The Quarterly Perspective

WRITTEN BY:

Christopher Riggs, JD, CFP®

Christopher Riggs leads portfolio strategy and research for Harman Wealth Management. He writes extensively about the economy and markets. His responsibilities include macroeconomic analysis, portfolio construction, and leading the HWM investment committee.

Riggs also heads Alphalytics Research, a subscription-based research service to investment professionals across the U.S. The service emphasizes rigorous and robust data analytics in the context of the U.S. business cycle.

ABOUT

Harman Wealth Management

At Harman Wealth Management, we provide private, advanced, independent planning and investment management to individuals, families, and institutional clients.

We value in-depth economic research, evidence-based investment methods, and rigorous risk management. We are committed to insightful, objective solutions, and always working solely for the best interest of our clients.

CONTACT US

HARMAN

1725 Hughes Landing Boulevard
Suite 1250
The Woodlands, TX 77380
Phone: (281)719-8601

www.harmanwealth.com

With Economy Re-opening, Attention Turns to Recovery

Unprecedented. It is a simple word, but its magintude can not be overstated when describing the series of events faced since February.

The speed of the global pandemic, the reactionary policy of containment, the painful economic shock, as well as the massive monetary and fiscal policy that followed – all of it was unimaginiable six months ago and unprecedented in size and scale when realized. Now, we face an unprecedented solution – that of re-opening the economy, ending the recession quickly, and returning to growth.

For investors, a swift return to economic growth should matter more than anything else. History associates contracting economies with dangerous, volatile market environments and growing economies with more stable periods.

For investors, a swift return to economic growth should matter more than anything else. History associates contracting economies with dangerous, volatile market environments and growing economies with more stable periods.

The uniqueness of the current episode offers hope recovering growth may be here soon. In the same way containment policy caused forceful declines across the economy, easing those same restrictions facilitates a return to growth. As mobility increases, businesses can reopen and restore profits. Workers can return to work and consumers can return to more typical behaviors. The process of normalizing should automatically reset the U.S. onto a path of sequential quarterly growth.

May employment data showed growth of 2.5 million jobs after states started reopening.[1] Granted, these were mostly returning workers; but, the return of workers increases the overall foundation for output and consumption. This will undoubtedly be a positive development for the recovery in the coming months. Other data shows maunfacturers optimisitc about the improved business climate ahead.[2]

What Does It Mean for Investors?

It is well recognized re-opening the economy isn't necessarily easy or seamless. Americans must learn how to mutually (a) be active in society and (b) be guarded against an unrelenting virus. In reality, investors should expect a bumpy path as policy makers react and respond to changing case counts, outbreak centers, and new lessons regarding viral spread.

Of course, medical advancements also factor into the recovery. Optimistic views foresee a potential vaccine by early 2021. There is added hope for anti-viral medications by late fall that can reduce the severity and duration of symptoms for those seriously ill. Achievement in both areas can rapidly accelerate the economic recovery process.

Morever, investors must know further fiscal and monetary policy support stands ready. Congress is expected to pass another substantial support package in the coming months. Meanwhile, the Federal Reserve continues to reiterate its commitment to low interest rates and stable markets.

Sources:
[1] U.S. Bureau of Labor Statistics.
[2] IHS Markit Flash US Composite PMI

"With the economy still running at impaired levels, the situation continues to call for more aid. The good news is both political parties appear to agree."

More Fiscal Support on the Way from Congress

Congress readies itself for more economic support in the coming months.

In late-March, with the economy under nation-wide containment policies, Congress urgently passed the Coronavirus Aid, Relief, and Economic Security Act (CARES act). Totaling $2.2 trillion, it was monumental in its size and scope. The CARES act delivered support for both businesses and households, as well as funding for emergency health care measures. Similarly, other developed-world peers from Europe, the UK, and Japan, also spent proportionately in their home countries to fill the gap of lost commerce.

With the economy still running at impaired levels, the situation continues to call for more aid. The good news is both political parties appear to agree. The difficulty, though, is finalizing the policy details.

WHAT'S LIKELY:

State and Local Government Assistance

- The loss of sales tax severely impacted many state and local governments. Considering they employ roughly 13% of the overall U.S. workforce, assistance would help restore jobs back to the economy.

Extending Unemployment Insurance

- During recessions, Congress has a precedence of extending unemployment insurance beyond the normal 26 weeks of assistance.

WHAT'S UP FOR DEBATE:

$600 Weekly Federal Unemployment Supplement

- The extra $600 per week in federal-based unemployment assistance stirred controversy. Many believed it disincentivized a return to work and there is no guarantee it will be extended. Some leaders are proposing a $1,200 "return to work" bonus instead.

