Great-West Investments Capital Markets Perspective

Week in Review: July 27th – August 2nd

INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD
Dow Industrials	Lg. Cap Eq.	26,428.32	-0.2%	-7.4%
S&P 500®	Lg. Cap Eq.	3,271.12	1.7%	1.2%
NASDAQ Comp.	US Equity	10.745.27	3.7%	19.8%
Russell 2000®	Sm. Cap Eq.	1,480.43	0.9%	-11.3%
Stoxx 50	Europe Eq.	3,174.32	-4.1%	-15.2%

INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD
FTSE 100	UK Equity	5,897.76	-3.7%	-21.8%
Nikkei 225	Japan Equity	21,710.00	-4.9%	-8.2%
EEM:US	Emkt. Equity	$43.29	0.3%	-3.5%
EFA:US	Non-US Equity	$62.05	-1.9%	-10.6%
UST 10y (yield)	US Treasury	0.53%	-0.05%	-1.39%
B/Barc AGG	Fixed Inc.	2,395.60	0.25%	7.67%

Last week's notable economic releases were jam-packed with economic data, earnings, and another round of jobless claims, as we received our first glimpse of how COVID-19 has impacted the economy in the second quarter. Simply put, second quarter GDP plunged by 32.9% between April and June on an annualized basis -- which is, by far, the most severe contraction on record. Amazingly enough, the figure actually came in above economist estimates, who were forecasting a drop of 34.7%. Though this annualized figure was widely expected, by comparison, the worst GDP drop seen during the Great Financial Crisis in 2008 was an 8.4% GDP drop in the fourth quarter of that year, which by then had seen both crises unfold for Bear Sterns and Lehman Brothers, and a continuation of mortgage defaults among residential borrowers.

Digging into the details associated with the drop in GDP, Personal consumption -- which represents a significant metric that drives the U.S. economy -- subtracted roughly 25% from the Q2 total, with services accounting for nearly all of that drop[1]. On the flipside, personal income soared – which is largely being attributed to government transfer payments associated with the pandemic. It's difficult to tell how this will all play out as we make our way through the second half of the year – the resurgence of the first wave (or second wave) may yet bring us some further economic impacts.

Weekly Jobless Claims were also released on Thursday in tandem with second quarter GDP data, and claims continue to stack up. The report came in with another rise to 1.434 million claims, which marks the 19th week in which claims totaled at least 1 million, and second consecutive week of rising claim count. This was an unexpected upward trend, which could be a residual effect of certain areas of the country that have been going back into lockdown as case counts continue to spike.

Despite a downward trend in jobless claims since the initial spike that occurred in March, continuing jobless claims came in at 17 million in the most recent reading, -- and has ticked up slightly, holding relatively steady since declining from over 24 million in March. This reading is a bit out of step with the rest of the market, as equities continue to surge forward and try to hold on to gains despite the prospect of a prolonged economic recovery.

[1] www.CNBC.com

On Friday, we got a glimpse of how personal incomes and spending are trending, as well as a read on consumer sentiment, which wound up as a bit of a mixed bag. Personal incomes fell more than expected in June, declining 1.1% from the prior month, as the effects from the one-time stimulus checks that arrived in people's bank accounts during the second quarter dissipated. Consumer spending increased 5.6% in June, as after having a record jump in May. Consumer sentiment posted a decline in July, with the final reading sliding to 72.5 as of the end of the month, falling from 78.1 at the end of June.

It would appear that sentiment towards outlook remains cautious, and even negative, as virus cases continue to surge in the US and congress is at an impasse in negotiating the next phase of the CARES act, with unemployment benefits expiring on Friday. This has been a crucial portion of keeping the economy afloat as consumers had reigned in spending when the virus resulted in a good portion of the country being locked down in mid-March and April/May. By all accounts, this data shows, at best, a murky, and perhaps disappointing picture of the economy going forward.

China manufacturing PMI figures, which measures the prevailing direction of economic trends in manufacturing, were also released on Friday, and came in at 52.8 from 51.2 in June[2] – showing a strong rebound, and also notching the fastest pace of expansion in nearly a decade. This is in line with China's narrative that they are experiencing economic recovery, after second quarter GDP grew by 3.2%, after contracting 6.8% in the first quarter due to the Coronavirus outbreak. China has been highly effective at containing the virus after the initial outbreak and subsequent lockdown of Wuhan and several other areas within the country.

