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ECONOMIC TALKING POINTS

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Lessons Learned From June Point To A Feeble Economy The Rest Of 2020

With the 4th of July weekend over, we enter the heart of a summer season that will be far different and disturbing from any other in modern US history.

What makes it unique, of course, is the onslaught of a pandemic that is now afflicting more Americans than ever before. Virtually every state in the country has seen their infection numbers take off again. In fact the US has just recorded the world's highest daily rate of Covid-19 infections, more than 55,000. And the nation's top epidemiologists warn it could spike to 100,000 in the coming weeks.

That should be disturbing enough.

But what makes it all so infuriating are the inane comments from the White House and some in Congress that the US economy is actually on the mend!

So let me step aside a moment to say that we are apolitical. We strive to be right on the 50-yard line when it comes to assessing Administration policies and determining the course of the economy. But we are in the midst of a fast-spreading coronavirus so it is important to look at the latest economic numbers with at least some minimal grain of intellectual honesty.

June's employment numbers last week recorded a 4.8 million increase in nonfarm payrolls and a drop in the jobless rate to 11.1% (from 13.3% in May). That was precisely the data the White House hoped to see as the country entered the holiday weekend. "The economy is roaring back," the President said. His top economic advisor, Larry Kudlow, described the pick-up in payrolls as a "spectacular number." A Congressman from Pennsylvania tweeted the numbers show "the great American comeback continues."

Our perspective of is, well, slightly different. It is oxymoronic to point to the June jobs report and say the economy is "roaring back" when in fact many of those jobs that were restored in May and early June have since been terminated again as the daily infection rates soar.

To make the point clearer let's drill deeper into two specific data sets —last month's employment report and the most recent claims for unemployment benefits.

<u>June Employment Report:</u>

The BLS surveyed the employment landscape during the week from June 7th to the 13$^{th.}$ We know that states like Arizona, Florida, Texas and California began to open up in May and early June. So employers in those states (with help from the Paycheck Protection Program) did indeed call back workers that were temporarily laid off during the lockdown phase. California saw employment increase by 141,600 in May, Florida 182,900, Texas 237,000, Arizona 64,000, Tennessee 93,000, Georgia 79,000) —– and it is highly likely this trend continued into the first days of June. (We'll get the state numbers for June on July 17th.)

But then everything started turning south the second half of June when many of the same states that prematurely opened up and enjoyed a jump in payrolls have since suffered the biggest flare up in infections. That has already led to a new round of dismissals and layoffs in those same regions.

How do we know this?

<u>June's Unemployment Insurance Weekly Claims Report:</u>

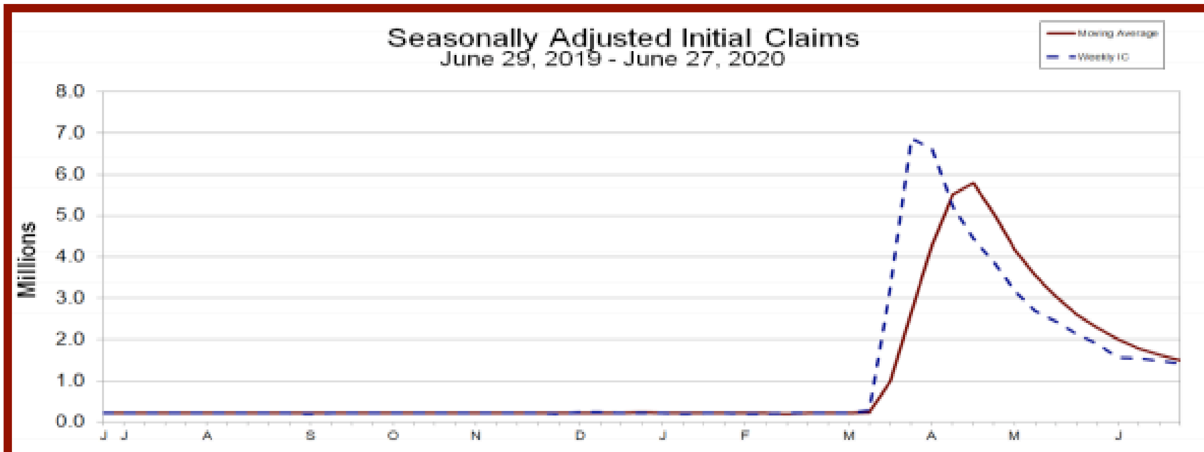
Barely a week after June 12th, the BLS reported that the number of people collecting unemployment insurance from those *very same states* shot up! In the week ending June 20th, the number of people relying on jobless benefits suddenly rebounded by 149,000 in California, 116,000 in Texas and 63,000 in Florida. And that is likely just the start layoffs 2.0. We'll see how many more found themselves dependent on such benefits during the week ending June 27th when the stats are published this Thursday.