Another Direct Payment

- Another round of direct payments will be hotly debated. It likely ends up an important bargaining chip between parties.

Infrastructure Spending

- A timely infrastructure package is enticing. This includes funding highways, waterways, and even next generation technology projects. Not only does infrastructure spending lead to real job creation, but it also carries a high multiplier effect whereby new investment follows.

WHEN CAN THE NEXT BILL BE EXPECTED?

The $600 per week federal unemployment supplement is set to expire on July 31st. Therefore, a sense of urgency hangs on having the new bill resolved and passed prior to that deadline.

After a brief break in early July, the House and Senate resume session July 20th. Expect an intense few weeks as leaders hammer out the final details of a much anticipated support package to help the economy in the back half of 2020.

Mortgage Refinance Window Still Open

Mortgage interest rates reach all-time lows.

One helpful development from the last few months is interest rates have once-again established new all-time lows. As of June 18th, the average interest rate for a 30-year fixed rate conventional mortgage was 3.13%. Likewise, the average for a 15-year fixed rate mortgage rate reached 2.58%.[3]

"As of June 19th, the Mortgage Bankers Association, reported refinancing activity was 76% higher than a year ago."

As of June 19th, the Mortgage Bankers Association (MBA), reported refinancing activity was 76% higher than a year ago.

Home purchasers are responding to the low interest rates as well. The MBA's Purchase Index for home buyers was up 21% from the same week of last year. Additionally, in spite of the recent struggles in home markets, new single-family homes sales increased in May by +12% compared to May, 2019.[4]

It's Official. March Declared the First Month of Recession.

National Bureau of Economic Research makes official statement.

Earlier this month on June 8th, the NBER (National Bureau of Economic Research) made an official declaration stating the previous expansion had ended and a new recession had begun.

This brings an end to the longest stretch of uninterrupted growth in U.S. history at 128 months.

"Even though only a short time has passed since March, the committee cited both the magnitude and breadth of the economic contraction as warranting the formal designation."

Consistent with the declaration, the latest GDP release showed the first quarter contracting at a -5% annualized rate. Expectations for the second quarter growth are varied, with some regional federal reserve experts estimating a contraction ranging from -20% to -45%.[5]

Hope of easing containment restrictions and a much more mobile workforce have many economists looking for a sizeable postive rebound in the 3rd quarter of 2020.

FAST FACTS ABOUT U.S. RECESSION DATING

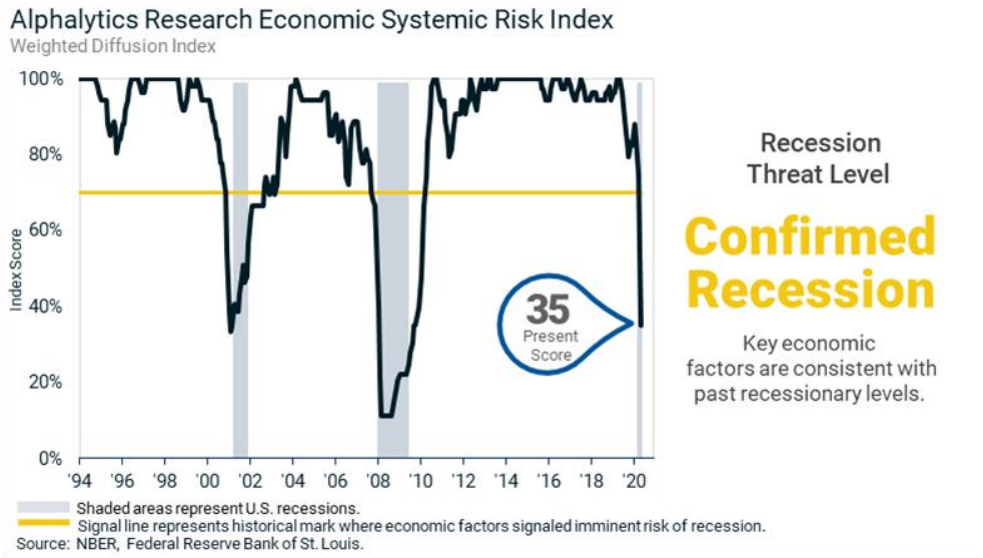
- A recession is generally understood as two consecutive quarters with negative GDP, but the NBER has a much more rigorous standard.
- The NBER's definition is a significant decline across employment, incomes, sales, and production. Conditions must last long enough to qualify as a substantial decline.
- The committee meets only when warranted to assess start and end dates of economic expansions.
- Even though only a short time has passed since March, the committee cited both the magnitude and breadth of the economic contraction as justifying the formal designation in this episode.

