The Quarterly Perspective

WRITTEN BY:

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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.

Tracking the Recovery: It's All About Jobs

Returning jobs exceed expectations, show hope for improving outlook.

In a world seemingly turned upside down in 2020, it can be difficult to maintain focus. As the media becomes evermore frenzied, we find the antidote is sticking with facts and fundmentals.

So, then, what would the facts lead us to believe about the economic recovery? According to the progress of returning jobs, there is reason to believe the recovery is real and sustainable.

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- Since peaking in April at 14.7%, the unemployment rate has fallen to 8.4% in August.[1]
  - This is one the fastest recovery rates in unemployment since tracking began in 1948.
  - In comparison, after the last recession in 2009, the unemployment rate peaked at 10%. It took another two full years for the unemployment rate to move below 9%.[2]
- Over 22 million jobs were initially lost in March and April. Since May, more than 10.5 million jobs were gained back.[1]
- Since peaking on May 9th, the amount of people receiving state unemployment benefits has been reduced by half.[2]
  - Over the last 18 weeks, the pace of returning jobs has averaged 685,000 jobs per week.

Additionally, when examining job losses by industry, it is easy to to see how even more jobs can come back quickly. Compared to February, almost 2.4 million jobs remain lost in the health care, state and local government, and education sectors. These have been historically resilient to past recessions, and their essential nature will likely lead to further recovery into 2021.

Likewise, there still remains over 4.4 million jobs lost related to travel, transportation, hotels, and restaurants. While social restrictions will still impede progress in the short-term, it is fair to expect substantial improvement once the U.S. can normalize to a post-pandemic environment. Eventually, demand will return for these industries and service-oriented jobs can't be outsourced overseas.

So, what's it mean for investors?

Arguably, the single most insightful metric for assessing the U.S. economy is job growth. By definition, the high unemployment rate signifies an economy still in distress. However, the improving job growth trend is critical to understanding where GDP growth is going.

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In essence, the workforce is the economy. A growing workforce can materialize into a self-reinforcing loop - leading to greater incomes, greater spending power, greater demand and more jobs.

While the challenges of COVID-19 are far from over, the swift improvement in employment is a much needed foundation for forging ahead.

Source:
[1] Bureau of Labor Statistics
[2] U.S. Employment and Training Administration

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"…evidence shows consumers normalizing to the times and beginning to spend again."

Americans Are Spending Again, Just Differently

Retail consumption sees a return to annual growth

One surprising development over the summer has been the resurgence of retail spending across the U.S. Overall, retail sales grew +2.6% in August over the same month last year. This was the third consecutive month in growth territory.[3]

With elevated unemployment, it would be easy to understand how spending could lock up. Instead, evidence shows consumers normalizing to the times and beginning to spend again. There is a notable difference, however, in the places where consumers are choosing to spend.

Where retail spending is down the most (based on July's data):

- Restaurant sales were down worst in April at -49% from the prior year, but by July restaurants spending was only down -13.4%.
- Traditional department stores were still -40.9% lower from July of last year.
- Sales at gasoline stations, still reeling from lack of commuters and low gasoline prices, saw a decline of -16.2% from a year ago.

Where retail spending is up the most (based on July's data):

- Sporting goods stores: +29.4% higher than July of last year.
- Sales for online retailers increased +27.2% compared to July of 2019.
- Home and garden equipment stores saw a climb of +16.3%.
- Supermarkets and grocers, after a growth surge of +30% in March, still showed a yearly increase in sales of +13.1% as of July.

Where retail spending is returning:

- New Car dealers: up +2.8% annually.
- Furniture and Home Furnishings Stores: up +2.5%.

What's left to be determined is the sustainability of these encouraging trends. Yes, the federal government injected an enormous sum of money into the economy through direct payments and various other aid programs. There is little doubt these programs initiated a spending response, jolting the economy towards recovery.

