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THE ECONOMY AT A GLANCE

ECONOMIC HIGHLIGHTS

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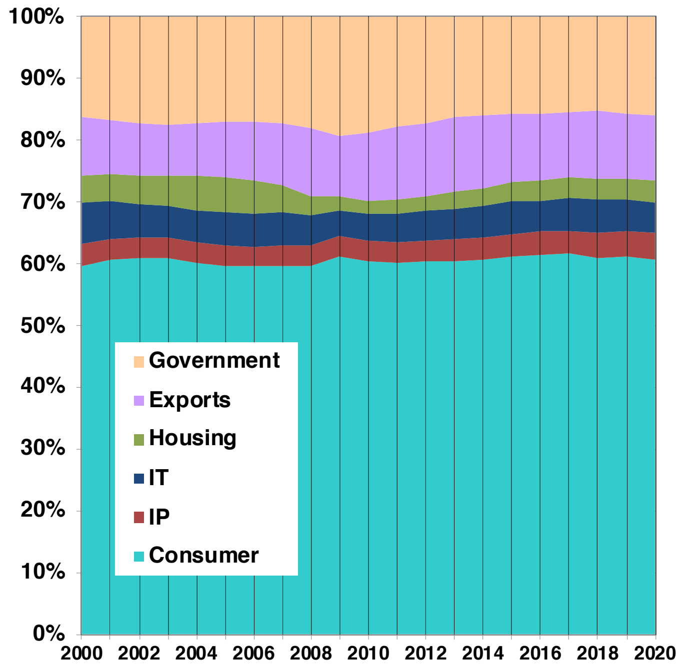
1Q GDP GROWTH RATE REVISED DOWNWARD

The Commerce Department reported that 1Q20 GDP declined at a 5% rate – slightly more than the 4.8% drop announced last month. The results were in line with Street estimates. Because 1Q20 included less than one month of the lockdown, GDP is sure to be even worse in 2Q20. Let's take a closer look at the key contributors to GDP. First, the consumer. During 1Q, personal consumption expenditures declined at a 6.8% pace and contributed 61% of core demand (which we define as personal consumption expenditures, equipment and intellectual property spending, housing, exports and government expenditures). This is in line with the 10-year average, as the consumer sector remains the most important element of the U.S. economy. Investments in intellectual property advanced in the quarter (a rare bright spot at +1.0%) and government spending increased at a 0.8% rate (including a 3.1% surge in nondefense spending that is certain to be higher in 2Q). Capital spending on equipment plummeted 17%, while spending on structures declined 4%; imports also declined, providing a boost to GDP. Deeper in the report, the BEA noted that core inflation rose at 1.6% rate in 1Q, up from 1.2% in the previous quarter.

GDP CONTRIBUTORS



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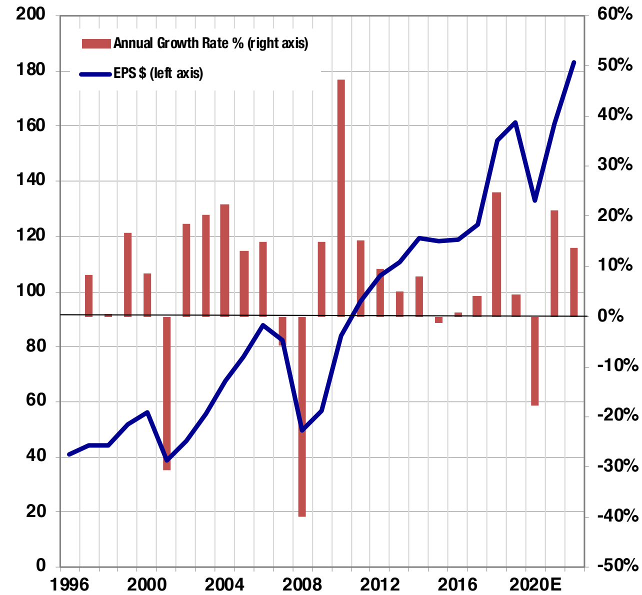
LOWERING EPS ESTIMATES AGAIN

We have reduced our EPS expectations for the S&P 500. Our revisions are based on the now-concluding calendar 1Q20 earnings season, company guidance, and changes in individual analyst estimates at the company-by-company level. The earnings season was a few points worse than we expected. The decline in 2Q20 EPS, which was always modeled as the steepest among the four quarters of 2020, also may be worse than our original expectations. We could begin to see a bounce-back in the fourth quarter. But we are also modeling future years off a lower base, resulting in downward revisions in our 2020 and 2021 forecasts. We have reduced our 2020 estimate of S&P 500 earnings from continuing operations to $133 from $144. While we had been modeling steep drops in Consumer Discretionary, Financial Services, and Energy in the first half of the year, we have added Industrials to the list of deeply distressed sectors. Off the lower base, we have reduced our 2021 forecast for S&P 500 earnings from continuing operations to $161 from $171. Realistically, forecasts even one year out have limited value given that we are in uncharted territory and most companies have withdrawn guidance.

