9/8/2020 Medical and Economic News Continues to Improve
A Message from Chris Phelps, Advisor

Here we are post-Labor Day which is about the six-month mark of our journey through this pandemic and the up and down responses by our various levels of government. The good news is that there are significant improvements on both the medical as well as economic fronts despite the best of intentions of our governmental authorities. Let's dive in.

Last week San Diego County qualified under the Governor's latest revised measurement system to re-open indoor dining, salons, barber shops, gyms, etc. which is obviously a positive. The downside is that over Labor Day weekend I think all of Southern California and part of Arizona was here. In San Diego County daily new case level averages crept up to about 295 per day in part due to new outbreaks in area colleges and universities which saw an influx of students from around the country. Hospitalizations however, continued to decline by about 20% over the last three weeks. California state reported new daily case levels continue to trend down dramatically with the current seven-day average at 4,450 compared to 9,446 three weeks ago. A more than 50% drop. Also, hospitalizations continue to trend down significantly with total positive and suspected cases hospitalized standing at 4,285 as of September 6, 2020. This compares to 6,360 three weeks ago (a drop of over 2,000) or a decline of 33% which represents an acceleration in the decline of hospitalizations over prior similar periods. If this rate of decline in hospitalizations remains stable, hospitalization levels would be near zero by mid or late October, 2020. So in California daily new case levels are dropping and fewer people are requiring hospitalization and extreme life-saving measures. This trend continues to be a positive development both medically and economically as California begins to re-open (hopefully).

It looks like the volatility I was warning about in the last few weeks notes has finally shown up. The bad news is that the stock market (as measured by the S&P 500 index) is down about 6.5% through today from its high last Wednesday. The good news is that the decline is largely occurring in the technology sector particularly in Apple, Amazon, Microsoft, Alphabet and Facebook. Considering that almost 50% of the gain in the S&P 500 since its March 23rd low was in these positions, it is not surprising they are leading in the move down to a more reasonable valuation level. In economic news over the last week we have seen almost 1.4 million jobs added in August and the unemployment rate fell into single-digit territory at 8.4%, which has occurred faster than most economists had predicted. Motor vehicle and parts production has finally gotten back to pre-Covid levels and consumption of goods has increased faster than production resulting in declining inventories. Small business owners have noticed and the NFIB Small Business Optimism index came in above its 46 year historical average. The Federal Reserve Bank continues to provide monetary support however, the fiscal stimulus could be running low due to the lack of agreement between the House and Senate. Overall, the positives for the stock market are accommodative monetary policy, a clearly recovering economy, improving U.S. and global production and low inflation. The primary negative is that the market appears to have priced in all the good news including a vaccine by the end of the year. Expect volatility on any disappointment with respect to the virus or the vaccine. Risks also include rising long-term interest rates and the return of some level of inflation in the future. A divisive election soon also does not help. All that being said, I still expect stocks to out-perform other asset classes over the next one and five years. As the next year unfolds these issues will get resolved and new uncertainties will develop however, the economy and stock markets will continue to reflect the opportunities that future growth provides. Long-term, I continue to bet on the U.S. economy and the American consumer.

I have attached this week's letter by Brad McMillan, Commonwealth's Chief Investment Officer. He is clearly positive on the status of the virus on a national level and is upbeat about the prospects for the U.S. economy in the future. Risks remain but they appear to be under control. I agree that we are on the right track both economically and with respect to containment of Covid-19.

I am always available to you via phone, zoom conference or in person. I encourage you to remain optimistic and to do what you can to contribute to growing the economy. I look forward to talking with you over the next few weeks. If you have any questions or if we can be of any help, please do not hesitate to contact Linda or me.

As always, stay safe and healthy!

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Medical and Economic News Continues to Improve

Presented by Christopher Phelps

This week, we had more good news on the medical front. The pandemic remains under control and is showing continued improvement. Case growth has declined over the past two weeks, and the case growth rate remains below the lows seen in mid-June. Overall, the control measures are working.

Nationally (as of September 3), the daily spread rate is 0.7 percent per day and has held steady around that level since mid-August. The seven-day average of the daily number of new cases is about 42,000, down from just under 45,000 two weeks ago. If this trend continues, the pandemic will remain under control. The continued improvement in new cases is a positive, but the stabilization in the growth rate suggests that further improvements will be slower.

