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Week in Review

June 22, 2020

LAST WEEK IN REVIEW

Stocks recorded gains and erased part of the previous week's steep declines. The technology-heavy Nasdaq Composite Index fared best and briefly moved close to the all-time intraday high it established on June 10. Energy stocks led the rebound, helped by signs that major oil-exporting nations were adhering to previously agreed on production cuts as well as optimism for increased global demand. Health care and materials stocks also outperformed, while Boeing and airline stocks were especially strong early in the week, boosted by reports of a resurgence in air travel. The small real estate and utility sectors lagged.

The week ended on a volatile note due in part to Friday's "quadruple witching"—the simultaneous expiration of four types of options or futures contracts, which occurs once each quarter. Traders I spoke with noted that the rebalancing of the S&P 500 Index and several other benchmarks were also likely to result in elevated volumes and price movements.

Stocks had a poor start to the week, as concerns over the worsening of the pandemic in several states, as well as a new outbreak in Beijing seemed to continue weighing on sentiment. The market then rebounded late Monday following the Federal Reserve's announcement that it will begin buying a broad portfolio of U.S. corporate bonds (bye-bye price discovery). The purchases will be made by the Fed's Secondary Market Corporate Credit Facility, an emergency lending program that, to date, has purchased only exchange-traded funds through Blackrock.

On Tuesday and Wednesday, Fed Chair Jerome Powell testified before Congress and urged that recent monetary stimulus be paired with more fiscal support. While no definite plans have yet to emerge, traders noted that reports of a USD 1 trillion infrastructure plan being prepared at the White House seemed to support sentiment further. Markets also seemed to get a lift from a study showing that a common steroid drug, dexamethasone, helped save lives in serious COVID-19 (the disease caused by the coronavirus) cases. This drug marks the first treatment for having a demonstrable impact on reducing the fatality rate.

U.S. - MARKETS & ECONOMY

The week's economic data offered mixed signals as to whether the economy will be able to manage a "V-shaped" recovery. On Tuesday, the Commerce Department reported a 17.7% surge in retail sales in May, better than double consensus expectations and the biggest gain in history—albeit one measured against the 23.3% cumulative decline over the previous three months. Labor market data disappointed, however. Weekly jobless claims fell less than expected, and continuing claims remained elevated at over 20.5 million. A gauge of current manufacturing activity in the mid-Atlantic region surprised dramatically on the upside, indicating considerable expansion instead of continued contraction, but overall industrial production in May rose less than expected.

US STOCKS – As of close Friday, June 19, 2020

Index	Friday's Close	Week's Change	% Change YTD
DJIA	25871.46	266.92	-9.35%
S&P 500	3097.92	56.61	-4.11%
Nasdaq Composite	9946.12	-357.31	10.85%
S&P MidCap 400	1789.96	37.58	-13.24%
Russell 2000	1420.90	33.22	-14.84%

Source: Bloomberg. This chart is for illustrative purposes only and does not represent the performance of any specific security. **Past performance cannot guarantee future results.**

US YIELDS & BONDS

Treasury bond yields ended the week roughly unchanged. (Bond prices and yields move in opposite directions.) The broad municipal debt market marginally outperformed Treasuries through most of the week, and traders I spoke with noted that new municipal issuance was elevated, both in terms of overall size and number of deals. Demand for new issues was strong across all sectors, including the first deal from the beleaguered life-care sector since before the pandemic. Industrywide flows into municipal bond funds continued to trend higher. According to Lipper, muni bond mutual funds experienced inflows of USD 2.8 billion for the week ended June 10.

Investment-grade corporate bond credit spreads (the additional yield offered over Treasuries), moved tighter after the Fed announced that it would begin buying individual corporate bonds to supplement its purchases of exchange-traded funds. However, traders noted that spreads moved wider as the week progressed amid increased selling to fund purchases in the primary market. The volume of new deals was well above expectations.

Traders also reported that news of the Fed's expanded bond-buying program was supportive of the performance of high yield bonds. This support was particularly true of issues from Ford and other "fallen angels"—companies that have recently lost an investment-grade rating (not to mention helping zombie companies). While the robust retail sales numbers also fostered positive sentiment toward risk assets, the high yield market struggled somewhat to absorb a large volume of new deals.

US TREASURY MARKETS AND WEEKLY YIELD CHANGE – As of close Friday, June 19, 2020

3 Mth: Flat bps to 0.15%

2-yr: +0.1 bps to 0.19%

5-yr: Flat bps to 0.33%

10-yr: -0..01 bps to 0.69%

30-yr: Flat bps to 1.46%

SOURCE: BLOOMBERG. YIELDS ARE FOR ILLUSTRATIVE PURPOSES ONLY AND DOES NOT REPRESENT THE PERFORMANCE OF ANY SPECIFIC SECURITY. YIELD CHANGES ARE OF ONE WEEK. PAST PERFORMANCE CANNOT GUARANTEE FUTURE RESULTS.

