



## Market & Economic Outlook 2020 – July Update: Market Surges as Economic Recovery Proceeds

Major Indices	2Q20 (3/31/2020 - 6/30/2020)			2020 YTD (12/31/2019 - 6/30/2020)		
	Value	Price Return	Total Return	Value	Price Return	Total Return
S&P 500	3,100.29	20.0%	20.5%	2,584.59	-4.0%	-3.1%
Dow Jones Industrial Average	25,812.88	17.8%	18.5%	21,917.16	-9.6%	-8.4%
NASDAQ Composite	10,058.77	30.6%	30.9%	7,700.10	12.1%	12.7%
Russell 2000	1,441.37	25.0%	25.4%	1,153.10	-13.6%	-13.0%
MSCI EAFE (USD)	1,780.58	11.9%	12.8%	1,559.59	-11.8%	-10.3%
MSCI Emerging Markets (USD)	995.10	15.9%	16.8%	848.58	-6.5%	-5.4%
Bloomberg Commodity Index	64.98	5.0%	5.1%	61.86	-19.7%	-19.4%
Barclays U.S. Aggregate Bond	110.44	2.1%	2.9%	108.20	4.6%	6.1%

Data Source: FactSet

### Outlook Summary:

The S&P 500 index gained 20.5%, including dividends, in the second quarter of 2020, reversing much of the Q1 decline as investor sentiment surged following unprecedented monetary and fiscal support from the Federal government and signs that the economic downturn bottomed in late-April/ early-May. The Q2 equity rally was broad-based, as the Nasdaq Composite index (led by Technology) gained 30.9%, and the Russell 2000 (small caps) increased 25.4%, both beating the S&P 500, and equities in emerging markets and developed foreign markets delivered double-digit percentage gains, as well. Equity gains for the 6-month period through 6/30/20 remained mostly negative, with the S&P 500 and Dow Jones Industrial Average down 3.1% and 8.4%, respectively. The notable exception was a first half gain of 12.7% for the Nasdaq Composite index, led by a surge in technology stocks and other large cap leaders with dominant Internet and cloud-based platforms, as those groups are well-positioned for a COVID and post-COVID economy. Markets rallied despite a deep U.S. and global recession, ongoing COVID-19 uncertainty, and severe social unrest in the U.S. as investors have looked past expected 2020 economic weakness and earnings declines, concluding that U.S. economic growth would resume in the second half of this year and support an earnings rebound in 2021. We agree with the assessment that the U.S. economy is likely to sustain solid growth beginning in 3Q20, but we do not expect economic activity to recover to pre-COVID levels until late 2021 or perhaps 2022. **Following our expectations for U.S. interest rates to remain lower for longer, and sustained economic improvement despite new COVID infections, we recently increased our S&P 500 fair value estimate to 3,200 from 3,000 previously. This estimate is 3.2% above 6/30/20 levels.**

From 2/19/20 to 3/23/20 (during the first quarter), the S&P 500 declined 34.0%, the fastest greater-than-30% decline in history. From the March low of 2,237, the index rallied 44.5% over 11 weeks to 3,232 on 6/8/20, and by the end of June was still 38.5% above the low. Equity prices have moved faster than any recovery in economic data, which we believe creates some challenges for investors over the second half of 2020. Market valuations, especially price to earnings (P/E) ratios, are trading at the high-end of historical ranges, and a recent resurgence of COVID-19 infections in the U.S. has led to renewed business and consumer restrictions at the state and local level. Before the new infection surge, the economic rebound was trending above expectations with employment, retail sales, airline travel and manufacturing all showing strong sequential improvement. The pace of recovery is likely to slow from recent levels, but we do not expect another national shutdown response, allowing economic growth to continue despite hot-spots of infection outbreaks. **COVID-19 risk and the economic rebound are likely to coexist for the immediate future, which could limit market gains from current levels until 2021 earnings visibility improves. We advise investors to temper return expectations for portfolios, remain diversified across sectors and use market volatility to upgrade portfolio quality.**