The testing news continues to be less good. The number of tests has remained relatively steady over the past two weeks, from around 650,000 to 750,000 per day. This testing level is insufficient, as the positive rate has held at more than 5 percent. This is a metric that will need to improve to keep the virus under control.

Beyond the headline numbers, state-level data is generally good, although there are concerns about states in the Midwest. Overall, the national risks remain under control.

With the medical news better, the economic recovery remains on track. The job market continues to improve and spending is holding up, although signs of declining confidence are something to keep an eye on. Before the recent drop, financial markets had continued to move higher in response to the positive developments. Let’s take a look at the details.

The Virus: Growth Rate Remains Low

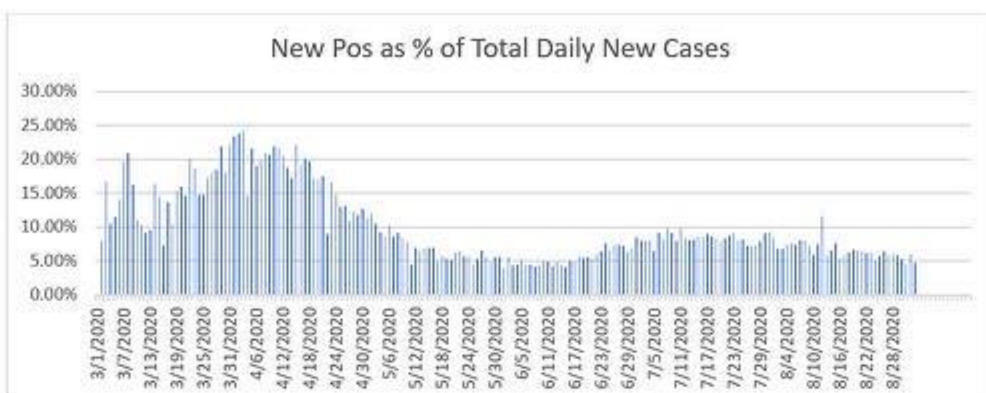
Growth rate. Over the past two weeks, the daily case growth rate has remained relatively steady at around 0.7 percent per day. It has been at that level since mid-August, and it is the lowest level of the pandemic thus far. Even as the case count declines, however, the spread has remained steady, which suggests future improvements will be slower. At this rate, the case-doubling period is about 15 weeks, leaving the infection curve flatter at a national level and leaving the risk to health care systems at a low level.

Source: Data from worldometer.com

Daily testing rate. As infections have dropped, testing has remained steady although variable, and it has stayed in the range of 650,000 to 750,000 per day for the past two weeks. This appears to be below the level of testing needed to develop a full understanding of the pandemic, despite the recent improvements in the spread rate.

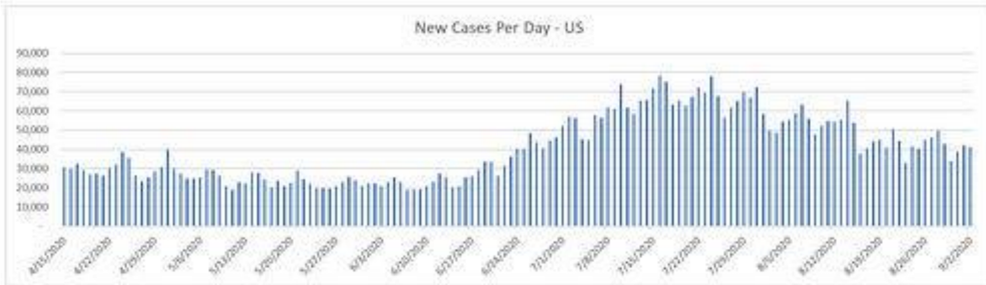
Source: Data from the COVID Tracking Project

Positive test results. We can see this lack of improvement by the positive rate on tests. If we look at the percentage of each day's tests that are positive, lower numbers are better, as we want to be testing everyone and not just those who are obviously sick. The World Health Organization recommends a target of 5 percent or lower; the lower this number gets, the wider the testing is getting. Here, we can see that the positive level has remained above that target, although we have seen some recent improvement.



