Congress Asset Management Company

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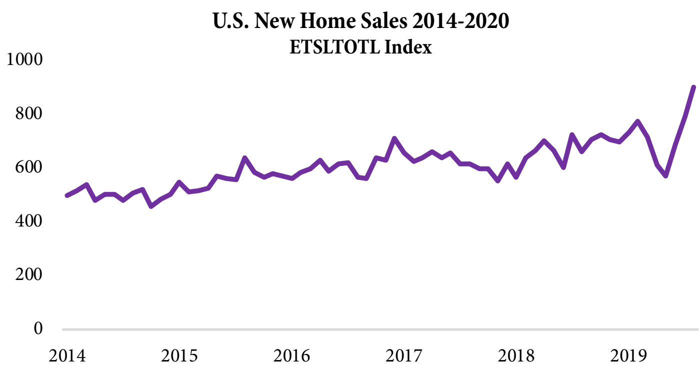
The Stock Market Since COVID

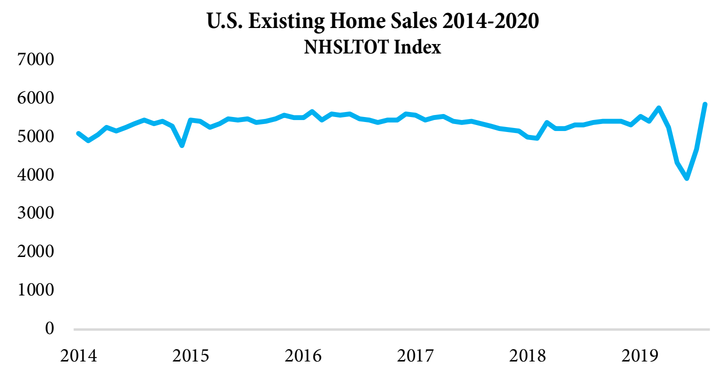
The stock market's relentless ascent since March is notable for its speed, its magnitude, and that it has ignored the realities of the coronavirus-driven economic collapse. Undoubtedly the economy is still struggling, but the overwhelming response of the Federal Reserve Bank is designed to ease the path to an economic resurgence. This path was further supported by federal stimulus packages. Stock investors have responded accordingly as the Fed's actions seem to be setting the stage for a recovery. Don't fight the Fed.

Since World War 2, and increasingly since the economic malaise of the 1970s, the Fed has become more proactive in response to recessions. Still, the Fed has appeared at times as stodgy and slow. This time is different – the Fed responded unabashedly and with alacrity. The Fed fast tracked tools used in its response to the 2008 financial crisis then threw caution to the wind by expanding its tool set, most notably by softening its inflation stance.

There is abundant evidence that the Fed's actions are working to spark economic growth even as Main Street continues to struggle. Most obviously, interest rates remain historically low and act to support the housing market through cheap mortgage rates. Importantly, the Fed's recent pronouncement to focus on average inflation rather than a specific 2% rate will allow the Fed to keep short term rates lower for longer. This is vital given the abrupt decline in employment and is tacit acknowledgement that Main Street and lower skilled workers face longer term challenges. This go-round, the Fed does not want to be accused of taking the punch bowl away.



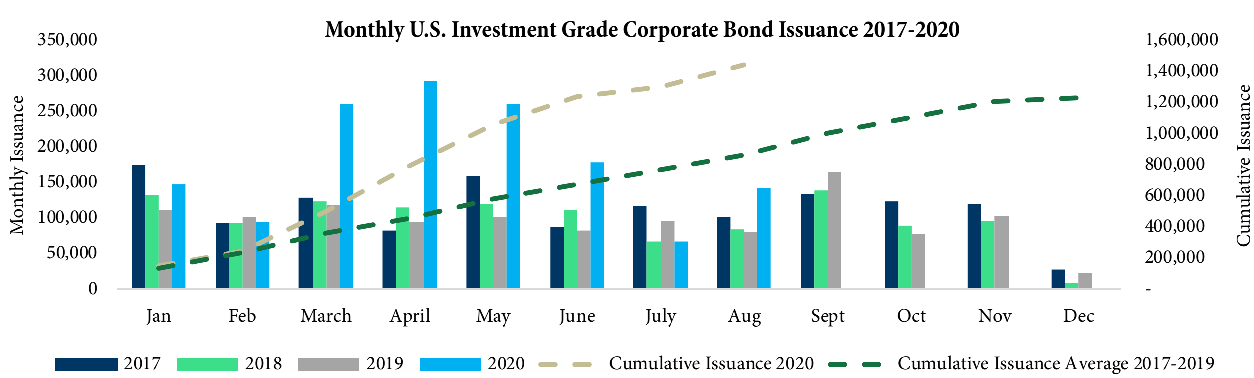
Source: Bloomberg



Source: Bloomberg

Less obvious is the increase in the money supply, referred to as M2. Fed measures to increase the supply of money should put more dollars in consumers' hands and spur investment.

The Fed is also supporting both the corporate and municipal bond markets, stoking increased demand for new corporate bond issuance. For corporations the longer-term benefits include a lower cost of capital and liquidity for future investments, helping to ease investors' concerns about a cash crunch.



Source: Bloomberg

The municipal bond facility is intended to support cash strapped issuers and is actively being used. The New York Metropolitan Transportation Authority issued over $450 million in bonds directly to the Fed. This facility should buy time for revenue challenged municipal organizations.

Recent economic reports indicate that the economy has stabilized, with certain areas growing again. For example, the August reading for the ISM Index, a broad measure of the manufacturing sector, was solidly positive with new orders reaching a 16-year high. Perhaps the most surprising economic indicator over the last few months is personal income which continues to register close to 10% growth, reflecting the benefits of the federal government stimulus. With spending opportunities constrained, the personal savings rate is higher than it has been, providing a cushion for some and potential for dry powder when consumers begin to re-engage.

Source: Bloomberg

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The stock market's reaction over the past five months reflects the unprecedented financial support that the Federal Reserve and federal government have committed to the economy. The path forward is still positive, but challenges await. For long term investors, a diversified equity portfolio remains the key to long term investment success. Bonds should continue to provide stability with modest income for safety and security.

-Congress Asset Management Investment Oversight Committee