What a Year!

The Bottom Line:

The first anniversary of the start of the coronavirus pandemic drawdown is upon us. Looking back, the level of stock market volatility was remarkable. Capital markets have more than recovered, so when does the economy catch up? There should be support in the form of continued monetary & fiscal stimulus, healthy consumer balance sheets, and vaccine rollouts. The fundamental economic outlook looks favorable, which means the market's optimism is probably justified.

The Full Story:

This weekend marks one year since the COVID-19 stock market drawdown began. On February 19, 2020, the U.S. stock market, as measured by the S&P 500, hit a new all-time high. However, the next day would commence a precipitous fall. The news stories from February 20, 2020:

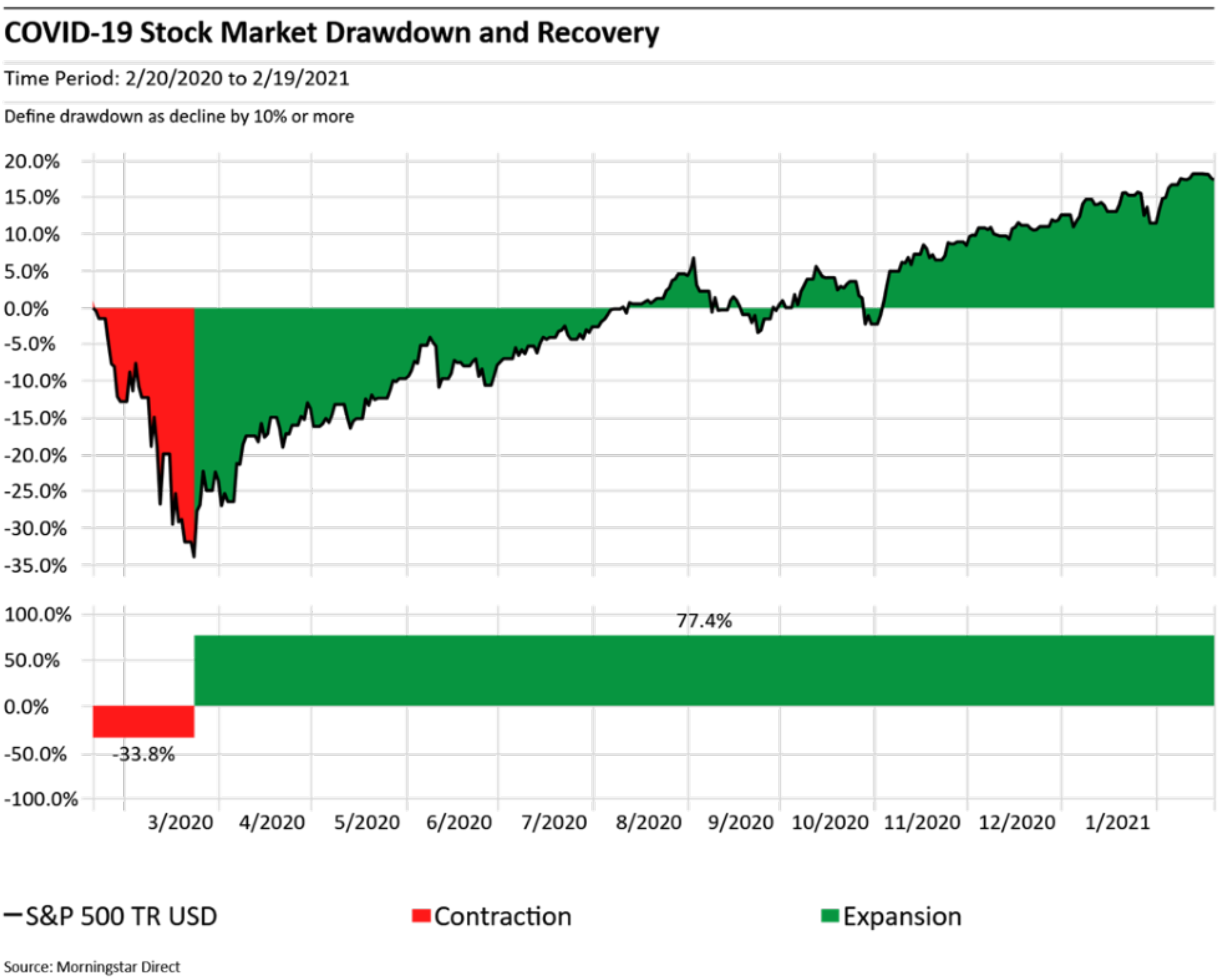
From Reuters: *Wall St. eases, led by tech decline on mounting fears coronavirus could spread*, "Investors were unnerved by a sharp late-morning drop that took the S&P 500 briefly down more than 1% on the day, with some traders attributing the move to a Global Times report that a central Beijing hospital had reported 36 new cases. This raised worries about a potential increase in infections in the Chinese capital."

From CNBC: *Dow falls more than 100 points after suffering a sudden midday sell-off that confused traders*, "Stocks fell on Thursday, with most of the losses coming in a sudden move midday. Traders could not pinpoint a catalyst for the sudden decline. However, some highlighted technical factors breaking down along with an increased risk-off sentiment stemming from fears of the coronavirus slowing the global economy."

The U.S. stock market and global stock market, as measured by the MSCI All Country World Index, declined approximately 34% over the next 33 days (only 22 trading days), achieving the fastest 30% decline on record. The stock market found a bottom on March 23, 2020. On that date, the Federal Reserve announced asset purchases with no limits and expansion into other bonds including corporates and agency commercial mortgage-backed securities.