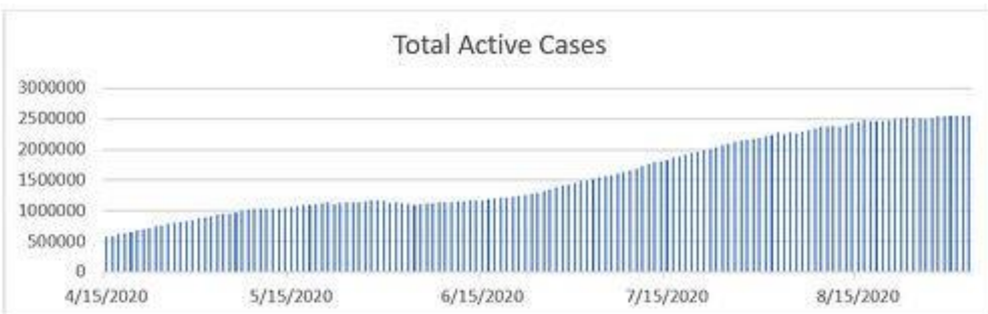
Source: Data from the COVID Tracking Project

New cases per day. The most obvious metric for tracking the virus is daily new cases. With increased control measures in place, especially in the outbreak states, the seven-day average number of new cases per day has dropped from just under 45,000 per day down two weeks ago to around 42,000 per day. While this is an improvement, it is much slower than what we saw in previous weeks.



Source: Data from worldometer.com

Total active cases. Another positive development is that as the number of new cases has slowed, the number of active cases has stabilized over the past two weeks. If case growth continues to decline, new infections will start to lag recoveries, and the number of active cases would actually decline, which would be a very positive sign.



Source: Data from worldometer.com

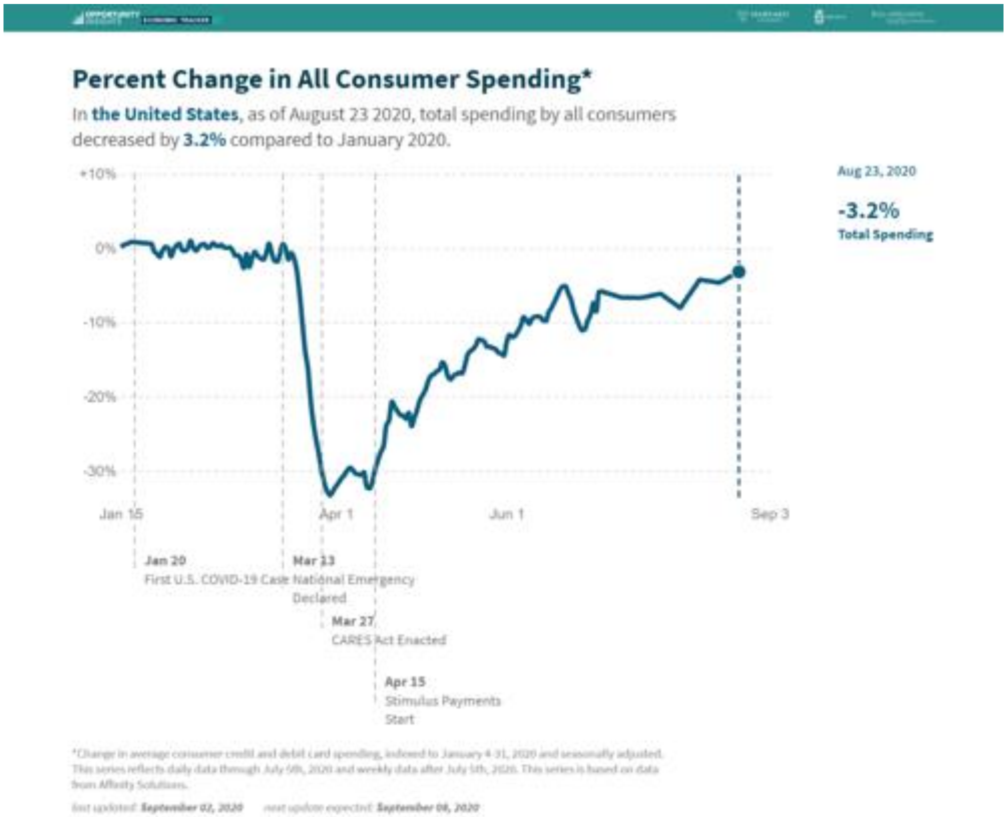
Overall, the pandemic is under control at the national level and continues to improve, although at a slower rate. At the state level, the health emergencies have largely passed, although concerns remain in some states. The good news here is that policy and behavioral changes have taken effect, as they did in the first wave, and that we have largely contained the virus as we did then.

