What's driving current market behavior?

Presented by Greg B. Thomas

In the era of COVID-19, and the financial woes it has created, I often get asked, “Why is the stock market holding up so well when the economy appears to be struggling?”

To understand why the markets react — or don’t — to certain outside factors, it’s always good to keep in mind that the stock market is not the economy. I can’t stress this enough.

The stock market is considered a “lead economic indicator,” meaning it’s anticipating what economic conditions will look like 6-9 months into the future. While it can sometimes be a tricky concept to grasp, remember that the stock market’s price today reflects potential future economic activity. [1]

Another “lead economic indicator” is building permits. When there is an increase in building permits, it lets us know that developers are bullish about future home sales prospects. If building permits are down, it tells investors that builders may be concerned about interest rates and consumer confidence.[2]

Although helpful in general, lead indicators should never be seen as infallible. Abrupt and unexpected changes will prompt lead indicators to rapidly recalibrate their expectations for the future. Look no further than when COVID-19 grabbed the headlines in early March, which ended the stock market’s 11-year bull market.[3,4]

Keep in mind that in addition to lead indicators, there are lag indicators and coincident (real-time) indicators. We take all three types of indicators into account to help provide context for what can often seem counterintuitive behavior, especially in the face of intense global disruption.

Let me know if you’d like to chat about the economy or any other topics you’re pondering. I’m always here to help.

Greg B. Thomas may be reached at 303-300-4344 or
gt@financialguide.com
www.gtfinancialguide.com

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Citations.

1 - Investopedia.com, April 18, 2020
2 - TheNatureOfMarkets.com, 2020
3 - CNBC.com, April 6, 2020
4 - USNews.com, March 11, 2020