Sources:
[3] Freddie Mac.
[4] U.S. Census Bureau.
[5] Federal Reserve Bank of Atlanta, Federal Reserve Bank of New York.

"The National Bureau of Economic Research confirmed the early recession call signaled by the Alphalytics Research Economic Systemic Risk Index."

Business Cycle Risk Profile

- The National Bureau of Economic Research confirmed the early recession call signaled by the Alphalytics Research Economic Systemic Risk Index.
- The Economic Systemic Risk Index reported a score of 35, which is historically consistent with the lows of past recessions (see chart below).
- The present score reflects six indicators scoring consistent with past recessionary conditions. They include home completions, manufacturing new orders, durable goods, retail sales, unemployment claims, and job losers.
- GDP expectations for the second quarter are for an extreme decline. However, the third quarter should see an encouraging rebound.
- Even though the data is still fresh, there are signs of the employment picture reversing toward improvement. Since May 9th, a total of 4.9 million people have come off of unemployment insurance, indicating a return to work for many. (Source: U.S. Employment and Training Administration)



Interpreting the Index Score:

- The index score measures nine economic factors that have demonstrated co-movement with the deteriorating conditions of the past seven recessions dating back to 1970.
- When the index score is at 100, it means all nine of the factors are measuring at levels consistent with past economic expansion.
- When the index score is below 100, it means that one or more of the weighted factors has moved to a level consistent with past economic contractions.
- In aggregate a score of 70 or higher is interpreted as a composite profile consistent with past economic expansion. A score lower than 70 is interpreted as a composite profile consistent with past economic contraction.
- Markets can, and sometimes do, demonstrate volatility even though the economic factors are measuring consistent with expansion.

Interested in Adaptive Business Cycle Investing?

Today's markets, economies, and policies are more complex than ever, challenging investors on what to watch and when to take action.

At Harman Wealth Management, we understand sound investments are uniquely supported by the conditions that favor them. And, when conditions change, so do the investments that benefit.

That's why we conduct rigorous and disciplined tracking of the U.S. business cycle. We also track the cyclical factors that shape our investing environment, like currencies, commodities, and rates. We embrace a world where investing dynamics are constantly evolving and believe it's imperative to have an investment strategy that adapts with it.

With Adaptive Business Cycle Investing we invest consistent with business cycle forces, aligning investments with the conditions driving returns in the present, rather than chasing what worked in the past.

About Harman Wealth Management

At Harman Wealth Management, we provide private, advanced, independent planning and investment management to individuals, families, and institutional clients.

We value in-depth economic research, evidence-based investment methods, and rigorous risk management. We are committed to integrative advanced planning by aligning investment objectives with business cycle opportunities and risks.

At Harman Wealth Management, our aim is to help clients realize their goals within a disciplined, insightful, and rewarding relationship.

For more information about Harman Wealth Management or investing with the business cycle, contact us at 281-719-8601.

Alphalytics Research is a separate business entity from Harman Wealth Management and does not conduct investment advisory services. The owners of Alphalytics Research are members of the Harman Wealth Management team. Alphalytics Research is not affiliated with SagePoint Financial, Inc.

Disclosures:

It is our goal to help investors by identifying changing market conditions. However, investors should be aware that no financial advisor can accurately predict all of the changes that may occur in the market. Information is based on sources believed to be reliable; however, their accuracy or completeness cannot be guaranteed.

Investing involves risk including the potential loss of principal. No investment strategy can guarantee a profit or protect against loss in periods of declining values. Past performance is no guarantee of future results. There is no guarantee that a diversified portfolio will outperform a non-diversified portfolio in any given market environment.

Please note that individual situations can vary. Therefore, the information presented here should only be relied upon when coordinated with individual professional advice.

The Standard and Poor's 500 is an unmanaged index generally representative of the U.S. stock market and cannot be invested in directly.

In general, the bond market is volatile as prices rise when interest rates fall and vice versa. This effect is usually pronounced for longer-term securities. Any fixed income security sold or redeemed prior to maturity may be subject to a substantial gain or loss. Bonds are also subject to other types of risks such as call, credit, liquidity, interest rate, and general market risks.

Securities and advisory services offered through SagePoint Financial, Inc., member /. Harman Wealth Management is a marketing designation. SagePoint Financial, Inc., does not provide any tax or legal advice. Economic research and analysis provided by Alphalytics Research, which is not affiliated with SagePoint Financial, Inc.