Looking forward, the question is whether the improvement will continue into the fall. The trends are positive. But given the slowing of the pace of improvement, combined with the pending reopening of school districts and universities, the risks remain material. These will be something we need to watch.

The Economy: Recovery Stable

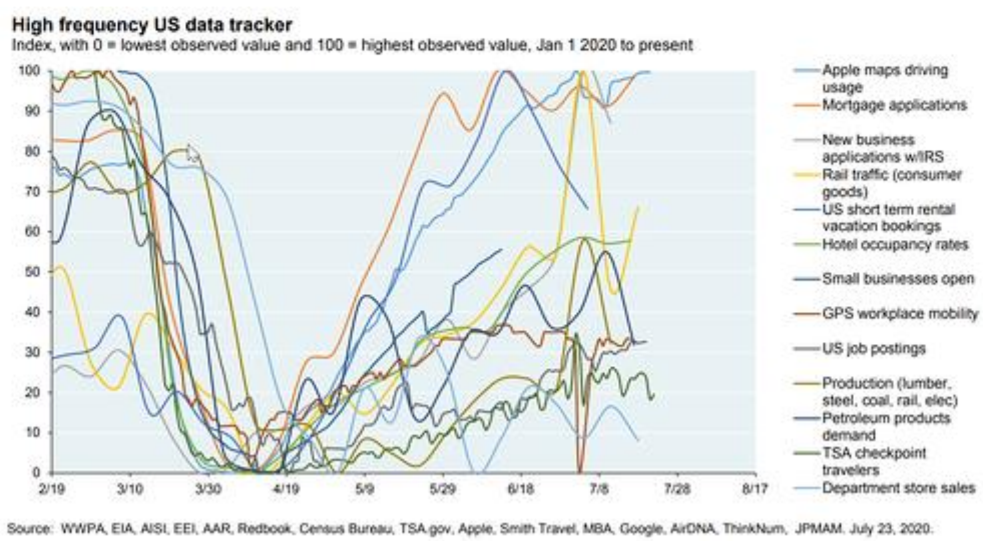
Jobs market. The economic news is also good, with the recovery continuing. The most recent initial jobless claims reports showed further drops, indicating fewer layoffs. The continuing unemployment claims have also improved, showing that many people are returning to work. Stabilization in the jobs market remains a relative bright spot as businesses continue to figure out how to operate under the constraints of the pandemic.

Consumer spending. Consumer spending has also rallied after a pause in the face of the second wave. In the past two weeks, spending has risen to a post-pandemic high, as consumer confidence has shown signs of bottoming and the jobs data has continued to improve. While there are risks, principally around the expiration of federal income support payments, the weakness seems to have passed. This metric remains something to watch, however.



Source: https://tracktherecovery.org/

Finally, we can see similar signs of improvement in many areas, despite a slowdown in some others, in this composite of many indicators from J. P. Morgan.



Source: J. P. Morgan

The big picture is that the recovery is still on track. The medical risks have improved significantly, and the economic risks, while still real, are fading.

The Markets: Respond to Positive Medical News

The recent selloff notwithstanding, the financial markets have appreciated steadily over the past two weeks in response to the positive news and have hit new highs. On the medical front, markets have responded to the improvement in the new case count and encouraging news on vaccine development. On the economic front, better job and confidence news combined with stronger business confidence have helped drive markets higher.

More Improvement Ahead?

The real takeaway for this update is that the second wave has been brought under control, just as the first wave was. The medical risks are now contained, although further future improvement is likely to be slower. The economic risks, while real, also seem to be getting better at this point. Markets have responded enthusiastically to the better news.

Given current trends, over the next couple of weeks, the most likely case appears to be continued improvement on both the medical and economic fronts. There are certainly risks, and we need to watch them. But for the moment, the news remains good.

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