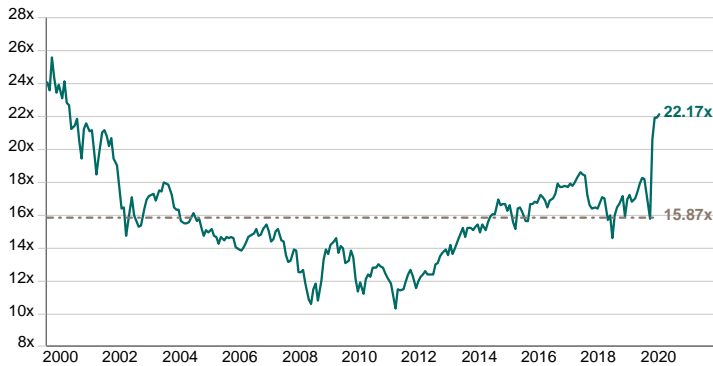


Data Source: FactSet as of 7/7/20. S&P 500 Price Changes 12/31/18 to 7/7/20

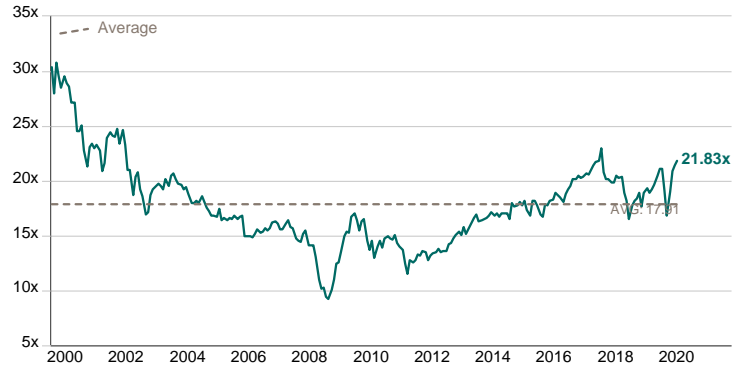
**Our S&P 500 fair value estimate of 3,200 represents a P/E of 22.5x the next 12-month (NTM) FactSet consensus EPS estimate of \$142, and 19.8x the consensus calendar year 2021 estimate of \$162.** Current S&P 500 estimates assume that 2021 earnings return to 2019 levels, a lower outlook than three months ago when 2021 expectations were above 2019. While some industries are likely to return to previous

earnings levels next year, others face a longer recovery following recession-level declines in 2020, and many consumer-spending exposed industries face challenges as social distancing recommendations remain in place. For the broader market, we believe the combination of an expected sustained earnings growth trajectory and low interest rates support the elevated P/E ratios that we see today. While we expect P/E ratios to remain above historical averages in the current environment we also believe that high market P/E ratios lead to lower expected market gains in future periods. This contributes to our view that the S&P 500 gains are likely to be modest from current levels, at least until we have a clearer picture of earnings gains in the future. We also expect market volatility over the second half of 2020, following the steady gains of the past 3 1/2 months. Over the past 20 years, the average peak-to-trough calendar year decline for the S&P 500 was 15.8%, and averaged 12.8% annually during the 11-year bull market of 2009 to 2019. Of course, in 2020 we have already lived through a 34.0% peak-to-trough decline, but market pull backs of 10% or more are very common. This year, since the market low on 3/23/20, the S&P 500 declined 7.1% over three days in early-June, and still has not recovered all of that pull back.

S&P 500 Forward P/E Ratio (next 12 months)



S&P 500 Trailing P/E Ratio (trailing 12 months)

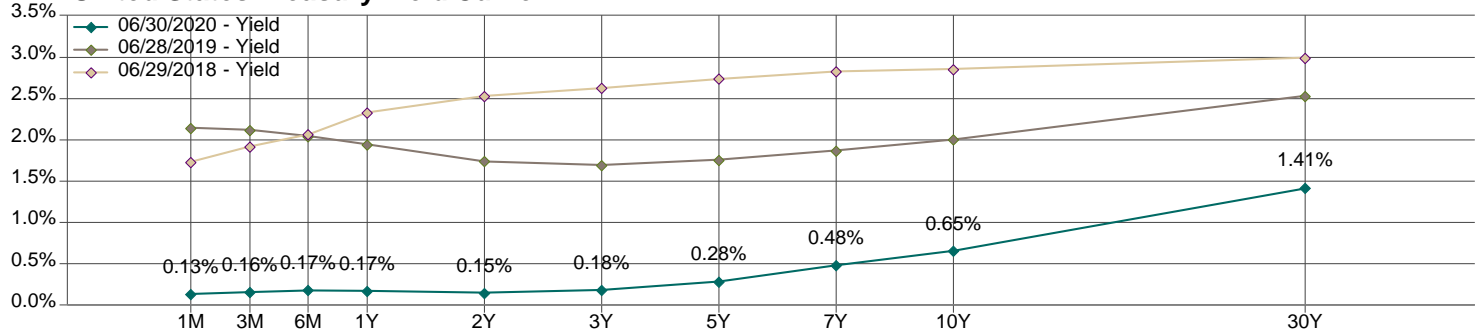


Data source: FactSet as of 7/7/20

**Over the second half of 2020, investors will balance multiple market risks against several potential catalysts. While this is likely to create ongoing volatility, we do not see the S&P 500 revisiting the March lows this year.** Market headwinds entering the third quarter include ongoing COVID-19 infection impacts, lower than expected jobs gains following the recent surge, negative reaction to weak Q2 earnings reports, increasing debt levels at both the Federal government and corporations, high market valuations discussed above, and the November general election, with a range of potential outcomes. Offsetting these risks however, are numerous potential catalysts that could drive positive investor sentiment and help to limit the downside on market pull backs. This includes an end to the recession in Q3, as GDP is expected to grow from Q2, massive liquidity provided by the Federal Reserve in fixed income markets, another Federal relief package passed by Congress, progress on a COVID-19 vaccine, low interest rates, large cash balances on the sidelines (money market fund balances on 6/30/20 were higher than on 3/31/20), and an investor willingness to look at 2022 prospects for earnings and GDP growth. We will discuss many of these headwinds and catalysts over the pages that follow.