INTERESTING NEWS OVERSEAS

Equities in Europe ended the week higher, supported by stimulus efforts and the reopening of critical economies. However, a resurgence of COVID-19 cases in the U.S. and China cast doubt on a quick recovery and hindered the advance. The pan-European STOXX Europe 600 Index ended the week 3.31% higher, while Germany's Xetra DAX Index climbed 3.51%, France's CAC 40 Index added 3.23%, and Italy's FTSE MIB Index advanced 3.99%. The U.K.'s FTSE 100 Index rose 2.93%.

Core Eurozone bond yields were mixed on the week. Yields edged up following the Federal Reserve's move to buy corporate debt, reducing demand for safe-haven assets. However, yields declined later in the week after it emerged that eurozone banks had borrowed a record EUR 1.31 trillion under the European Central Bank's targeted longer-term refinancing operations (TLTRO). The Fed announcement and TLTRO uptake put downward pressure on peripheral eurozone bond yields, which fell markedly on the week. Meanwhile, the German 10-year bund yield was trading at -0.41% on Friday, up slightly from Monday's -0.46%. The Italian 10-year yield traded at 1.35% on Friday, compared with Monday's 1.41%.

Like the Fed, the Bank of England (BoE) enlarged its bond-buying program by GBP 100 billion and left its key interest rate at a record low of 0.1%. It also said it would slow the rate of purchases and expected to meet the new target of GBP 745 billion by the end of the year. However, the language in the Monetary Policy Committee meeting minutes was on the hawkish side, pointing to a faster recovery than previously expected while acknowledging that unemployment could remain high for some time. Futures markets indicated that traders no longer expect negative interest rates in the U.K. through the end of 2021.Stocks in Japan produced small gains for the week. The Nikkei 225 Stock Average advanced 173.31 points (0.78%) and closed at 22,478.79. The widely watched benchmark has made up much of the ground lost in February and March but remained down about 5% for the year-to-date period. The TOPIX Small Index was up 1.6% for the week, outperforming both the Nikkei and the large-cap TOPIX Index.

The global sentiment seemed to be the most significant driver of Japanese markets, as hopes for a robust economic recovery and news of additional stimulus measures from the U.S. Federal Reserve narrowly outweighed fears of a resurgence of the coronavirus in China and the U.S. Data showing a sharp drop in exports also weighed on Japanese stocks. Japan's Finance Ministry reported that the country's exports declined 28.3% year over year in May as the coronavirus impacted global demand. Vehicle exports dropped by more than 60% during the period, and total Japanese exports to the U.S. also fell by about half. Reuters reported that the monthly decline—the largest since the global financial crisis—was worse than consensus expectations.

Lastly, China's domestic large-cap index, the CSI 300 Index, gained 2.4% for the week, outpacing the 1.6% advance in the country's benchmark Shanghai Composite Index. The gains in Chinese stocks came despite a reported surge in new COVID-19 cases in Beijing over the June 13 weekend, highlighting the risk of a second wave of infections. In response, Beijing returned to tight movement restrictions, though not a complete lockdown, after the new cases were traced to a wholesale food market. Despite fears of another wave, public health experts believe that China will be able to better manage a resurgence in infections, given the country's extensive experience in battling the coronavirus.

On the political front, a meeting between U.S. Secretary of State Mike Pompeo and Chinese Politburo member Yang Jiechi in Hawaii, the first high-level U.S.-China talks this year, was described as constructive. Less pleasing for China, however, was President Donald Trump's signing on Thursday of the Uighur Human Rights Policy Act, which authorizes sanctions against Chinese officials involved in the mass detention of Muslim minority groups in Xinjiang Province.

THE WEEK AHEAD

The U.S. will be publishing the final estimate of first-quarter GDP on Thursday. Early estimates suggested the economy shrank by an annualized 5.0 percent in the first three months of the year, the most since the last quarter of 2008, as several states were forced to impose lockdown measures from mid-March in response to the coronavirus pandemic. Meanwhile, durable goods orders in May are seen rebounding from the steepest fall in nearly six years the month before.

Other notable publications include: flash Markit PMI survey; personal income and outlays; PCE price index; existing and new home sales; Chicago Fed National Activity Index; the advance estimates of goods trade balance and wholesale inventories; and the final reading of Michigan consumer sentiment.

Other key data to watch for in America include Canada's average weekly earnings; Mexico retail sales, economic activity, and trade balance; Brazil's current account and business morale; and Argentina's first-quarter GDP figures and unemployment rate. The central bank of Mexico will be deciding on monetary policy on Thursday.

Call us at LCP if you have any questions. Have a great week!

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