As late August fades into September, it’s easy to feel depressed: The days are getting noticeably shorter; the Red Sox are awful; school plans are in disarray; thousands of people are dying every day from Covid-19 while government response remains muddled; and the economy remains mired in deep recession with over 10% unemployment.

But it’s not all bad. There are indeed reasons to be cheerful as the global economy struggles to emerge from the Covid-19 pandemic. Most notably, more than 160 potential vaccines are in various stages of development, with six in their final large-scale trials. The pharmaceutical companies are likely to report on these trials late this year, even as they concurrently ramp up production. Large-scale vaccination programs may be underway in the first half of next year.

The remainder of this commentary takes an admittedly scattershot look at a variety of economic and public health metrics that we have been following through the course of this pandemic. No single chart can tell the entire story, but collectively this data does suggest that the economy is likely to continue its recovery and that markets have room to continue drifting upward.

Let’s start with some public health numbers. Chart 1 shows the trajectory of Covid-19 in the United States, including both total reported cases and average daily new cases:

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The title of this article isn’t just an homage to the full name of Ian Dury’s wonderfully silly 1979 hit single, released just as the U.S. and Europe were plunging into a deep recession caused by the second OPEC oil embargo. It’s also a sequel of sorts to “Connections and Disconnections” (June 15) and “Grendel in Hiding” (May 19), which also found some reasons to be cheerful – or at least hopeful – in this difficult time.
For a short while in the spring, it looked as if we had effectively “flattened the curve,” but premature re-openings led to a massive surge through the early summer. In recent weeks, the number of new cases has again declined, offering hope that this time Americans will be more cautious about protecting themselves and each other.

As the red line in Chart 1 has turned downward, the economy has continued to reopen and gather momentum. The labor market still looks ugly; millions remain unemployed (Chart 2), and millions more have dropped out of the workforce (Chart 3). But signs of hope are also emerging, not least the decline in unemployment rolls and the pickup in labor force participation in the past couple of months. Chart 4 shows that fresh unemployment claims have continued to decline, and Chart 5 shows that companies are posting more job openings. These charts still have a long way to go before they reach pre-Covid levels, but they are at least moving in the right direction.

The slight improvement in the labor markets has helped sustain consumer spending – as has the CARES Act and President Trump’s recent executive order to extend federal supplemental unemployment benefits through year-end. In the initial stages of the lockdowns that rolled across the country in late March and April, consumer spending collapsed because everything was closed. Today, more of the economy is open, and consumers are flush with cash – from savings, from investments, from restored employment, and from government support. The recovery in consumer spending has not been uniform, however.
Chart 6 shows that retail sales have come back astonishingly sharply, and indeed have surpassed their pre-Covid levels. This recovery has been especially beneficial for companies with robust online capabilities (Amazon.com, Target, Wal-Mart, Home Depot, Lowe’s, Best Buy, and others); on the other hand, companies that rely on high-touch service models (upscale department stores, apparel merchants, and impulse-retail places like TJ Maxx or Marshall’s) have not yet seen much improvements. By and large, smaller chains and independent merchants have suffered while larger firms have captured more market share.

Similar dynamics are at play in the restaurant industry (Chart 8), where overall demand is rising after a near-death experience for the industry. Here, too, the strongest corporate earnings reports are coming from larger chains that have adapted well to outdoor dining and take-out services, while smaller chains and independent eateries (especially upscale dining establishments) continue to struggle. As with retail, the quick rebound so far should not be taken as a sign that further recovery will be easy; indeed, the full recovery of indoor dining will likely not happen until large-scale vaccination programs are in place.

Chart 9 shows similar trends farther upstream in the economy. Freight rail traffic has been slowly recovering, partly due to improved retail sell-through and inventory restocking. Other industrial metrics are showing slight gains in volumes, though prices remain depressed.
Not surprisingly, our spending habits – with respect to both time and money – have changed in the past several months. Despite the best efforts of airlines to provide safe environments, Americans have been slow to resume flying (Chart 10). The work-from-home mandates also led to a sharp falloff in urban mass transit usage, which has been even slower to recover (see Chart 11 for a local example).