**Interest Rates are historically low in 2020 as U.S. Treasury yields have dropped across the entire yield curve to record low levels.** Several factors have contributed to low interest rates including the Fed lowering its overnight fed funds target rate to 0% in March from 1.50% at the end of 2019, very low inflation in the U.S. and globally, and expectations for low GDP growth potential following the COVID-19 recession. The Federal Reserve’s Open Market Committee (FOMC) met twice in the second quarter, in late-April and early-June. The April meeting was held at the depths of the government-imposed shutdown and economic downturn, and the Fed pledged to keep interest rates at zero as long as necessary and reiterated its commitment to quantitative easing and liquidity support that included \$700 billion (B) available for Treasury and mortgage securities purchases, and other securities such as money market funds, corporate bonds, and municipal bonds; as well as \$2.3T in loan availability for small businesses and municipalities. At the June meeting, the Fed reiterated its commitment to low interest rates and said that its efforts to provide liquidity had help stabilize financial markets. The FOMC also discussed the idea of managing long-term rates as well as overnight rates, which some have termed “yield curve control,” but Fed Chair Jerome Powell said it was only discussed and more investigation was needed. Mr. Powell also said the Fed was “not even thinking about **thinking about** raising rates,” and the June Summary of Economic Projections (often called the dot plot) confirmed that conclusion. The median FOMC participant estimate for the fed funds target was 0% at the end of 2020, 2021 and 2022, an indication that U.S. interest rates are expected to remain at historically low levels for the next few years. The dot plot also reflected a median estimate for U.S. GDP of -6.5% in 2020 and 5.0% growth in 2021, with a 12/31/20 unemployment rate of 9.3%, and 6.5% at 12/31/21.