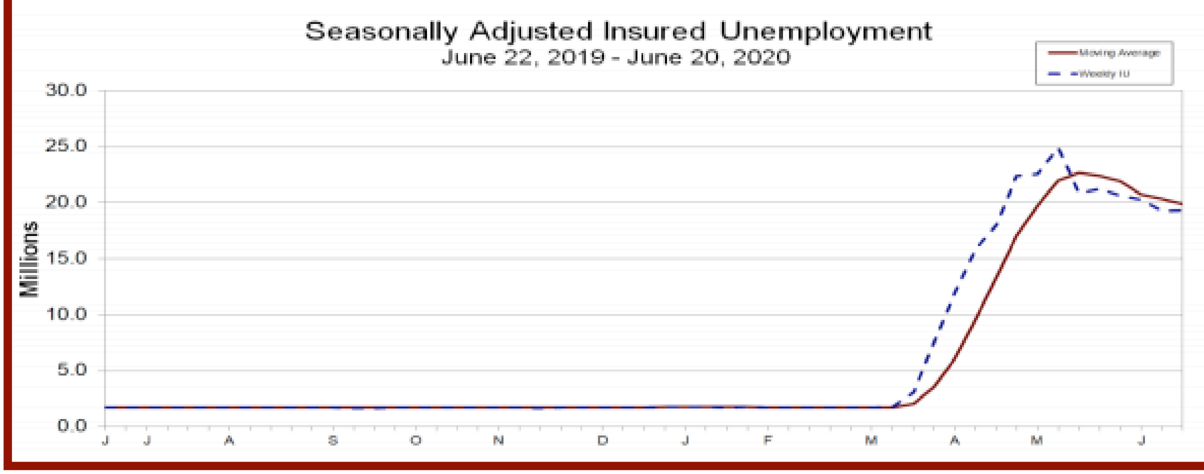
Yet the White House chose to talk up June's employment report despite the fact it was obsolete even *before* it was released. The Administration and others simply disregarded the broader context of what was going on in the labor market. It reminds me of blinders placed on horses so they would only see what's directly in front of them to avoid getting startled by activity around them.

What does this means for the economy the rest of the year?

Let me begin with a cautionary note. The monthly economic indicators that we typically rely on fall short of being useful this time. They were never designed to cope with the extraordinary shock of a fast-moving global pandemic. There is no historical parallel for such a circumstance, so we have to guard ourselves against making rash projections, especially when it is based on a narrow set data.

Our assessment, not surprisingly, is bleaker than the Administration's and its key advisors. The modest traction the economy demonstrated in May and early June is losing momentum. Simply put, the recovery is in danger of stalling again.





The key remains the consumer.

If there is one truism that spans all business cycles (yes, even this one) it is that consumers are the bedrock of the economy. If 65% of US GDP remains fearful of the coronavirus, there's no chance the economy will bounce back in any meaningful way. Though household confidence appears to have perked up lately, that does not necessarily translate into more spending, especially with this virus still lurking. As a result, we do not expect household expenditures to return anywhere close to normal until we get control over Covid-19 — and we're nowhere near that stage.

Another lingering concern for Americans is job security. So long as Covid-19 hangs over the economy, Americans will remain fearful about their jobs. The June unemployment rate of 11.1%, though less than May's 13.3%, is still one of the highest since the 1930s when the US economy suffered its greatest collapse in history. Today, more than 19 million Americans collect unemployment insurance, compared to just 1.7 million in early March.

Many on furlough worry their jobs will be gone by the time the coronavirus is arrested—– and that concern is fully justified. Even the ostensibly upbeat June employment report revealed the number of permanent jobs lost leaped by another 588,000 that month.

There is also a troubling gap in the time line between when Covid-19 no longer poses a threat to the public (about 6 to 18 months from now) and the duration of the enhanced unemployment benefits (Pandemic Unemployment Assistance), which abruptly ends this month.

That PUA was designed to keep households whole so they can pay their mortgages, rent, auto loans, credit card debt, food bills and health care. What Congress will do next, however, is uncertain. It is highly improbable they will extend the current $600/week program. So those out of work are thus rapidly approaching a “cash cliff,” one that is certain to increase household financial stress and likely shut down consumer spending.

