Weekly Market Review

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As quickly as the bear market hit in the first quarter, it is now a thing of the past, just six months later. Last week, the S&P 500 Index officially traded beyond its February 19th high, commencing a new bull market. On the surface, it has been a strong recovery since the market bottom on March 23rd; however, not all stocks participated. According to CNBC, only 38% of stocks in the S&P 500 Index are in positive territory since the last market peak. Technology companies like Apple, which became the first company with a $2 trillion market cap, are leading the market higher. In contrast, travel and energy companies struggle to gain momentum in a COVID-19 world.

At the beginning of the COVID-19 recovery, experts discussed the type of recovery we would experience. Theories ranged from a quick “V” shaped recovery, to a long drawn out “L” recovery, and everywhere in between. Peter Atwater recently proposed what could be the most likely and previously overlooked outcome: the “K” shaped recovery. Part of the economy is acting like we are not in the midst of a global pandemic and trading to new highs (the upward sloping section of the “K”). Then, thereis the downward sloping part of the “K,” or the parts of the economy still struggling and unable to regain their footing since the economic shutdown.

While it might seem the economy and stock market are not in sync, it is much harder to make a direct comparison between the two. The U.S. economy’s services sector makes up 86% of U.S. employment, but only 31% of earnings for the S&P 500 Index. Manufacturing accounts for the remainder of both measures. Looking further into this divergence, the services sectors most directly impacted by the COVID-19 pandemic (restaurants, retail, travel) contributed 19% to GDP last year, but only 7% to S&P 500 earnings. So, the sharp spike in unemployment has an outsized impact on GDP growth. At the same time, the stock market is being driven by technology companies and those benefiting from the new work-from-home environment.

The stock market’s divergence leaves us asking, where do we go from here? A handful of companies are leading the market higher, while parts of the economy are struggling, and companies that make up most of U.S. employment are downsizing or closing for good. Unfortunately, no one knows what is going to happen over the short to intermediate-term. However, we do have confidence in success over the long term, and times like this show the importance of active managers being able to position themselves for success, even when it is a challenging environment.

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