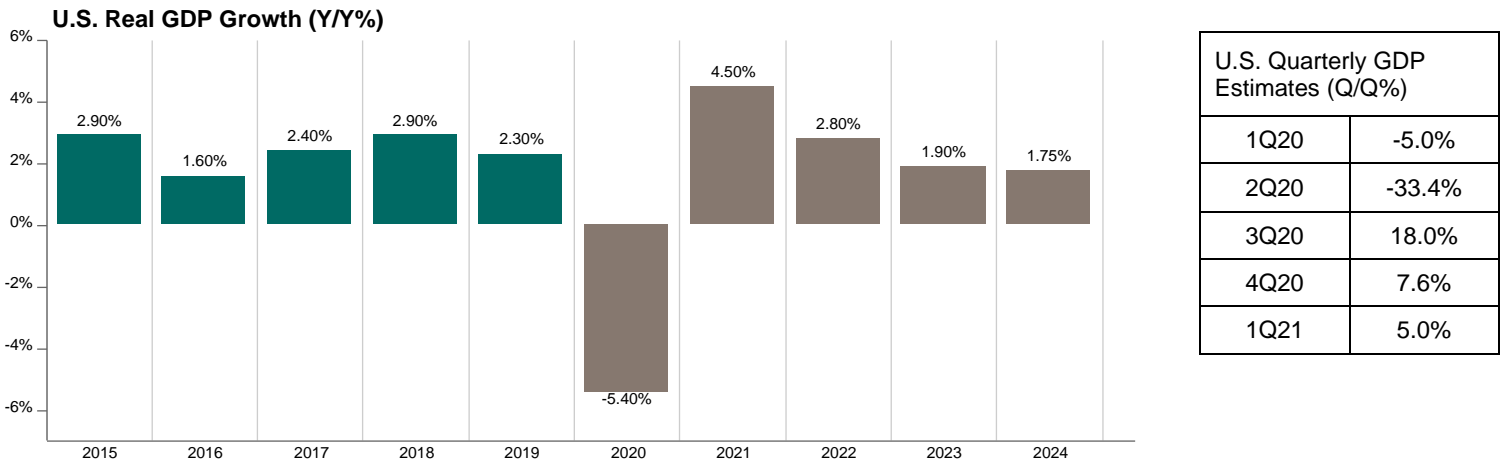
United States Treasury Yield Curve



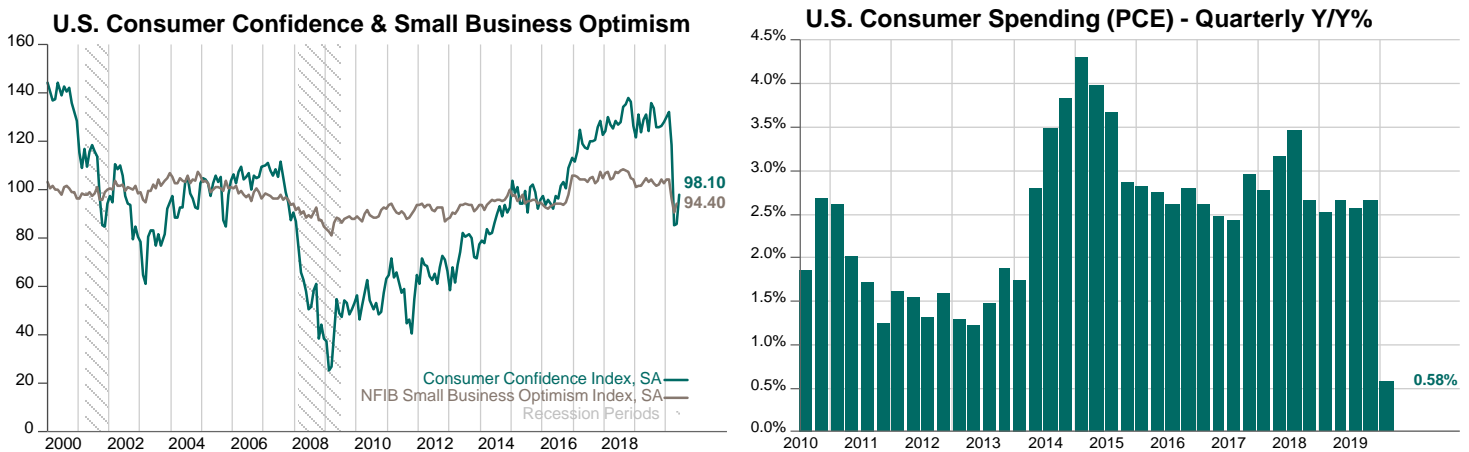
Data source: FactSet as of 6/30/20

**U.S. GDP levels remain highly uncertain due to the extreme impact of the shutdown and measured reopen trajectory, but directionally we expect improving data in the second half of 2020 and 2021.** According to consensus estimates, U.S. GDP is expected to decrease 5.4% in 2020 and return to 4.5% growth in 2021. Strong growth is expected next year due to the unprecedented nature of the COVID-19 recession, which was caused by a government-initiated economic shutdown to fight the pandemic, and not due to economic imbalances such as inventory build-up, over capacity, or consumer spending excess. This should lead to a faster recovery as pandemic headwinds subside and consumer and business activity normalizes. While 4.5% GDP growth in 2021 would represent significantly stronger annual growth than in any year following the Global Financial Crisis (GFC) in 2008 (the highest post-GFC GDP growth years were 2015 and 2018, both at 2.9%), the nominal GDP at year-end 2021, would be \$20.7 trillion (T), still below 2019 U.S. GDP of \$21.0T. In that case, U.S. nominal GDP would not return to the 2019 levels until 2022.

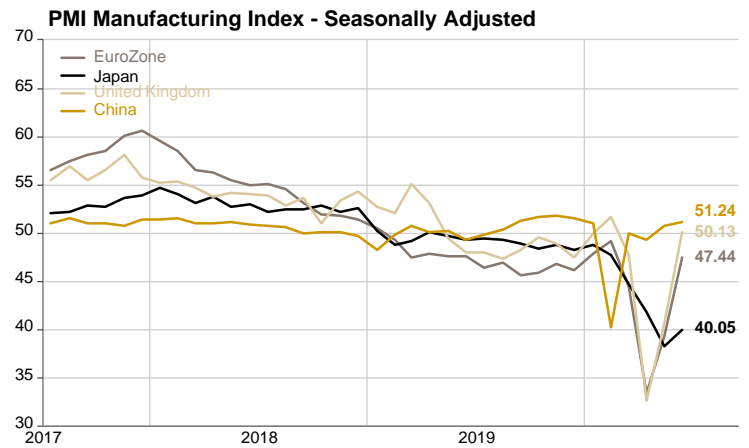
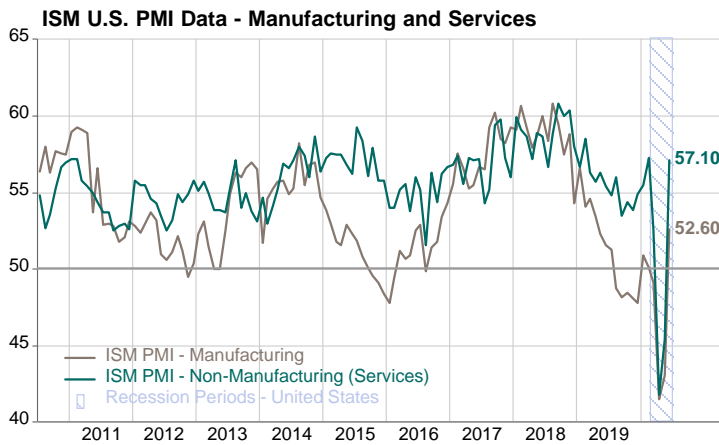
It remains difficult to estimate GDP in the current environment due to the sudden, across-the-board shutdown, better than expected early restart, and new headwinds created by the recent surge in COVID infections. Q1 2020 GDP has been reported and it declined 5.0%, driven by a 6.8% Q1 decrease in consumer spending, and a 10.2% decline in fixed investment; offset by a 1.1% increase in government expenditures. Within those numbers, there were a few areas of growth, including residential construction, grocery and merchandise stores, and business investment in software. But Q1 included just a few weeks of shutdown orders and the full brunt of those orders will be incurred in Q2 (mostly in April and May). Q2 2020 GDP is expected to decline 33.4% on an annualized level from Q1, and we have seen a wide range of estimates from down 25% to down 40%. We expect to see weakness across the board including severe declines in consumer spending and business investment, and even the Q1 growth areas of residential construction, software investment and government spending (due to a drop in state and local expenditures) likely turned negative. However, in June, we saw an inflection in several important data points, indicating that the downturn has likely bottomed (although economic activity remains below pre-pandemic levels). Consumer confidence and small business optimism plunged in April and May but moved higher in June, and ISM Manufacturing and non-Manufacturing (services) surveys both spiked above 50 in June, indicating an end to the recession. The PMI services rebound was a significant positive surprise. June also saw an improvement in manufacturing PMIs in major foreign economies, including the Eurozone, China, the U.K., and Japan. This has important ramifications for large-cap U.S. equities as the S&P 500 generates more than 1/3 of its revenue from outside the U.S. Many of these countries have sustained reductions in COVID infections and are poised to benefit from rebounding economic growth.



