WEEKLY MARKET UPDATE, AUGUST 17, 2020

GENERAL MARKET NEWS

• Last week's heavy supply certainly affected the long end of the curve, as the 10-year Treasury yield moved from a historical low of 0.50 percent to 0.72 percent. (It opened at 0.69 percent on Monday.) The 30-year, which was at 1.18 percent last week, spiked and opened at 1.43 percent on Monday. The 30-year seems to have created a floor around 1.20 percent over the past five months, as it has not approached the historical low of 0.997 percent it set in March 2020. The 2-year, which opened the month at a steady 0.11 percent, backed up to 0.16 percent last week and opened at 0.14 percent on Monday.

• Last week's rally was driven by the industrials-oriented Dow. The Nasdaq, which had been leading much of the recovery, lagged as cyclical sectors, such as industrials, consumer discretionary, and energy, were among the top performers. Financials also had a strong week, outperforming utilities, real estate, communication services, and technology, all of which lagged. In the past month, we've seen strength in sectors that may benefit from reopening efforts. Technology led through the early part of the rebound, and it remains to be seen which sectors will benefit as schools and businesses look to cautiously reopen in the fall. Two major questions are looming: what will a second round of stimulus payments look like, and when might it occur?

• On Tuesday, July's Producer Price Index report was released. This measure of producer inflation rose by 0.6 percent against forecasts for a 0.3 percent increase. This brought producer prices down 0.4 percent on a year-over-year basis. Core producer inflation, which strips out the impact of volatile food and energy prices, also came in above expectations, increasing by 0.5 percent against forecasts for a 0.1 percent increase. Nonetheless, the deflationary pressure created by anticoronavirus measures earlier in the year continues to keep inflation muted year-over-year.

• Wednesday saw the release of the Consumer Price Index for July. Consumer inflation grew by 0.6 percent against expectations for a more modest 0.3 percent increase. This brought year-over-year consumer inflation to 1 percent, up from 0.6 percent in June. Core consumer inflation, which strips out the impact of food and energy prices, also increased by 0.6 percent during the month, against calls for a 0.2 percent increase. This was the largest monthly increase for core consumer prices since 1991; however, as was the case with producer prices, the declines earlier in the year helped keep inflation constrained year-over-year. Given the continued stress on the labor market, the Federal Reserve (Fed) is not expected to react to rising inflation until the employment picture improves considerably.

• On Friday, July's retail sales report was released. Sales were mixed, with headline retail sales increasing by 1.2 percent against expectations for a 2.1 percent increase. Core retail sales, which exclude the impact of volatile auto and gas sales, increased by a solid 1.5 percent against expectations for 1 percent growth. Sales staged an impressive rebound in May and June once reopening efforts began, and this continued growth in sales in July was another positive sign that consumers were willing and able to spend. Despite July's slowdown in the pace of sales growth compared with May and June, this was still an encouraging report, given that both major measures of consumer confidence fell during the month, which typically serves as a headwind for sales growth.

• Finally, we finished the week with the preliminary estimate of the University of Michigan consumer sentiment survey for August. This measure of consumer confidence increased from 72.5 in July to 72.8 in August, against calls for a decline to 72. This better-than-expected result helped the index avoid testing the recent low of 71.8 it hit in April. Rising case counts and slowing reopening efforts caused consumer confidence to decline in July, but progress in containing local outbreaks in the beginning of the month helped bolster consumer sentiment. Typically, improving consumer confidence supports faster consumer spending growth, so this was an encouraging report that should help support additional consumer spending in August.

WHAT TO LOOK FORWARD TO

We started the week with Monday's release of the National Association of Home Builders Housing Market Index for August. This measure of home builder confidence increased by more than expected during the month, rising from 72 in July to 78 in August, against calls for a more modest increase to 74. (This is the second straight month in which home builder confidence beat expectations, as the index jumped from 58 in June to 72 in July.) This better-than-anticipated result eclipsed the record high the index reached in 1998. Home builder confidence has been boosted by record-low mortgage rates that have been driving additional prospective home buyers into the market since reopening efforts started in May. After the index reached a seven-year low of 30 in April, we've seen a swift recovery in home builder confidence that has supported a rebound in new home construction.

Speaking of new home construction, Tuesday will see the release of July's building permits and housing starts reports. Both permits and starts are expected to show continued growth during the month, with permits and starts slated to rise by 5.9 percent and 3.7 percent, respectively. If estimates hold, they would bring the pace of new home construction to levels last seen in the first half of 2019. Still, even with anticipated increases for permits and starts, the pace of new home construction would be down nearly 24 percent from its recent high, set in February. So, the results for July are likely to highlight the long road back to pre-pandemic construction levels.

