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Market Commentary

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By

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At the end of 2019, the market was at all-time highs, closing the year at $3,231, up 31.5% for the year. All seemed wonderful, but as I noted then, there was reason for concern. Earnings, the source of long-term growth in the market, did not increase in 2019. The entire rise in 2019 was due to valuation. The market's price/earnings multiple had risen from 14.6x to 18.8x, which is a very high valuation, historically speaking. Without a significant increase in earnings, I thought it would be tough to maintain that valuation level. Thus, my outlook was for a slight decrease in the market. The risks that I noted were (1) high valuations, (2) trade issues with China and (3) a contentious presidential and congressional elections.

We were priced for a strong economy. We certainly don't have that now. It's obvious that we are in a severe recession, due to the social distancing required to stop the coronavirus spreading around our cities, our country and the world. Corporate earnings will be down sharply, and tough to predict with the travel, restaurant and entertainment industries largely shut down, higher costs in health care, continued pressure on brick & mortar retailers, drastically lower oil prices in the energy sector and coming write-downs and write-offs from companies across the market.

I'm not an epidemiologist, or a scientist, but I am a great believer that those who are will solve this health care crisis. Therapies and vaccines are coming. Of those who get the virus, most all will survive as their immune system will build up antibodies, which should allow them to return to work and/or assist in fighting the virus. We must do all we can to help save those with serious and life-threatening reaction to the coronavirus. We grieve those who are and will be lost to this disease. My guess is that the worst of the pandemic will be over by June, and by then we will be able to see the end of this scourge.

Fiscal and monetary policy are firmly behind the economy and will help consumers and businesses weather this global economic contraction. Business leaders have been quick to respond. When this ends, the economy will be a bit different, with more emphasis on working-from-home and distance learning, more reliance on the internet, a stronger health care system with added resources. But the economy will be stronger.

My earnings estimate for the S&P 500 for 2021 is $185, which would be 4.5% annual growth over the three years from 2018, below the long-run average of 7% growth. By September, the market should be focused on 2021 earnings. With the continued low interest rate environment, a price/earnings ratio of 17.5x can be supported which would yield a price target of $3,240, up 27% from the March 27th close of $2,541.

It will likely be a bumpy ride, with tough news on the medical front and social distancing lasting longer than anybody wants. But the economic recovery should be powerful and quick. We look forward to ending 2020 on a higher, stronger note.

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Information obtained through Zacks Investment Research—www. zacks.com

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