Putting Market Activity Into Perspective

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With the 'unofficial' end of summer marked by the Labor Day weekend, the S&P 500 and NASDAQ have disappointingly fallen 7% and 10%, respectively, over the last three days. Throughout this recent pullback, it has been the sectors with the strongest year-to-date returns that have led the decline. Pullbacks within the equity market are always unsettling, so below are ten points to put the recent decline into perspective and, hopefully, reduce investors' elevated levels of anxiety.

1. *First Three Consecutive Daily Declines in Three Months*

It is unusual for the equity market to move up in an uninterrupted, straight line. In fact, this recent three-day pullback marked the first three consecutive day decline since June 11 and only the second since March 10. Over the last ten years, it is common to see the equity market exhibit short bouts of volatility like this. In fact, on average, the S&P 500 typically has ~10 individual periods of three consecutive days of declines over a six-month time period (that is almost twice a month). Volatility is part of the fabric of the market.

2. *Back to Levels of One Month Ago*

Despite the S&P 500's 7% decline over the past three days, it sits at the levels we saw just one month ago! Additionally, the S&P 500 and NASDAQ are up 3% and 21%, respectively, year-to-date. Both were at record highs just one week ago.

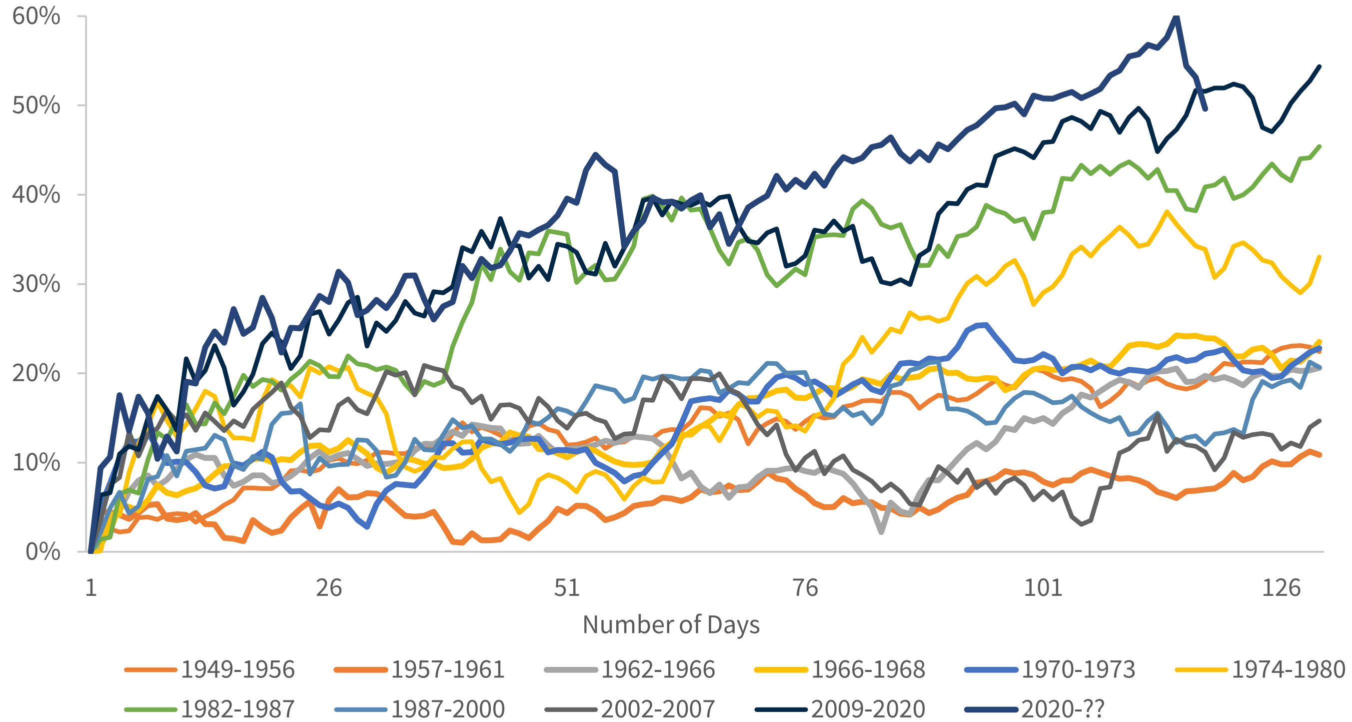
3. *Still the Second Strongest Bull Market at this Juncture*