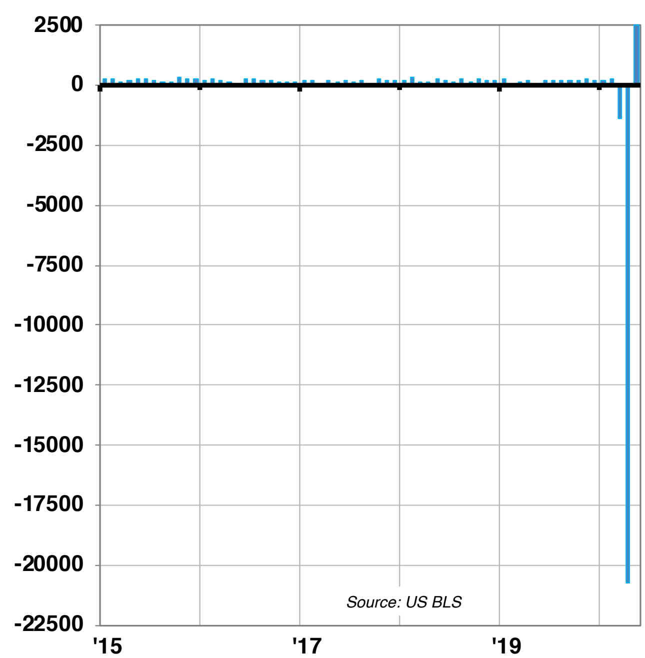
S&P 500 EPS TRENDS & ESTIMATES



POSITIVE PAYROLLS SURPRISE

The U.S. economy added back 2.5 million jobs in May, as companies started to bring employees back to work. The unemployment rate dropped from 14.5% in April to 13.3%. Employment rose sharply in Leisure and Hospitality, Construction, Retail Trade and Health Services, though employee counts in these industries are still well below prepandemic levels. Manufacturing and Business Services also reported growth. The employment data is a bit murky lately. On June 4, the Labor Department reported that another 1.9 million people filed first-time unemployment benefit claims, bringing the total to 40 million since mid-March. Yet continuing claims are stabilizing (currently around 19.3 million). We expect the unemployment rate to remain high through 2020 as the U.S. economy slowly recovers. Fed Chairman Jerome Powell has said that the central bank will use "whatever tools it can" and "for as long as it takes" to bring the economy back. The stock market is already looking ahead to that recovery. We note that the VIX volatility index remains extremely high, and expect volatile trading conditions for an extended period.

NONFARM PAYROLLS
(MONTHLY CHANGE, THOUSANDS OF JOBS)

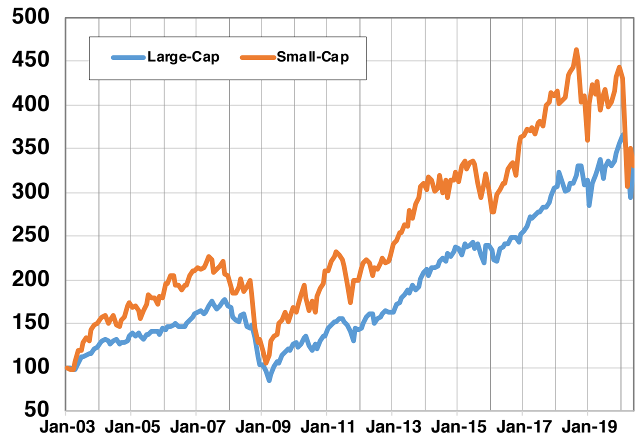


FINANCIAL MARKET HIGHLIGHTS

OPPORTUNITIES AMONG SMALL CAPS

Large-caps have outperformed over the past 12 months, but small- and mid-caps may be in a better position to generate market-beating returns going forward. Many smaller companies are focused on domestic operations and may not be exposed to the global economic uncertainty caused by the coronavirus. But small-caps can be risky. Large-caps outperformed small-caps in 10 of the 17 years of our test period. Annual returns were negative four times for both, but the average decline for small-caps was 16% in down years versus 12% for large-caps. Yet when small-caps rise, they tend to rise sharply. The average annual gain in positive years was 19% for small-caps, versus 16% for large-caps. Despite the risks, diversified investors look to have exposure to small- and mid-caps based on their long-term performance record.