But also, in response to low interest rates, a sizeable increase in big ticket purchasing has followed. The recovery in housing, in particular, carries a critical role as a spending multiplier. Secondary spending in consumer durable goods tends to follow.

Source: all retail sales data from the U.S. Census Bureau Monthly Retail Trade Report

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Past Performance is No Guarantee of Future Results

The Housing Market Leads as a Bright Spot to the Recovery

Record Low Interest Rates Spur new home buyers.

"Where many would assume housing to freeze up under the strained conditions of 2020, home buying has accelerated."

After a hard stop in April, the housing market has witnessed an impressive rebound. Where many would assume housing to freeze up under the strained conditions of 2020, home buying has accelerated.

Existing home sales for August grew by +10.5% over the same period last year. The uptick in demand outpaced new homes for sale and the available supply fell to the lowest in seven years. In response, homebuilding is beginning to quicken. For August, the National Association of Home Builders Housing Market Index recorded its highest reading in twenty years.

Interestingly, the gains in housing may be fueled by more than just a momentary rebound. We explore three reasons for the stirring growth.

1. **HISTORICALLY LOW INTERST RATES**
The average interest rate for a 30-year fixed rate conventional mortgage reached 2.9%. A 15-year fixed rate mortgage dropped to 2.5%. Both are at record lows.

2. **WORK FROM HOME & URBAN EXODUS**
The work from home arrangements in response to COVID-19 restrictions appear to be sticking. No longer saddled with commutes, many workers are finding the extra space of the suburbs to be attractive.

3. **SHIFTING GENERATIONAL DEMOGRAPHICS**
The millennials, a generation larger than the baby boomers, are now seeing their children reach school age. In place of the efficiency and buzz of urban living, millennials are prioritizing parks, playgrounds, and quality schools offered in the suburbs.

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Existing Home Sales

+10.5%
Growth Since Last Year

Median Home Price

+11.4%
Growth Since Last Year

Residential Home Construction

+0.5%
Growth Since Last Year

Source: All data from Federal Reserve Bank of St. Louis.

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Business Cycle Risk Profile

- The National Bureau of Economic Research declared an official recession beginning in March.
- Encouraging signs that the economy is recovering can be seen in manufacturing, employment, housing, and retail sales which have all grown since bottoming in April.
- The index score currently reflects seven of its nine factors scoring consistent with historical growth. The two remaining indicators are related to employment and tend to lag a recovery.
- After GDP declined -31.7% in the second quarter, expectations for the third quarter are optimistic at +15% to +30%.
- Unemployment declined at an unprecedented pace to 8.4% in August after peaking in April at 14.7%. More than 11 million jobs have come back to the economy in that time span.

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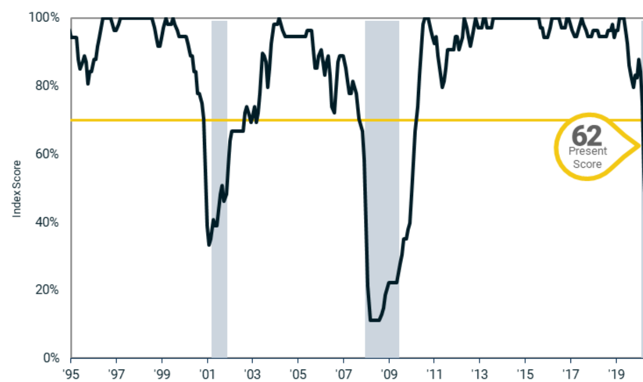
Alphalytics Research Economic Systemic Risk Index
Three Month Average, Weighted Diffusion Index



Shaded areas represent U.S. recessions.
Signal line represents historical mark where economic factors signaled imminent risk of recession.
Source: NBER, Federal Reserve Bank of St. Louis.

State of the Economy
Confirmed Recession

Factors consistent with a recovering economy:

- Home Completions
- New Orders
- Durable Goods
- Retail Sales
- Yield Curve
- Inflation

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.

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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.

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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.

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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.

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