From CNBC: *The Federal Reserve just pledged asset purchases with no limit to support markets*, "The Federal Reserve said Monday it will launch a barrage of programs aimed at helping markets function more efficiently amid the coronavirus crisis. Among the initiatives is a commitment to continue its asset purchasing program 'in the amounts needed to support smooth market functioning and effective transmission of monetary policy to broader financial conditions and the economy.' That represents a potentially new chapter in the Fed's 'money printing' as it commits to keep expanding its balance sheet as necessary, rather than a commitment to a set amount."

The speed of the recovery would almost match the speed of the drawdown. After just 140 days, on August 10, 2020, the S&P 500 had fully recovered and reached a new all-time high, which was also in record time. Through Friday, the S&P 500 is up 77.4% since the March 23rd bottom and 17.4% over the trailing year (the pre-COVID peak).



The overall stock market recovery has been pleasantly uneventful. There were a couple of pullbacks in September and October as we navigated COVID second waves and pre-election jitters; however, neither of those rose to the technical level of a correction – a decline of more than 10%.

The economy's recovery has been much slower, but resoundingly solid even as mandated and voluntary restrictions on activity hinder growth. Outside of jobless claims, almost every other economic indicator has been trending higher. With COVID cases now down more than 70% from their peak, inertia in the economy should only ease from here. It may be gradual improvements as vaccines roll out, but we are working towards a more normal economy.

What to make of the stock market at current levels?

I have heard some trepidation about expectations for the stock market exceeding potential reality. On one hand, stock valuations appear stretched, we are coming off a 10-year bull market that never truly got reset during the brief COVID bear market, and there is a speculative frenzy among investors in cryptocurrencies, IPOs/SPACs, and crowd-sourced stocks (GameStop) that is reminiscent of the dot-com bubble.

On the other hand,

- **Markets are in an uptrend.** See the returns during the recovery and for the trailing year above. It's not just U.S. large growth stocks (e.g., FAANG). U.S. small caps and emerging markets are surging. Developed internationals and value stocks are keeping pace. There is a healthy breadth to this bull market.

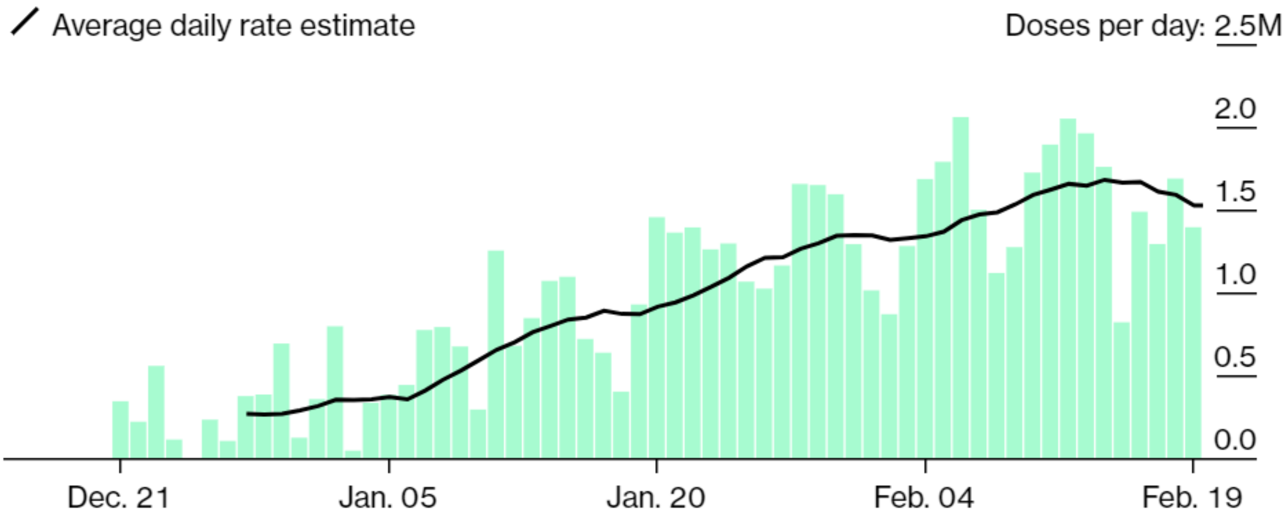
- **The Federal Reserve is providing easy money for as long as possible.** The Federal Reserve has committed to letting the economy and inflation run hot if needed to get back to full employment. In doing so, the federal funds rate has remained at 0%, and quantitative easing continues.

- **More fiscal stimulus is on the way.** President Biden's $1.9 trillion

COVID relief bill is working through Congress's budget reconciliation process. The Biden administration seems willing to overspend to ensure that the economy recovers from the pandemic. It was Biden as Vice President that witnessed the American Recovery and Reinvestment Act of 2009, which was ultimately deemed convoluted and lacking when addressing the Great Recession. And there may be another $1.6 trillion of infrastructure spending on tap. We are potentially looking at wartime spending levels in 2021 and beyond.

- **Consumers are flush with cash**. Although there are still millions of people unemployed and small businesses who are struggling, consumer balance sheets have likely never been stronger coming out of a recession due to all the fiscal aid provided.

- **There is a light at the end of the COVID tunnel by way of vaccines.** In the U.S., 60.5 million doses have been given, according to state-by-state data. In the last week, an average of 1.49 million doses per day were administered.



Note: Vaccinating roughly 70% to 85% of a country's population would enable a return to normalcy, according to top U.S. infectious disease doctor Anthony Fauci. Current vaccines require two doses for full protection. Data are from Bloomberg's Covid-19 Vaccine Tracker.

Call me an optimist, but I think those are more compelling arguments.

Have a great Sunday!

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Sources: Bespoke, Morningstar, Bloomberg, A Wealth of Common Sense, CNBC, Reuters