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WealthManagement

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Market Insights

A periodic newsletter from Idaho Trust Bank

The U.S. economy suffered its worst period of economic growth ever in the second quarter. Economic output fell at its fastest pace on record as the coronavirus pandemic forced businesses across the United States to close their doors and kept millions of Americans shut in their homes for weeks. The collapse was unprecedented in its speed and severity. The only possible comparisons in modern American history came during the Great Depression and the demobilization after World War II, both of which occurred before the tracking of modern economic statistics.

Economic Activity

During the second quarter, Gross Domestic Product (GDP) sank 32.9% on an annualized basis, according to the Commerce Department's initial reading, which is subject to revision. It was the sharpest drop ever recorded. The report follows a first-quarter GDP decline of 5%. Sharp contractions in personal consumption, exports, inventories, investment and spending by state and local governments converged to bring down GDP, which is the combined tally of all goods and services produced during the period.

Consumer spending, which historically has accounted for about two-thirds of all activity in the U.S., subtracted 25% from the total, with services accounting for a

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majority of the drop. Spending shrank in health care and goods such as clothing and footwear. Inventory investment drops were led by motor vehicle dealers, while equipment spending and new family housing shrank as well.

Prices for domestic purchases, a key inflation indicator, fell 1.5% for the period, compared with a 1.4% increase in the first quarter. The Personal Consumption Expenditures (PCE) price index dropped 1.9% after rising 1.3% in the first quarter. Excluding food and energy, the "core" PCE prices were off 1.1%. However, during the second quarter, personal income soared, due in large part to government transfer payments associated with the coronavirus pandemic.

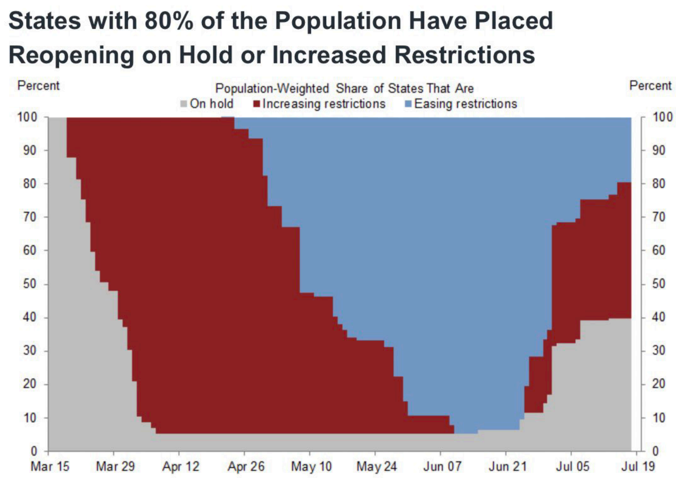
The economic figures are alarming but all self-inflicted with about half the quarter reflecting almost full shutdown in the economy and the second half reflect the slow reopening. Neither the Great Depression nor the Great Recession ever caused such a sharp drop over so short a period of time. By comparison, the worst quarter during the financial crisis of 2008 was the 8.4% GDP decline in the fourth quarter. (see chart above)

Unlike past recessions, this one was a result of a conscious decision to suspend economic activity to slow the spread of the virus. Congress pumped trillions of dollars into the economy to sustain households and businesses, limit long-term damage and allow for a rapid rebound. Initially, the plan worked, however, as cases have begun to increase in much of the country there appears to be a possible pullback in economic activity, reflecting consumer unease and renewed shutdowns.

So far, the unemployment rate peaked at 14.7%, a post-Depression high as workers across the country were told to stay home from any job not considered essential. This resulted in a near economic shutdown, which the National Bureau of Economic Research said resulted in a recession that started in February, a month before the pandemic declaration.

Jobless claims have started to rise again after falling for 15 weeks in a row. At the most recent reading, the number of Americans filing new claims for state unemployment benefits totaled 1.43 million, according to the Labor Department. It was the 19th straight week that the tally exceeded one million. It was the second weekly increase in a row after nearly four months of declines, a sign of how the rebound in cases has undercut the economy's recovery.

The $600 supplemental weekly unemployment payment from the federal government is ending, a potential financial blow to millions. Negotiations are underway to extend these government assistance programs but no deal has been finalized as of this writing. Fears are growing that after rebounding strongly in May and June, the economy has run out of steam, with many states reversing the reopening of businesses. (see chart to right)



Source: Goldman Sachs Global Investment Research

At its most recent meeting, the Federal Reserve Bank (Fed) made no changes to interest rates, but Chairman Jerome Powell said that economic growth is "well below" where it was before the pandemic. The Fed has signaled that it will keep rates near 0% though 2022 at a minimum.

Corporate Earnings

During the first half of 2020, analysts have lowered earnings estimates for companies in the S&P 500 for the year by 28.6%. This marked the largest decrease in the annual EPS estimate for the index over the first six months of the year in recent memory. The previous record was -24.4%, which occurred in the first six months of 2009, the beginning of the Great Financial Crisis. All 11 sectors experienced a reduction in their earnings forecasts for 2020, led by the Energy (-104.4%), Consumer Discretionary (-60.8%), and Industrials (-56.0%) sectors. One positive development is that the pace of the cuts to EPS estimates declined significantly in recent weeks.

Conclusion

The economic contraction experienced in the U.S. has been profound affecting many segments of the population. Many are hopeful that it will be short-lived and economies around the world will be back on a positive track in 2021. However, at this point, there remain many unknowns surrounding coronavirus, which is likely to keep volatility levels elevated over the next few months at a minimum.

S&P 500 Index

3 Month	12.87%
Year-to-Date	2.38%
1 Year	11.94%
3 Year	11.99%
5 Year	11.46%

MSCI EAFE Net Index

3 Month	10.42%
Year-to-Date	-9.28%
1 Year	-1.67%
3 Year	0.63%
5 Year	2.10%

Barclays Aggregate Bond Index

3 Month	2.61%
Year-to-Date	7.72%
1 Year	10.12%
3 Year	5.69%
5 Year	4.46%

As of 7.31.2020

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