust technological infrastructure that allows us to work seamlessly. In fact, many of you have participated in virtual meetings with your Beacon team members. In general, the feedback from these virtual meetings has been very positive. All of us at Beacon continue to wish you and your family maximum health, safety, and security at this unparalleled time.

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