Data source: FactSet as of 7/8/20; data for 2020 through 2024 are FactSet consensus estimates. U.S. Quarterly GDP estimates for 2Q20 to 1Q21 are FactSet consensus, 1Q20 is the actual number from the U.S. Department of Commerce reported 6/25/20.



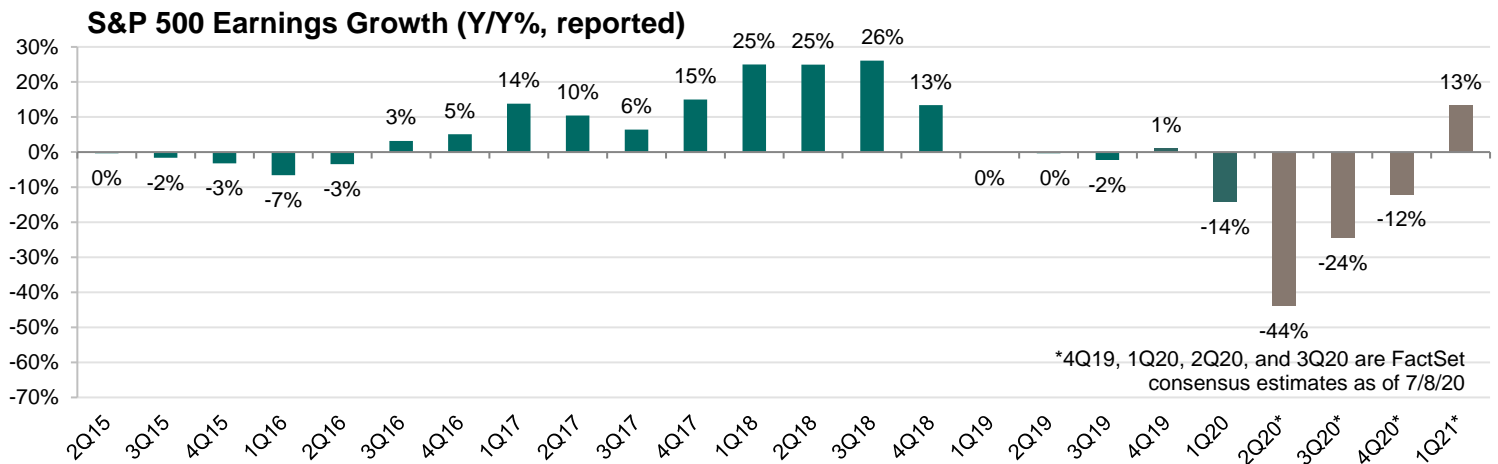
Data source: FactSet; U.S. Consumer Confidence data as of 6/30/20; U.S. Consumer Spending as of 3/31/20



Data source: FactSet as of 6/30/20

**Following the report of 4.8 million (M) new jobs created in June, and a 2.7M increase in May, the U.S. has recovered 34% of the 22.4M jobs lost in March and April due to the COVID-19 shutdown.** Employment growth over the past two months exceeded expectations as states allowed restarting business activity from depressed levels. This highlights the resiliency of the U.S. economy and the potential for strong recovery. The level of employed remains significantly below pre-pandemic levels however, as the June unemployment rate was 11.1%, reflecting 17.8M persons out of work. This compared to February 2020 levels of a 3.5% unemployment rate and 5.8M workers unemployed. We expect the pace of jobs growth to moderate in future periods as the initial reopen push is completed and sustained hiring trends will be dependent upon consumer activity returning to more normal levels, and business investment improving. While we do not expect a complete recovery in the jobs market until a COVID vaccine is approved and available (expected sometime in 2021), we believe that the jobs market will continue to improve through year-end. With an estimated range of 2020 year-end unemployment numbers of 10.0M to 15.0M, the midpoint of that range of 12.5M would reflect 5.3M new jobs over the next six months (averaging 875 thousand monthly) and a 7.8% unemployment rate.

