John Dessauer Investments, Inc.

John Dessauer's market review and update as of Wednesday June 17, 2020

There is a little ray of sunshine breaking through the dark COVID-19 clouds. AstraZenica is doing human testing of a vaccine for the virus. And so is Johnson & Johnson. There are others including Glaxo Smith Kline and Pfizer that are also developing potential vaccines. All are also getting ready to manufacture hundreds of millions of doses once a vaccine is approved. Liberals need not worry. These giant pharmaceutical companies have pledged to do this on a not-for-profit basis. You can be sure that there will be substantial private donations as well as government assistance to make sure everyone will have access to the vaccine.

Meanwhile there are signs of a V-shaped early-stage U.S. economic recovery. It remains to be seen if the recovery can continue at this pace. A resurgence of virus infections could force more restrictive government actions that would slow the recovery. But the current situation is a strong indicator than once a vaccine is available the economy will likely bounce back strongly.

We know about the surprising, solid May job creation numbers. Data in early June indicate that the May strength is continuing. Department store sales in the week ended June 10 were above year-earlier levels, according to Facteus, which analyzes transactions by 16 million debit and credit card holders for banks. Grocery, discount, variety and general-merchandise stores all recorded sales above year-ago levels. Restaurants and hotels were still down in early June but not nearly as much as in April. Movie theaters, airlines and amusement parks, however, are still deeply depressed.

To be sure the economy overall is still depressed, and millions are still out of work. But the little ray of sunshine is shifting attitudes to a more positive outlook. For example, economists at Goldman Sachs estimate that consumer spending now stands at 90% of the pre-pandemic level, up from 74% at the mid-April bottom. The Goldman economists also say that manufacturing exports stabilized in May after slumping in March and April. Jan Hatzius, Chief Economist at Goldman Sachs, expects 'unprecedented' growth in the second half of this year. And economists at the Federal Reserve expect the U.S. economy to grow 5% next year - a growth rate not seen since 1984.

Last Thursday the Dow Jones Industrial Average plunged 1,800 points. Federal Reserve chairman Jerome Powell got most of the blame for the markets' sudden, steep and scary reversal. Following the June meeting of the Federal Open Market Committee Powell said: "We're not even thinking about raising interest rates." That followed statements that the Fed will keep interest rates near zero through at least 2022 and will increase bond buying to record levels.

Traders and some investors took Powell's comments to mean the economy was in much worse shape than they had believed. Why else would we need extremely low interest rates for so long with record Fed bond buying in addition? The answer as it turns out is the Fed is focused on the smooth functioning of financial markets, not just the level of economic activity. Markets froze in March, threatening a total financial collapse. The Fed came to the rescue in March and now wants to be sure that doesn't happen again. The pessimists' post Fed meeting siren calls were short lived. Bond markets quickly recovered and stabilized. The day after the Fed meeting, yields on 10-year treasury bonds dropped back below 0.7%.

Kevin Matras of Zacks Investment Research says profit taking was the main culprit in the one-day stock market plunge. He added: “Pullbacks are common. And healthy. Of course, they can seem scary when they’re big and fast. But pullbacks aren’t to be feared.”

In addition to Powell’s policy promises, fear of an outbreak of new virus cases played a role in the stock market’s plunge. Kevin Matras addressed those concerns, “But for context, it’s important to note that on a national level, overall case counts earlier this week rose just under 1%--which was the smallest increase since March.”

The members of the Federal Reserve Board and the regional Federal Reserve Bank presidents are all experienced professionals and well aware of the uncertainties surrounding COVID-19. They gather all the relevant data and formulate an economic outlook. Remember the pessimists’ predictions of a 20% unemployment rate that the media hyped just a few weeks ago? At the time, visions of an economy closed down for a long time made such notions seem plausible. The pessimists did not take into account the resilience of American business managers and their employees. COVID-19 is still a threat, but the U.S. economy is adapting. Thanks to the efforts of so many Americans the Fed board and regional presidents foresee an unemployment rate down to 9.3% by year-end, which would be a fantastic recovery. In addition to their 5% growth outlook for 2021 they see a growth rate of 3.5% in 2022, with a jobless rate of 5.5% in 2022.

The bad news is the cost of the fiscal stimulus response to the virus. Federal government revenues have collapsed, down 25% in May from a year earlier. Spending was up 36% in May. Unemployment insurance rose to $93 billion in May up from $2 billion a year ago. The Congressional Budget Office or CBO says the federal budget deficit from October to May reached $1.9 trillion or $1.17 trillion more than the same period in 2019. The deficits are likely to keep climbing as Congress keeps spending to counter the downward pull from the virus and the lock-downs.

There are signs that the economy will recover quickly and robustly, but still it will take years of solid growth to dig out from the virus budget hole. Let's hope voters will focus on the need for economic growth come the November elections.

I will have the next market review and update one week from today on Wednesday June 24, 2020.

All the best,

John Dessauer