Even with the recent weakness, the S&P 500 remains up ~50% off of the lows on March 23. This marks the second strongest start to a bull market at this juncture (117 days) on record, just below the record of 52% in 2009.

4. *Best Summer Since 2009*

Even with the recent pullback, the S&P 500 posted the best summer return (up 16% from Memorial Day to Labor Day) since 2009 and the second best over the last 50 years. This reflects how strong the recent momentum in the market has been despite continued COVID and political uncertainties.

Second Strongest Bull Market at This Juncture



Source: FactSet, as of 9/8/2020

5. *September Is the Weakest Month*

On an historical basis, September (particularly during an election year) has been the weakest month of the year, on average. While volatility tends to increase during September and October, the market pullbacks, on average, tend to be relatively contained and offset by a rally in November and December.

6. *Pullbacks Are Normal*

Not only have we rallied strongly and very quickly, it is not uncommon to see pullbacks in a given year. In fact, over the last 30 years, the market typically experiences approximately four 5% or more pullbacks a year, on average. Year-to-date, this is the third.

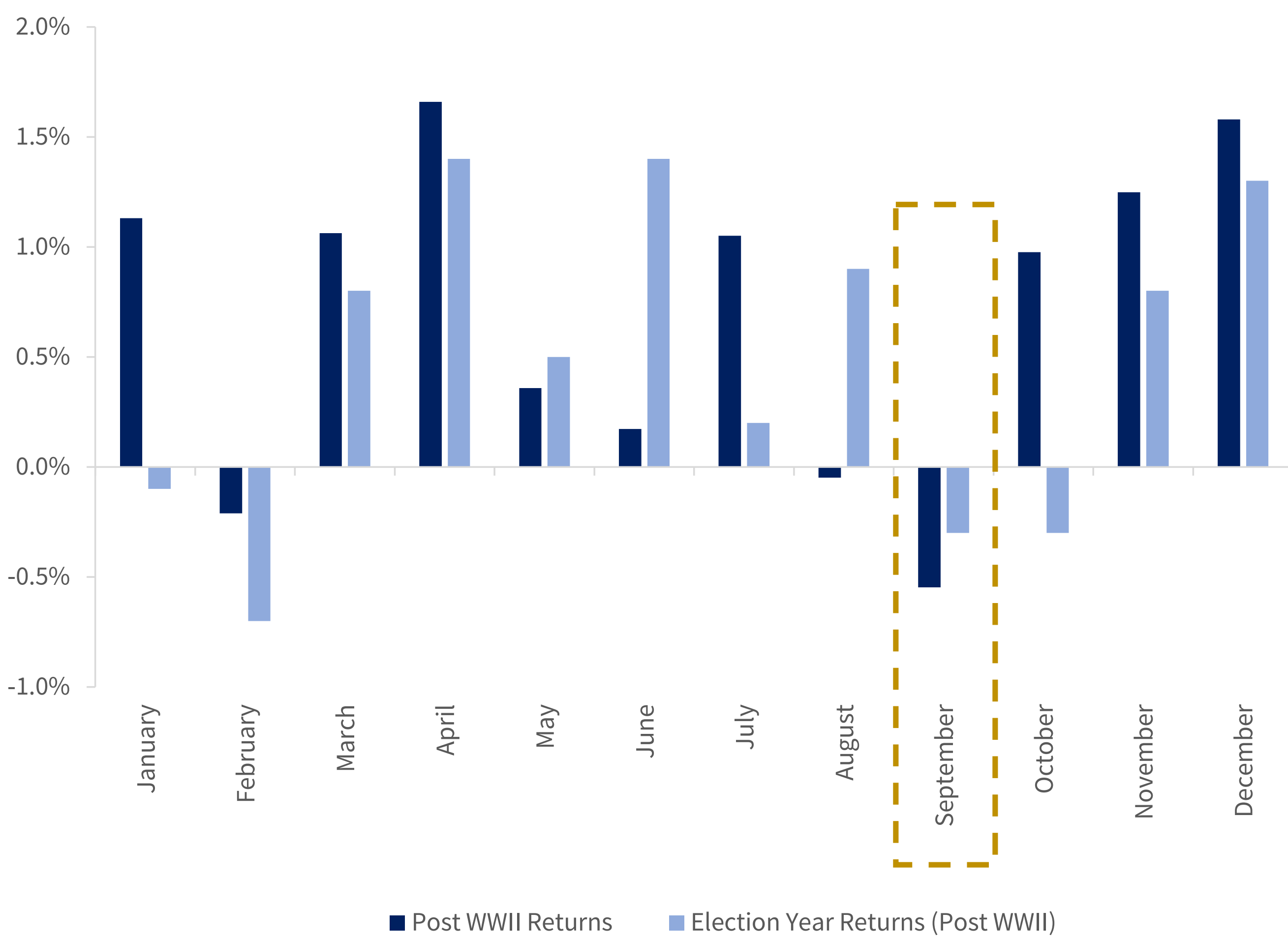
7. *Improving Economy*

Evidenced by both the improving labor market report (1.4 million jobs added and unemployment rate falling to 8.4%), and a strong ISM reading (the new orders subcomponent rose to the highest level since 2004) last week, the US economy continues to recover from the COVID-driven weakness. We forecast 3Q US GDP to rebound and grow ~30% and improving economic activity should remain supportive for the US equity market.

8. *Continue to Believe in a Phase 4 Package*

As both political parties continue to jockey around a Phase 4 stimulus package, our Washington Policy Analyst, Ed Mills, believes that there will be an agreement. Further fiscal stimulus (particularly targeting the consumer) should be supportive of both consumer spending and the equity market.

