Market review and outlook

The strong market rebound continued into the third quarter with risk assets finishing in positive territory. However, markets experienced a pullback in September based on fears of a second wave of COVID-19 and uncertainty over the upcoming election. Economic data largely improved from the cycle lows, but the recovery has been uneven. The Federal Reserve (Fed) maintained its accommodative stance and committed to a more flexible inflation target, a key implication short-term interest rates will likely remain lower for even longer. Progress on an additional bipartisan fiscal stimulus bill remained at a standstill as the two sides have been unable to reach an agreement on the size and scope. Although the world appears to be learning to live with COVID-19 and another full lockdown seems improbable, the reopening of the US economy will likely have setbacks on its recovery until the virus is contained or we see meaningful progress on a vaccine.

The S&P 500 Index (S&P 500) fell -3.8% in September but finished the third quarter +8.9%. Year-to-date, the S&P 500 has gained +5.6%. Cyclical sectors, consumer discretionary (+15.1%), materials (+13.3%), and industrials (12.5%) led for the quarter as these sectors received the greatest tailwinds from the reopening of the economy. Information technology (+12.0%) also posted strong returns for the quarter, but stretched valuations led to the sector falling -5.4% in September. Energy (-19.7%) faced large headwinds stemming from declining demand and a growing wave of oil and gas company bankruptcies. Growth-oriented maintained a significant lead over value. Large cap equities are ahead of mid and small cap equities for both the quarter and year-to-date.

The MSCI EAFE Index gained +4.9% for the third quarter but is still down -6.7% year-to-date. Developed international markets benefitted from the reopening of economies, but recent increases in COVID-19 related hospitalizations within the eurozone sparked concerns the trend will continue to rise. Lack of progress in Brexit negotiations weighed heavily on the UK and led to a meaningful depreciation of its currency. The MSCI Emerging Markets Index gained +9.7% for the third quarter, helped by a declining US dollar. China, a key driver of returns for emerging markets, also contributed to performance due in part to its early success in containing the virus.

Investment-grade fixed income, as measured by the Bloomberg Barclays US Aggregate Index, gained +0.6% for the third quarter and +6.8% year-to-date. The 10-year Treasury yield was rangebound, ending the quarter at 0.68%. Credit spreads continued to contract, generating strong returns for the sector. Expanded support from the Fed has served as a tailwind for credit securities as it has flattened the default curve. Municipals finished the quarter slightly above treasuries.

We think the most likely path in the near term is a sideways equity market as we face uncertainty around the upcoming election, ongoing COVID-19 impacts, and a slow, uneven return of the economy. There are catalysts for a near-term pullback, including a contested election, negative impacts from the lack of another fiscal package, or reacceleration in serious COVID-19 cases; however, we view a bear market as a low probability event. A more benign election outcome, a breakthrough in COVID-19 therapeutics or a vaccine, or a broad-based V-shaped rebound in the economy could help drive markets higher in the near term. We will continue to be vigilant in assessing opportunities and positioning appropriately to take advantage of the compelling opportunities through our active multi-asset class approach.

Brinker Capital Market Barometer

We continue to focus on the COVID-19 pandemic and the upcoming election as key drivers for the economy, financial markets, and confidence over the near term. The Federal Reserve remains extremely supportive from a monetary policy perspective, while it remains to be seen whether Washington, DC can agree on another fiscal package. Due to our uneven economic recovery, and uncertainty surrounding the upcoming election, we expect the equity market to remain range-bound in the near term. Overall, the barometer leans neutral to slightly positive, in-line with our modest overweight to risk across portfolios.

SHORT-TERM FACTORS (< 6 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Momentum				●	Momentum remains solid
Trend				●	US markets above 50-day and 200-day moving averages
Investor sentiment			●		Sentiment surveys show optimism but equity outflows continue
Seasonality		●			Seasonality weaker through October, especially during election cycle

INTERMEDIATE-TERM FACTORS (6-36 months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Fiscal policy				●	Strong initial fiscal response; debate on additional package continues
Monetary policy				●	Fed all in to support markets and economy; Global central banks also supportive
Inflation				●	Global inflation low; Fed committed to more flexibility with inflation target
Interest rate environment				●	Treasury yields remain at low levels but stable; yield curve positively sloped
Macroeconomic			●		Macroeconomic data has bottomed; uneven improvement as economy reopens
Business sentiment		●			CEO confidence improved but still weak; small biz optimism improving
Consumer sentiment		●			Increased sharply in August, but remains below pre-pandemic levels
Corporate earnings		●			Looking for improvement after negative impact of COVID-19 on 1H2020 results
Credit environment				●	Credit environment is stable and Fed remains supportive

LONG-TERM FACTORS (36+ months)

	CHANGE	NEGATIVE	NEUTRAL	POSITIVE	
Valuation		●			Equity valuations above long-term averages but not a near-term driver
Business cycle			●		US exited recession that began in February; recovery will be uneven
Demographics			●		Mixed - US and emerging markets positive but developed international negative

Information as of October 8, 2020

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