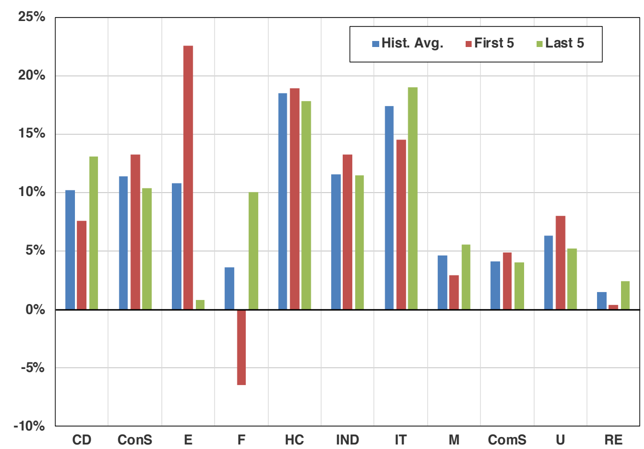
LARGE-CAPS V SMALL-CAPS



TECH SECTOR CONTRIBUTES TO EPS

The Tech sector accounts for about 27% of total market cap -- and that's not including the 11% weighting of Communication Services, which was carved in part out of Tech. The highest weight we recall for a sector was 35% just before the "dot-com" bubble burst in 2000. This time, we note that the lofty weighting is supported, at least in part, by the sector's contribution to overall S&P 500 EPS. We measured each sector's contribution to earnings going back to 2008. Tech and Healthcare have been the biggest contributors, at 17% and 18%, respectively. Tech has been increasingly important. During the first five years of the period, Tech generated 15% of earnings; in the past five years, it generated 19%. In 1Q20, Tech contributed 34% of total S&P 500 profits. On the downside is Energy, which contributed on average 23% of S&P 500 earnings in the first five years and just 1% in the last five years.

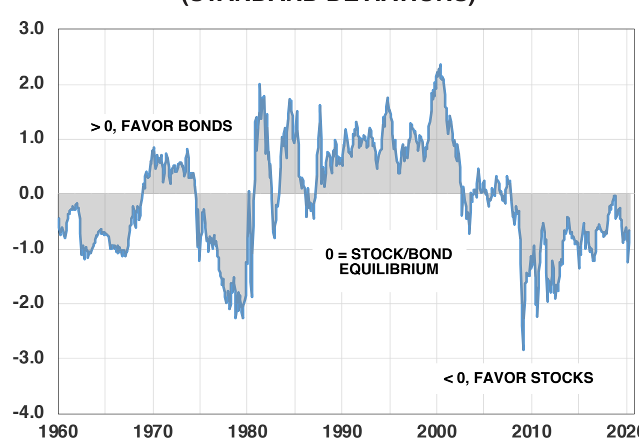
SECTOR CONTRIBUTION TO S&P EPS



STOCKS ABOVE FAIR VALUE, BUT STILL FAVORED

The asset-allocation portion of our bond/stock model favors stocks over bonds, despite the April-May rally in equities. Generally, our model has done a good job of highlighting value. Stocks were very attractive compared to bonds in the late 1970s, when benchmark Treasury rates were in the high teens before heading consistently lower over recent decades. The model indicated that stocks were at a sharp premium to fair value prior to the "dot-com" crash of 2001 and at a premium prior to the Great Recession in 2007-2009. Starting in 2009, the model favored stocks -- another good call, until 1Q20. The model is not perfect: it failed to call the pandemic. But it has responded to changes in prices, rates and EPS forecasts, and it still indicates that stocks are the more attractively valued asset class.

BOND V STOCK BAROMETER
(STANDARD DEVIATIONS)



ECONOMIC CALENDAR

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
10-Jun	Consumer Price Index	May	-0.8%	0.0%	0.0%	NA
	CPI ex-Food & Energy	May	-0.4%	0.0%	0.0%	NA
	FOMC Rate Decision	NA	0-0.25%	0-0.25%	0-0.25%	NA
11-Jun	Producer Price Index	May	-1.3%	0.0%	0.0%	NA
	PPI ex-Food & Energy	May	-0.3%	-0.2%	-0.2%	NA
12-Jun	Import Price Index	May	-2.6%	0.4%	0.4%	NA
	U. of Michigan Sentiment*	June	72.3	76	75	NA

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
22-Jun	Existing Home Sales	May	4.33mm	4.00mm	NA	NA
23-Jun	New Home Sales	May	623k	635k	NA	NA
25-Jun	U.S. Gross Domestic Product	1Q	-5.0%		NA	NA
	GDP Price Index	1Q	1.4%		NA	NA
26-Jun	Personal Income	May	10.5%	0.0%	NA	NA
	Consumer Spending	May	-13.6%	0.5%	NA	NA
	U. of Michigan Sentiment	June	NA	NA	NA	NA

* *Preliminary*
** *Final*
^*Final*

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