September Is the Weakest Month



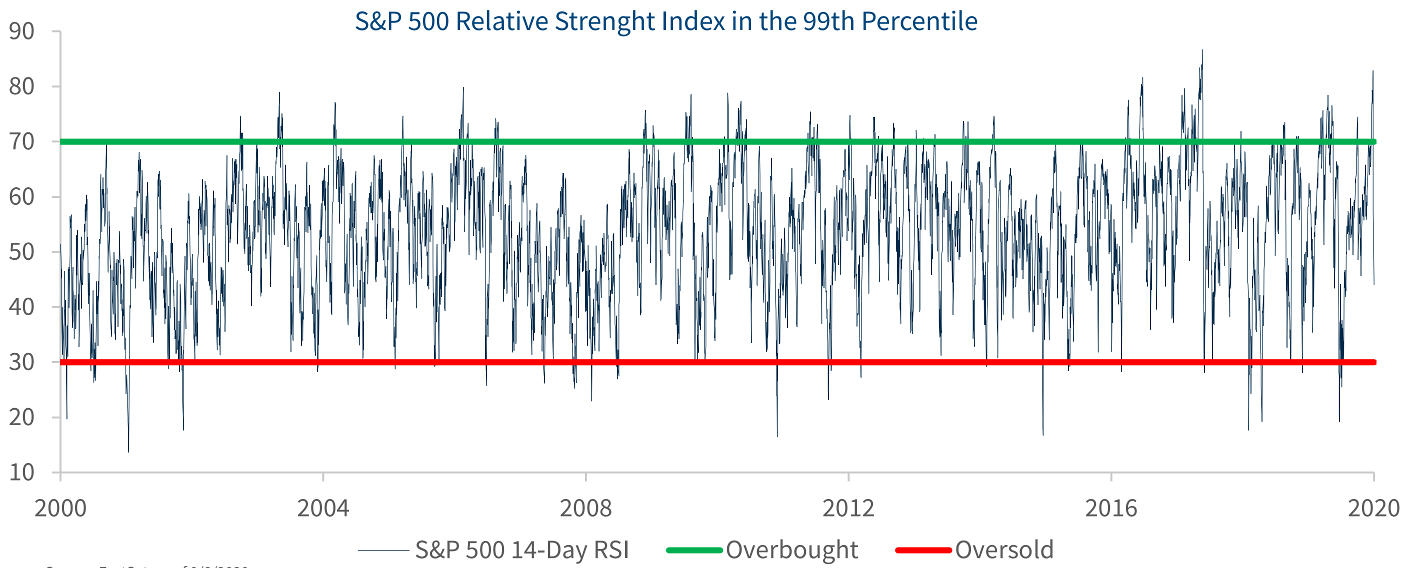
Source: FactSet, as of 9/8/2020

9. *Improving Earnings*

While earnings expectations had been slashed following the COVID-driven crisis, earnings throughout the second quarter came in significantly better than expectations. Going forward, we expect earnings to continue to improve as full-year 2020 and 2021 Earnings Per Share (EPS) expectations continue to move higher. Our S&P 500 2021 earnings forecast is ~$160, with room for upside.

10. *US Equities Remain Technically Sound*

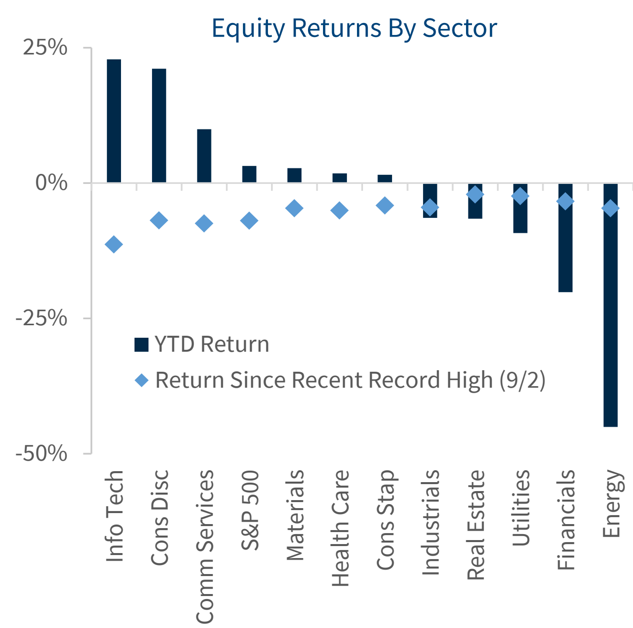
Despite the recent pullback, US equities remain above both their 50-day (3,305) and 200-day (3,094) moving averages. Technicians will look for these to remain levels of support. Staying above these moving averages will continue to portray a technically sound equity market. From a sentiment perspective, there were several technical indicators that suggested the equity market was 'overbought' and in need of a consolidation period. For example, given the rally before the recent pullback, put/call ratios moved to multi-year lows (showing investors becoming complacent) and the 14-day Relative Strength Index (RSI) rose to the highest level in 2.5 years and moved into the 99th percentile over the last 30 years.



Source: FactSet, as of 9/8/2020

Bottom Line:

Given how far and fast the equity market had rallied, it is not surprising to experience a period of consolidation and digestion. Given that valuations on both a trailing and forward basis remain near multi-year highs, the market was priced to perfection and susceptible to disappointments. Near term, equities are likely to remain volatile with the potential for further weakness due to the uncertain timing for a potential COVID vaccine, fiscal relief deliberations, the upcoming presidential election and burgeoning tensions with China. However, the trajectory for US equities is higher over the next 12 months (12-month target 3,600) as a result of improving global economic activity, recovering earnings and still supportive fiscal and monetary policy. As a result, we believe that long-term investors should continue to use periods of weakness as buying opportunities to add to our favorite sectors (Information Technology, Communication Services, Health Care and Consumer Discretionary).



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