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Investment Institute

Market Commentary

Weekly perspective on current market sentiment | March 25, 2020

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Last Week's S&P 500 Index: -15.0%

Adjustments Needed

Key takeaways

- Estimates of economic growth have come down. Less economic activity will likely have a negative effect on corporate earnings growth.
- Less economic growth will also reduce our expectations for stock market performance over the balance of the year. Adjustments to targets have been made.

After a terrible five days for the stock market, the U.S. Treasury Secretary made comments over the weekend that the coronavirus effects may last through June. Then a number of economists piled on with negative news surrounding estimates of second-quarter gross domestic product (GDP) falling as much as 25% at an annualized basis. As we mentioned in this piece a few weeks ago, it is no wonder equity traders do not want to go home for the weekend carrying meaningful unhedged long positions. The risk of negative news or comments coming out while financial markets are closed is just too high right now. Certainly the last handful of weekends have largely produced exactly that—bad news for the market.

The risks to our economic estimates in the wake of the COVID-19 outbreak have been to the downside. Indeed, after coming into the year expecting 2.1% growth for the economy, we are now looking for just 0.5% growth as many parts of the country are on virtual lockdown and are operating under "stay at home" directives from state and/or local governments. Most of these directives appear set to expire at the end of March or the first week in April, but a number of medical experts think the timeline could stretch out longer. That is helping to feed market uncertainty and volatility. So, estimates of the economic impact could change again.

Reduced expectations for economic growth have a direct effect on other financial asset classes, particularly equities. In addition to lowering the growth estimate for the U.S., our economics team lowered expectations for global GDP (2.3% down to 1.2%) as well as developed international economies (1.3% down to -0.1%), and emerging markets (3.0% down to 2.1%). Growth expectations that fall by this degree of magnitude are likely going to have a noticeable effect on corporate earnings expectations. As a result, we have made adjustments to earnings estimates and year-end targets for the five major equity asset classes we cover.

Given all of the uncertainty surrounding just when the coronavirus will peak and the number of new cases will begin to decrease as well as the magnitude of the ultimate negative effect on the economy, we think it is important at this time for investors to focus more on the direction of our equity asset class targets rather than the numerical projected year-end range. Our target range for the S&P 500 for the end of the year is 2670 to 2850. Based on Monday's close, that represents a 23% return (excluding dividends) between now and year end. We have been recommending that investors take advantage of this tumble in the market to step into U.S. large- and mid-cap stocks. Our year-end targets indicate that we believe the best opportunities for return lie in those two equity asset classes.

Expectations for economic growth have required adjustments to equity expectations. But opportunities do exist.

Risk Considerations

Forecasts are not guaranteed and based on certain assumptions and on views of market and economic conditions which are subject to change.

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