Weekly Market Review

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The Week Ending April 24, 2020

We have been in some extraordinary times over the past two-plus months, but last week might have marked the most unprecedented theme to date. We made history Monday, as oil futures traded in negative territory at the beginning of the week. The commodity known as "black gold" could not even be given away for free; sellers had to pay buyers as the price of oil dropped to negative territory.

One factor leading to oil's volatility is the difficulty in trading the commodity. Trading oil is not as simple as buying or selling a stock. Oil trades in the futures market. When you trade oil futures, you are trading a contract for the purchase or sale of physical oil at a specific price on a specific date in the future. Traders who have bought futures must later sell them to close out their position, or they will have to take physical delivery of the commodity. As you might imagine, most futures traders do not have the storage or use for millions of barrels of oil at their firms. Thus, when the May futures contract expired on April 21, traders were so desperate to close their positions that they were willing to pay buyers to take this obligation off their hands. As a result, oil crashed below zero.

Now that we are trading June's oil contract, prices have rebounded back into positive territory. Considering the sharp drop in price and elevated volatility are caused by both the supply and demand sides of the equation, volatility is expected going forward. As long as the U.S. and most of the world are under a "stay at home" order, demand will be stressed. And as producers continue to drill, supply will increase, meaning the probability is downward pressure on prices over the near term.

While oil was the biggest event of the week, the estimate of the April Purchasing Managers' Index for global services and manufacturing also reared its ugly head. PMIs posted results lower than during the depths of the Financial Crisis. The services sector was the largest detractor for the month. This makes sense, given the global shutdown has had the most significant effect on those industries. Since this is also a large component of GDP, it is highly probable that the second quarter is going to be a sharp contraction.

The upcoming week could start to provide clues to the damage COVID-19 has caused to the economy. We will receive the first-quarter GDP estimate and earnings from over 100 companies. While companies are unlikely to share meaningful outlooks, hearing directly from company management can provide some insight on what to expect over the next couple of months.

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