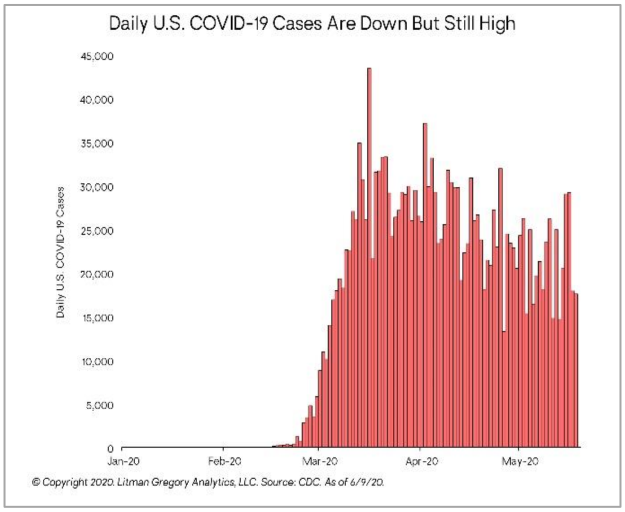
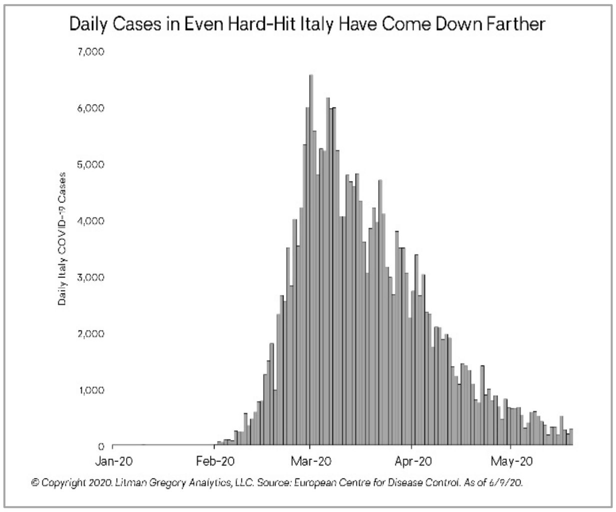
Why Is the Market Still Going Up When COVID-19 Risks Remain?

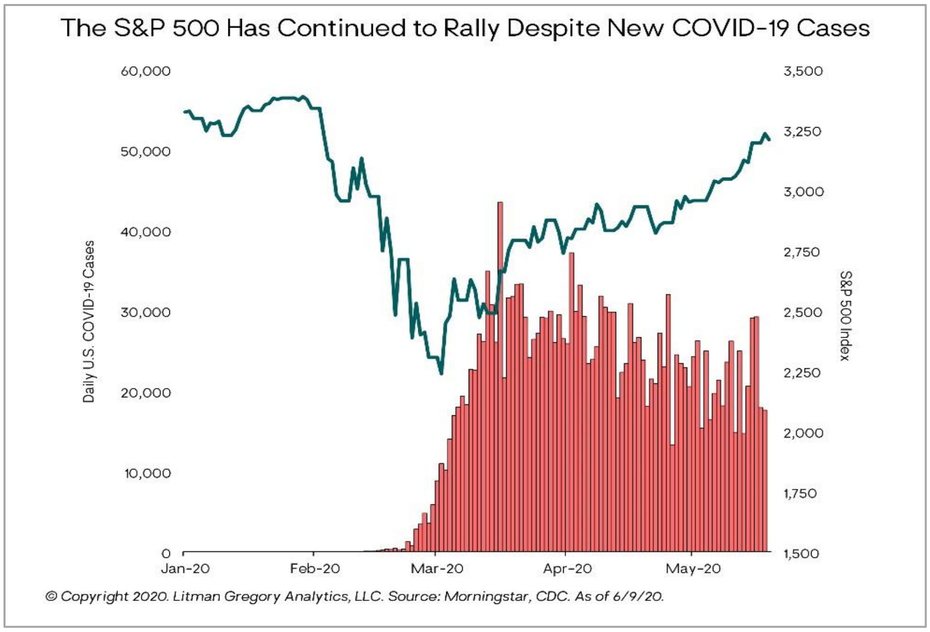
June 10, 2020

In May, we shared a piece called "Why Is the Market Going Up When Economic News Looks Grim?" In it we tried to explain the curious situation where stocks were rebounding as unemployment was rising to historic levels and economists were forecasting a huge drop in economic activity. Since then, the market has rallied even further. The Bespoke Investment Group recently shared a wild statistic: the S&P 500 Index had its best 50-day rally on record since the March low—39.3%. The S&P is now flat since the start of the year, erasing the 30%-plus decline in February/March.





Through all this, stocks seem to be looking past not only terrible economic data, but also the continued spread of COVID-19 in the United States. Daily U.S. cases of COVID-19 have certainly declined since the peak in March, but not nearly as dramatically as they have in China and many countries in Europe. See the charts above comparing the United States and Italy, one of the hardest-hit in Europe initially. Daily new cases are down by just over half in the United States since the peak, while two weeks ago, cases were down 95% in Italy from the peak there (Italy is two weeks ahead of the United States in terms of the virus outbreak timeline).



As of the beginning of June, the United States is still seeing around 20,000 new cases a day. Yet equity investors have also taken this in stride, especially in the United States. It appears they are assuming a best-case scenario in which COVID-19 is eventually contained and a damaging second wave of infections is avoided.

And yet as states reopen (some without meeting CDC guidelines), a continued downward trajectory for cases and deaths is not a given. Moreover, the lingering economic effects of the shutdown periods show in very high unemployment and financial duress for many. And, as we write this, we are witnessing nationwide protests and the demand for structural societal change.

So we understand that it may seem very odd that stocks are continuing to go up. And indeed, they may retrench for a period (it's always good to be prepared for a downturn). Nonetheless, for now this divergence reinforces the important investment lesson we highlighted last month: The market is forward-looking and prices reflect a consensus view about the future. So far, investors expect better days ahead.

—Litman Gregory Investment Team