Weekly Market Review

By: Joe Clark, CFA, Allegheny Research Team

The Week Ending August 28, 2020

With one trading day left in August, it is safe to say the S&P 500 has continued its monthly winning streak, now at five months. Typically, August is one of the worst months for stock market performance. Traders usually enjoy what is left of summer leading to lower than usual volume and a rather dull month for the markets. However, this is 2020, and no one should expect the norms to continue. In typical 2020 fashion, the S&P 500 is well on its way to posting its best August since 1984 with a gain of about 7% (given a sell-off does not occur on Monday).

As in recent years, technology stocks were the dominant drivers of August's performance. According to Bank of America Global Research, the technology sector recently became more valuable than the entire European stock market. In 2007, Europe was about four times larger than the U.S. technology sector. A decade of underperformance for Europe and the U.S. technology sector being one of the strongest performers worldwide led to that one sector growing larger than an entire continent's stock market. Some of these companies might be expensive, but they continue to beat expectations and prove they are great companies that deserve these lofty valuations.

Along with the technology rally, "Don't fight the Fed" continues to the be standard for this year's rally, and last week was no different. In his annual speech at the Jackson Hole Economic Policy Symposium, which took place online this year, Federal Research Chair Jerome Powell announced a change to how the Fed will react to inflation going forward. Previously, the Fed has targeted a 2% inflation rate to gauge when to raise interest rates. In the future, the Fed will be looking more at a rolling period to have sustained inflation above 2%, perhaps even approaching 2.5%, before increasing short-term rates.

While this may not seem like much of a change, it does increase the emphasis on inflation rather than employment, the other piece of the Fed's dual mandate. If conditions of the past expansion continue, and inflation remains difficult to find, this could lead to near-zero short-term interest rates for the foreseeable future. While this is great for borrowers, the financial sector will once again be challenged, after only a few years reprieve from the last time interest rates were at the zero boundary. The Fed has shown they will go all-in to support the stock market and prevent another crisis-like event. The Fed is on the investors' side, and portfolios best positioned for the long term will benefit from the Fed's market-friendly policies.