Weekly Market Missive

Looking on the Bright Side

April 27, 2020

Another wild ride characterized the financial markets last week. While we were gaining ground on the battle against the coronavirus, the price of oil more than completely collapsed on Monday as the price for West Texas Intermediate (WTI) oil futures contracts fell below zero and for a couple of seconds was quoted at a minus $40 per barrel! How can the price of oil be negative? Oil consumers can buy oil contracts for "future" delivery to insure they can match their costs with the prices they charge for their services (think airlines). Speculators get involved in these markets by buying contracts in the hope of making a profit by selling them before they mature with no intention of taking delivery of the actual oil. One oil contract equals 1,000 barrels of oil. Recently the combination of oversupply and collapsing demand for oil due to the coronavirus and a resulting global slowdown has resulted in a record amount of inventory. As the contract for the next delivery approached expiration, speculators panicked again as they could not take delivery of thousands of barrels of oil! As a result, traders had to pay someone to accept the oil that they would have had to receive. The price charged to take the oil was about $40 per barrel! Once the short-term crisis was over, oil climbed back into the $15-$20 per barrel level. But another crisis was around the corner in the form of storage capabilities—limits will be reached by mid-May. Another volatile week is in store for oil prices. For energy consumers, the good news is that gasoline prices are plunging to as low as $1.19 per gallon in Wisconsin. Natural gas prices are also falling allowing for lower heating and air conditioning bills as energy companies that use natural gas as a source of energy production experience favorable input costs.

At the end of last week, the President signed another bill adding $310 billion to the Paycheck Protection Program (PPP). Further increases in government spending is estimated to increase the federal deficit to $2.6 trillion! This deficit compares to the largest budget deficit in history of $1.4 trillion in 2009. Congress is preparing additional federal spending to target states that have lost the most income due to the virus which will further balloon the federal deficit. To provide an even wider safety net under the economy, the Federal Reserve has increased its balance sheet by $1.6 trillion over the last two weeks to support the private sector of the bond market by promising to buy debt issues of both high-yield and investment grade issuers. Even though the deficit mongers are in intensive care, we still do not see how this emergency spending is going to translate to higher inflation or higher interest rates in the foreseeable future.

The U.S. is having a "coming out" party as several states are allowing selected exceptions to the federal lockdown. This change of direction to increase economic activity has not been lost on the stock market. The general stock market has climbed out of "bear" market territory and the S&P 500 is down only 11.7% year-to-date ended April 24th. Favorable day-to-day news on "flattening the curve" relative to new coronavirus cases, progress on therapies and potential vaccines and good earnings numbers in our Information Superhighway and Quality Healthcare themes gives us reason to believe that the stock market rally is sustainable. This week and next are busy with earnings reports. Stay tuned!

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