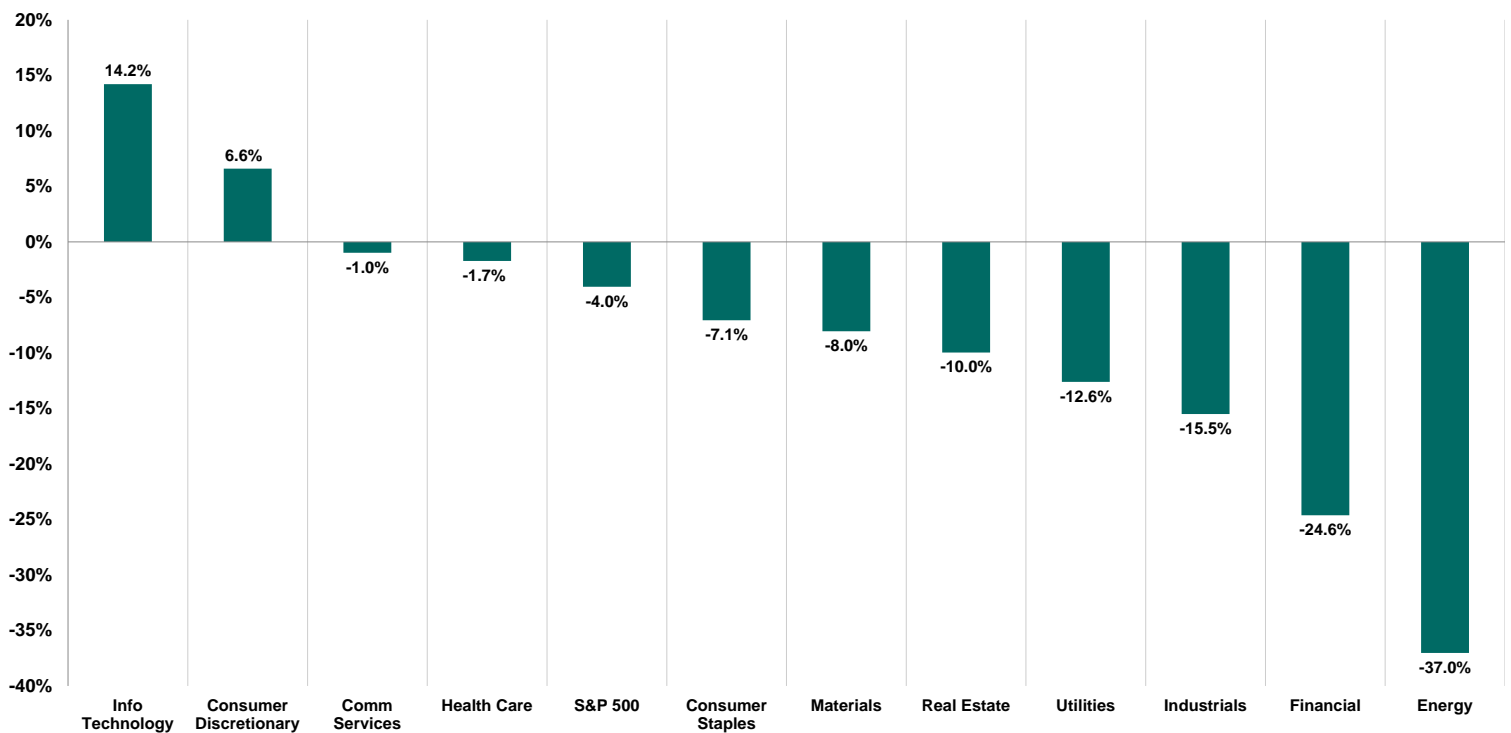
**S&P 500 earnings are expected to decrease year-over-year each quarter of 2020 and return to growth in 2021.** Three months ago, we believed that earnings growth could resume in the fourth quarter this year, but that outlook has been pushed out to the first quarter of next year. This is primarily due to a deeper 2020 earnings contraction than was contemplated as the shutdown took hold, requiring a larger move from the bottom to return to growth. On an annual basis, S&P 500 earnings are estimated to decline 23% in 2020, and then grow 29% in 2021. In Q1 2020, S&P 500 earnings declined 14%, but six of the eleven macro sectors showed Y/Y growth. Q1 earnings growers included Health Care, Technology, Communications Services, and Consumer Staples. The bulk of the market earnings decline was attributed to the Financials, Consumer Discretionary, and Industrials sectors. In Q2 however, all eleven sectors are estimated to deliver Y/Y earnings declines, leading to an expected S&P 500 earnings drop of 44%. We expect the same three sectors, Financials, Consumer Discretionary, and Industrials to contribute the bulk of the overall weakness, while the sectors with the best (least negative) estimated Y/Y declines are Utilities, REITs, and Technology. As we discussed earlier, equity investors appear to have largely discounted the 2020 earnings decline to focus on the expected strong growth in 2021. While some have questioned the strength of the expected earnings recovery in 2021, as many sub-industries such as airlines, hotels, specialty retailers, and restaurants face multi-year headwinds, other sectors will recover quickly and growth in foreign economies will help U.S. exporters. If 2021 earnings trail expectation, but still sustain growth close 20% we believe that investors will begin to look at 2022 estimates if sustained growth appears likely.