On Monday morning, we received U.S. ISM manufacturing data, which measures manufacturing trends across orders and production, supplier delivery, raw materials inventory, and materials pricing. July's reading recorded the fastest pace of expansion since March 2019 – coming in at 54.2 last month, from 52.6 the month prior[3]. The data are pointing to steadier footing for producers – however, the recovery picture is still very much up in the air as we go into the fall season, which brings flu season along with it. This will be a key metric to monitor going forward as a gauge of productivity – manufacturing has experienced a strong rebound, but investors will likely not be too accommodating to a declining read over the next few months.

On Wednesday, we received the Federal Open Market Committee rate decision and Chairman Powell's press conference, which reiterated the FOMC's dovish posturing and continued commitment to use its full range of tools to support growth amid the fallout from the virus. Powell did acknowledge that recent economic data has indeed gotten worse, and that the outlook is highly uncertain – the only constant going forward appears to be a pledge to keep rates near zero for as long as necessary to help the United States economy recover.

The backdrop of uncertainty has certainly been apparent during earnings season, though results have largely been much better than expected, with a handful of technology companies leading the market with favorable earnings from the second quarter. On Thursday, we had Apple, Facebook, Alphabet (formerly Google) and Amazon release their earnings which have been much anticipated in light of the pandemic. Along with Microsoft's earnings, released a week earlier, all companies have logged at least 6% increases in revenue over the first half of 2020 compared to 2019, with Amazon logging a 34% increase in revenues among their lines of business. All companies beat estimates, even with Google logging a sales drop due to a slowdown in ad-spend related to the pandemic, though this was lower than analyst estimates[4].

Despite a large number of beats within reported earnings in the S&P500 index, here are pockets within the market exhibiting weaker recoveries – namely within apparel and restaurants, but also energy. Exxon Mobil and Chevron reported lackluster earnings on Friday, missing analyst estimates by a fairly wide margin. While losses in energy, and particularly within drilling, were expected, the magnitude and severity of the drop in the price of oil due to lack of demand is being felt at two of energy's giants. Exxon Mobil saw revenues plummet, reporting $32.6B vs analyst estimates at 36.08B – which reflected a 47.8% expected decline year over year. Chevron also had a difficult

[2] https://www.markiteconomics.com/Public/Home/PressRelease/735f017c129749aaa031566e4a325581
[3] https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/pmi/july/
[4] Bloomberg.com

quarter, after seeing revenue plunge 65% year over year to $13.49B. Both companies continue to see unfavorable conditions going forward, as demand for oil remains largely depressed globally amid the pandemic[5]. With less than 100 days to go until national elections on November 3rd, it is likely that volatility is here to stay for some time, though 2020 has been no stranger to sharp market moves. As we get closer and closer to Election Day, it's likely that both Republicans and Democrats will start to ramp up rhetoric, as candidates offer up their policy ideas and priorities going forward. Election cycles typically are no stranger to increased volatility, and this time around is sure to be no different.

What to Watch This Week: August 3rd – 9th

What to Watch (August 3rd – 7th)

Monday: Markit Manufacturing PMI, ISM Manufacturing Index

Tuesday: Factory Orders

Wednesday: ADP Employment Report, Trade Deficit, Markit Services PMI

Thursday: Jobless Claims, Continuing Claims

Friday: Nonfarm payrolls, Unemployement Rate, Wholesale Inventories

This next week, we will get a glimpse of factory order data, monthly trade deficit, and more jobless claims/continuing claims data. We will also get a glimpse of wholesale inventories that will give us an idea of whether or not consumers are ramping back up their spending habits, and nonfarm payrolls will also be released on Friday. We will also continue to receive earnings from companies all over the market, with nearly 1000 companies reporting on Wednesday and Thursday.

Payrolls will continue to be one of the biggest releases on the street, and continues to give us a glimpse of the economic recovery in a post-COVID world. While jobless claims have been trending downwards since March, continued claims have largely plateaued and registered a slight uptick last week. These two datasets are critical for understanding the whole picture of the economic recovery going forward, as businesses try to get up and running again.

Factory orders will provide us with more color regarding the PMI/ISM data that has been released this past week, and will continue to fill in the blanks as investors search for clues in how businesses that are involved in the space are returning back to normal. Raw order activity has seen weaker demand, so this metric could provide more clues into whether we will have a sustained recovery, or if this is just a one-off increase.

Source for index data: Bloomberg.com; GWI calculations.
Investing involves risk, including possible loss of principal. This material is neither an endorsement of any index or sector nor a solicitation to offer investment advice or sell products or services.

[5] www.Investors.com