On Wednesday, the Federal Open Market Committee will release the minutes from its July meeting. The committee did not change policy at this meeting, voting unanimously to keep the federal funds rate at virtually zero. These minutes are expected to provide more insight into how Fed members viewed rising case counts in July, as the meeting took place while counts were rising notably in several states. Several members have noted one of the major risks to their economic outlook is the uncertainty created by the pandemic, so it will be interesting to see how the Fed reacted to the worsening public health picture in July. The minutes could also contain hints regarding the types of additional stimulus Fed members prefer, if further economic support is needed. Increased asset buying and forward guidance are two of the potential solutions expected to have been considered.

On Thursday, the weekly initial jobless claims report for the week ending August 15 is set to be released. Economists expect to see 990,000 initial unemployment claims during the week, which would be a modest increase from the 963,000 claims the previous week. This report will be an important test for the labor market, as a better-than-expected result here would be further evidence that headwinds created by rising cases in July are dissipating in August. But, even if initial claims beat expectations, they will likely remain well above historical norms, highlighting the possibility of a long road ahead before employment numbers return to pre-pandemic levels. We'll continue to monitor this important weekly release until unemployment claims are closer to historically average levels.

We'll finish the week with Friday's release of July's existing homes sales report, which is expected to show an increase of 14.4 percent during the month, following a strong 20.7 percent rise in June. If estimates hold, they would bring the pace of existing home sales to virtually the same level we saw in July 2019, highlighting this indicator's swift rebound following reopening efforts. Record lows in mortgage rates have been the major driver of rising housing sales. Rates continued to fall in July, so they should help boost growth in housing sales. Nonetheless, despite the improvement we've seen and the anticipated increase in July, if estimates prove accurate, existing home sales would be down more than 17 percent compared with February's recent high. This report will likely highlight the work that needs to be done in this sector.

Equity Index	Week-to-Date	Month-to-Date	Year-to-Date	12-Month
S&P 500	0.69%	3.20%	5.66%	20.75%
Nasdaq Composite	0.09%	2.61%	23.53%	43.26%
DJIA	1.87%	5.82%	–0.68%	11.78%
MSCI EAFE	2.46%	4.46%	–5.23%	8.19%
MSCI Emerging Markets	0.39%	1.39%	–0.36%	16.14%
Russell 2000	0.59%	6.66%	–4.62%	9.55%

Source: Bloomberg

Fixed Income Index	Month-to-Date	Year-to-Date	12-Month
U.S. Broad Market	–0.91%	6.85%	6.79%
U.S. Treasury	–1.03%	8.67%	7.01%
U.S. Mortgages	–0.14%	3.68%	4.83%
Municipal Bond	–0.31%	3.96%	3.89%

Source: Morningstar Direct

Disclosures: Certain sections of this commentary contain forward-looking statements that are based on our reasonable expectations, estimates, projections, and assumptions. Forward-looking statements are not guarantees of future performance and involve certain risks and uncertainties, which are difficult to predict. All indices are unmanaged and are not available for direct investment by the public. Past performance is not indicative of future results. The S&P 500 is based on the average performance of the 500 industrial stocks monitored by Standard & Poor's. The Nasdaq Composite Index measures the performance of all issues listed in the Nasdaq Stock Market, except for rights, warrants, units, and convertible debentures. The Dow Jones Industrial Average is computed by summing the prices of the stocks of 30 large companies and then dividing that total by an adjusted value, one which has been adjusted over the years to account for the effects of stock splits on the prices of the 30 companies. Dividends are reinvested to reflect the actual performance of the underlying securities. The MSCI EAFE Index is a float-adjusted market capitalization index designed to measure developed market equity performance, excluding the U.S. and Canada. The MSCI Emerging Markets Index is a market capitalization-weighted index composed of companies representative of the market structure of 26 emerging market countries in Europe, Latin America, and the Pacific Basin. The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The Bloomberg Barclays US Aggregate Bond Index is an unmanaged market value-weighted performance benchmark for investment-grade fixed-rate debt issues, including government, corporate, asset-backed, and mortgage-backed securities with maturities of at least one year. The U.S. Treasury Index is based on the auctions of U.S. Treasury bills, or on the U.S. Treasury's daily yield curve. The Bloomberg Barclays US Mortgage Backed Securities (MBS) Index is an unmanaged market value-weighted index of 15- and 30-year fixed-rate securities backed by mortgage pools of the Government National Mortgage Association (GNMA), Federal National Mortgage Association (Fannie Mae), and the Federal Home Loan Mortgage Corporation (FHLMC), and balloon mortgages with fixed-rate coupons. The Bloomberg Barclays US Municipal Index includes investment-grade, tax-exempt, and fixed-rate bonds with long-term maturities (greater than 2 years) selected from issues larger than $50 million.

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