Data source: FactSet as of 7/8/20

**Despite strong S&P 500 gains in Q2 that saw all eleven sectors trade higher, just two sectors were positive YTD through mid-year, and only four sectors outperformed index.** Technology has been the standout performer in 2020, as the sector is uniquely positioned in the COVID-19 environment as companies invest to enhance productivity, build cloud infrastructure and support remote access for work-from-home and hybrid employees. Many tech sector sub-industries have outperformed, including software, hardware & storage, semiconductors and IT services. While some spending was likely accelerated in response to COVID, we believe the sector remains well positioned as cloud and remote access are secular trends, and companies may prioritize tech investments over headcount increases as the economic recovery matures. We also should discuss Consumer Discretionary as the YTD sector performance is largely driven by a single company, which comprises more than 40% of the S&P 500's Consumer Discretionary weighting. More broadly, the Consumer sector faces economic headwinds and portfolios should remain diversified across sub-industries within the sector. The four sectors (Technology, Consumer Discretionary, Communications Services, and Health Care) to outperform the index YTD are also the four largest by market capitalization, comprising 63% of the S&P 500's total weighting. This outperformance of a select few sectors has offset the impact of double-digit percentage declines from the bottom four performing sectors, which collectively comprise 25% of the index capitalization. This includes Energy, Financials, Industrials, and Utilities. We continue to see strong investor interest in the top performing sectors as three (Technology, Healthcare, and Communications Services) reported earnings growth in Q1 and appear well positioned during the COVID-19 recession. In addition to the relative earnings resiliency, these sectors, along with Consumer Discretionary, include the largest mega-cap companies, which are positioned to gain market share post-pandemic. Two defensive sectors, Consumer Staples, and Utilities, reported earnings gains in Q1, but have underperformed the market this year, as investor interest has gravitated to growth stocks with the potential to benefit from an economic recovery. While markets have largely priced in the Q2 expected earnings decline, the magnitude of a 44% drop or worse, could drive market volatility as reported results begin in mid-July. This could boost near-term interest in defensive sectors, as it is typical for defensive groups to outperform during a recession due to less exposure to economic weakness. But because we see recent economic growth as sustainable, we caution against becoming overly defensive. **We still expect cyclical sectors to lead the recovery, which includes Technology, Industrials, Financials and Materials. We also believe Health Care is an attractive sector in the current environment. We believe that investors should build investment portfolios of high quality companies that are diversified across sectors, and use market volatility to manage exposures and rebalance where appropriate. Although it appears today that the top performing sectors will continue to lead, history tells us sector leadership rotates over time and a well-constructed diversification strategy can help to reduce risk.**

**S&P 500 Sector Performance – Year-to-Date (price returns)**



Data source: FactSet as of 6/30/20

**We recommend that investors prioritize high quality companies in their equity portfolios, especially as economic and earnings uncertainty remains high.** High quality companies often enhance their competitive positions during periods of economic weakness, as they are able to sustain investment in research and development and have access to cash flow and capital to make strategic investments. Important indicators of high quality, in our view, are market leadership (strong product positions), quality management, resilient profitability (generating income and cash flow), and strong balance sheets.

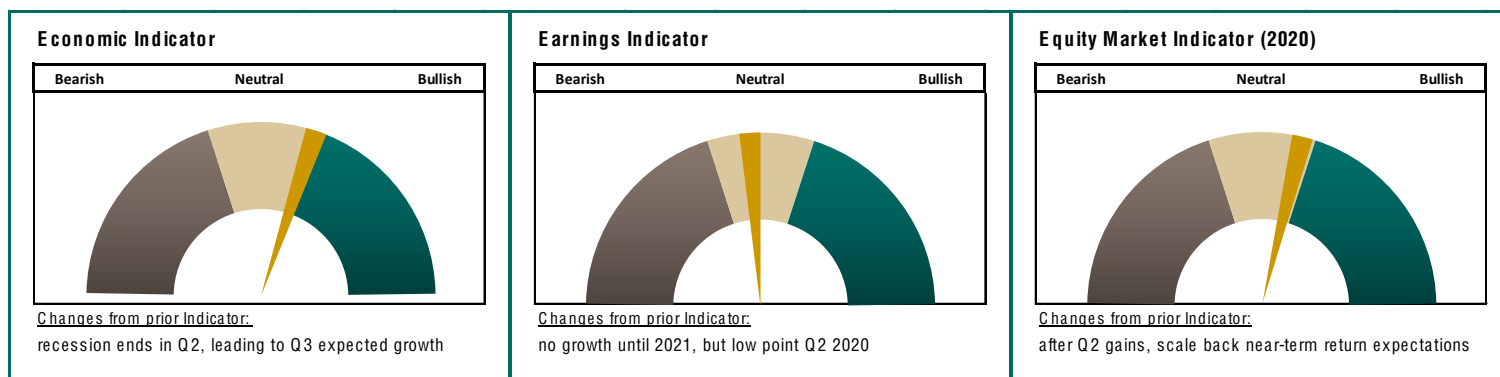
Our S&P sector recommendations are updated below.