Without spending time examining all these charts (and more), consumers have developed a fairly keen sense of the current state of the economy. They know that recovery is underway, but they also seem aware that future improvement will be increasingly difficult – that it will depend on reopening theaters and indoor restaurants, that people will need to be willing to cram together on the T or inside TD Garden; until then, the unemployment picture is likely to brighten only slowly. Chart 12 shows that consumer sentiment has improved, but only barely, after plunging in March and April. The proof of economic recovery, it seems, will be in the pudding. 

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2 On the other hand, confidence is clearly volatile. Note the sharp dip in mid-2011 when U.S. Treasury debt was downgraded amid a government budgetary impasse. As soon as Congress agreed on a “sequester” plan, confidence improved rapidly. Note also that the most recent dip in confidence followed the uptick in new Covid-19 cases shown in Chart 1; as case numbers decline, sentiment could reasonably be expected to improve again.
Employers have discovered that worker productivity remains high even when working from home, so they have further delayed returns to the office. Some economists believe that this trend foretells a collapse in commercial real estate values; if productivity remains high, why should employees ever return to the office? And if they don’t, companies will presumably try to unload surplus office space – thereby depressing office rents for a decade as leases gradually expire. The contrary view is that safety protocols will require more square footage per worker, keeping total demand relatively constant. For the moment, this debate will continue without any definitive answer.

One clear ramification of the work-from-home movement, however, is that white-collar workers are investing in their homes. Home Depot, for example, reported shockingly strong results, as sales from stores open at least year jumped 23% in the recently reported period. People are also rediscovering suburbs that may have seemed too far from the city center for a daily commute, fueling a hot residential real estate market. Chart 13 indicates that builders have resumed new construction after a Covid-induced slowdown earlier this year, but it’s clearly not enough; as shown in Chart 14, vacancy rates and for-sale inventories continue to drop, extending a years-long housing crunch.

It’s become fashionable to complain that the financial markets and the real economy have become disconnected, with buoyant markets seemingly ignoring the severe distress so many of us are feeling today. Yet markets focus on the future, and most indicators point to a better economy ahead.3

The markets have also been fueled by extraordinary action by the Federal Reserve and Congress. The CARES Act and other legislation have put trillions of dollars into consumers’ wallets and into businesses’ coffers, which has helped sustain solvency and spending. That, in turn, has boosted corporate profits, as second-quarter reported earnings were far better than investors had feared.

3 Stock prices reflect the prospects of individual companies, not the entire U.S. or global economy (see “Connections and Disconnections,” June 15, 2020). Setting this aside for the moment, the point today is that the prospects for the entire economy are also looking better than they have in many months.
The Fed’s ever-growing engagement has injected liquidity to ensure that markets function smoothly, reduced credit risk from selected markets, brought down interest rates, and flattened the yield curve. All of these actions have drawn money into the nation’s securities markets, pushing asset prices higher.

The combination of congressional and Fed intervention, along with improving profits, can be seen in Chart 15. Low interest rates and ample liquidity have helped drive the stock market’s price/earnings ratio higher, to levels unseen since the dot-com bubble of the late 1990s. Yet the high P/E ratios in 1999 and in 2020 are very different in nature: In 1999, earnings were already strong and interest rates were high; today, earnings expectations are depressed and interest rates are low. In other words, investors in 1999 had a steep bogey to clear, while today’s markets are more forgiving.

So what does this collection of pictures tell us about the state of the economy and markets today? Above all else, the data show that our response to Covid-19 is the key driver of near-term economic activity. Whether by government decree or personal choice, our earnings and our spending are still following the course of the virus. The easiest reopenings have already occurred, and the path ahead will be harder; many businesses will need to reimagine and restructure their operations and products, and consumer confidence needs to be restored. Some industries may never fully recover. But even if the path ahead is rocky, investors are increasingly looking ahead to a large-scale vaccination program and a resumption of economic growth. The initial real-world data indicate that we’re on the right road. Markets also recognize that interest rates are likely to remain close to zero for a long time into the future.

With demand for physical goods and services subdued (for the moment), hopes rising for sustained recovery, and a financial system flush with cash, it seems likely that money will continue to flow into financial assets and thereby to continue to bid up prices. From an investor’s perspective, we have plenty of reasons to be cheerful.

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