**S&P 500 Sector Recommendations - July 2020**

GICS Sector	S&P 500 Weight by Market Cap	WM Research 2020 Outlook	Notes	Change
Technology	27.4%	marketweight	well positioned in post-COVID-19 world, rich valuations	
Health Care	14.6%	overweight	on the front lines of COVID-19 battle, valuations attractive	
Financials	9.8%	overweight	2020 Stress Tests were positive, but headwinds to dividend growth	
Communications Services	11.1%	marketweight	look to market leaders, ad spending to be challenged	
Consumer Discretionary	11.1%	marketweight	direct hit from COVID-19, look beyond retailers	
Industrials	7.9%	overweight	attractive valuations, global exposure a positive as countries reopen	
Consumer Staples	7.0%	marketweight	safe haven in down market, but will lag the recovery	
Utilities	3.0%	underweight	strong defensive and domestic appeal, but sector is expensive	
Real Estate (REITs)	2.8%	underweight	vulnerable to dividend cuts, watch exposure to hotels and retail	
Energy	2.7%	marketweight	supply/demand improving, challenges remain, stick with leaders	
Materials	2.6%	marketweight	some deflationary pressures, stick with specialty products	

Data source: D.A. Davidson Wealth Management Research as of 7/9/20; no changes to individual sector outlooks were made from our prior update in April

**Wealth Management Research Investment Cycle Gauge**



Source data: D.A. Davidson & Co. as of 7/9/20

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**Market Indices:** The information on indices is presented for illustrative purposes only and is not intended to imply the potential performance of any fund or investment. Indices provide a general source of information on how various market segments and types of investments have performed in the past. Index performance assumes the reinvestment of all distributions, but does not assume any transaction costs, taxes, management fees, or other expenses. You may not invest directly in an index. Past performance is not an indicator of future results. The Russell 2000® Index is a market cap weighted index that measures the performance of the 2,000 smallest companies in the Russell 3000® Index. The S&P 400 Index is a market cap weighted index comprised of U.S. stocks in the middle capitalization range, generally considered to be between \$200 million and \$5 billion in market value. The S&P 500 Index is a market cap weighted index that is designed to measure the US large-cap equity performance. The index is composed of the 500 leading publically traded US companies based on size, liquidity, industry, and profitability criteria. The Dow Jones Industrial Average is a price weighted index that tracks 30 large, publicly-owned companies trading on the New York Stock Exchange (NYSE) and the NASDAQ. The MSCI EAFE® Index (Europe, Austral, Asia, Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the US and Canada. The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets.

**Other Disclosures:**

The forward S&P 500 price-to-earnings ratio (P/E) is a valuation measure, calculated by dividing the price of the S&P 500 index over the weighted average earnings per share (EPS) estimate of each company in the index. Earnings are based on “forward” consensus estimates expected over the next 12 months (NTM).

The yield of the 10-year U.S. Treasury bond is a widely followed barometer of the current U.S. interest rate environment.

S&P 500 earnings growth reflect the year over year change in operating earnings on a per share basis. Earnings data are aggregated for all S&P 500 constituents and are measured according to the relative market capitalization weights for each company. Estimated earnings are the combined FactSet estimates of analysts covering each company included in the index.

Non-residential fixed investment is an indicator of U.S. corporate capital expenditures (capex), measured by the amount spent on structures, equipment, and software. Seasonally adjusted annual rate (SAAR) is used to normalize data by adjusting for seasonal changes in business and economic data for a more accurate comparison between different time periods

The ISM Purchasing Managers' Index (PMI) is an indicator of the outlook for the manufacturing (PMI – Manufacturing) and services (PMI – Services) sectors of the economy. The index is based on a wide survey of company executives in these sectors. A reading above 50 indicates expectation for expansion compared to the previous month; a reading below 50 suggests contraction. Seasonally adjusted (SA) is used to normalize data by adjusting for seasonal changes in business and economic data for a more accurate comparison between different time periods. United States and Euro Zone data is provided by IHS Markit, Japan data is provided by Nikkei, United Kingdom data is provided by the Chartered Institute of Procurement & Supply, and China data is provided by Caixin.

The Treasury yield curve displays the market interest rate across different contract lengths for U.S. Treasury bonds, indicating the relationship between the interest rate and the time (“term”) to maturity.

The yields of the 10-year and 3-Month U.S. Treasury bonds are widely followed barometers of the current U.S. interest rate environment. The spread is the difference in interest rates between the two securities.

U.S. Personal Consumption Expenditures (PCE) is an indicator of the growth in consumer spending.

Country GDP estimates are aggregated and redistributed by FactSet. This does not constitute investment advice or recommendations of any kind. Estimates data is provided for information purposes only. IMF-Global GDP estimate is the International Monetary Fund's World Economic Outlook last published on 10/2/19.