Indeed, credit and debt card usage already show signs that consumers are retrenching, according to JPMorgan Chase.

That leads directly to my second point.

Some firms have taken advantage of the government’s Paycheck Protection Program (PPP), which allow firms with 500 employees or less to take out loans that can be converted to grants if they agree to call back workers or retain existing employees at full pay.

But here’s the rub. These small companies have re-opened and called back workers on the assumption that it would be followed by an increase in demand for their products and services. They were counting on a recovery in sales, revenues and profits. But if that demand remains anemic, or if states or cities re-impose restrictions on these businesses as the coronavirus spreads, these firms may not survive much longer.

While it is possible for eligible companies to still seek PPP loans (the program has been extended to August 8th), the $670 billion package is nearly depleted, with 80% of the funds already loaned out. What happens afterwards is unclear. The PPP program is supposed to be a lifeline for small businesses until the economy bounces back. But that is not going to happen until the coronavirus comes under control. If the PPP money runs out AND these businesses do not see a hefty pick up in sales, they will slash their workforce, or just shut their doors permanently.

Sadly, this latter scenario represents our baseline forecast. Unless Congress passes another multi-trillion aid package, which many Senate Republicans have shown a reluctance to do, it would trigger another wave of business failures and leave more people out of work. The result will be a reversal in job gains from last spring and the economy growing at a more subdued rate of below 3% in the second half of the year, after contracting an estimated 16.75% rate in the first half.

This is a perilous moment for the country. What happens next for the economy depends on how much worse the 2nd wave of the coronavirus becomes AND what aid package Congress decides to pass next after it returns from its two-week recess on July 20th.

Key Economic Forecasts

- Actual
- Forecast

United States

	I 2019	II 2019	III 2019	IV 2019	I 2020	II 2020	III 2020	IV 2020	I 2021	II 2021	III 2021	IV 2021	I 2022	II 2022	III 2022	IV 2022
Real Gross Domestic Product (GDP):																
%	3.1	2.0	2.1	2.1	-5.0	-28.5	2.1	3.8	2.2	2.8	2.5	3.1	2.8	4.5	4.0	3.7
Personal Consumption Expenditures:																
PCE %	1.1	4.6	3.2	1.8	-6.8	-24.7	2.4	4.1	2.3	2.5	2.7	3.3	2.4	5.1	4.8	3.7
Inflation, end of period, year-over-year:																
CPI %	1.9	1.6	1.7	2.3	1.5	-4.3	-0.6	1.0	1.3	1.8	1.8	2.0	2.1	2.5	2.3	2.2
Unemployment Rate (end of period):																
%	3.8	3.7	3.5	3.5	3.8	13.0	14.0	10.9	10.6	9.5	9.1	8.0	7.5	6.9	6.2	6.0
Non-farm Payrolls, monthly avg. thousand:																
	174	152	188	210	-142	-4,429	-250	280	780	765	550	1,100	650	320	650	850
Treasury 10-yr Note Yield % (end of period):																
	2.42	2.00	1.65	1.88	0.63	0.65	0.45	0.50	0.75	1.00	1.15	1.20	1.20	1.30	1.38	1.40
Federal funds rate % (end of period):																
	2.38	2.38	1.88	1.63	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.63	1.13

GDP Growth - Global Economy

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
US	2.6	1.6	2.2	1.8	2.5	2.9	1.6	2.4	2.9	2.3	-6.9	2.7	3.8
Eurozone	1.7	1.4	-0.9	-0.2	1.4	2.1	1.9	2.5	1.9	1.2	-8.8	3.5	2.5
United Kingdom	1.7	0.7	0.3	1.8	2.9	2.2	1.9	1.9	1.3	1.5	-10.9	3.8	3.9
Japan	4.6	-0.4	1.6	1.5	-0.1	1.1	0.5	2.2	0.3	0.7	-5.2	2.4	3.2
Canda	3.1	3.1	1.8	2.3	2.9	0.7	1.0	3.2	2.0	1.6	-7.6	4.1	3.4
India	8.4	8.6	6.7	4.9	7.4	8.0	8.1	7.2	6.8	4.2	-4.4	5.9	6.4
China	10.5	9.5	7.8	7.7	7.3	6.9	6.7	6.8	6.6	6.1	1.1	7.2	6.2
Brazil	7.5	2.7	0.9	2.3	0.1	-3.5	-3.5	1.2	1.2	1.1	-6.6	1.9	2.7
Mexico	5.2	4.0	3.9	1.4	2.3	2.7	2.7	2.4	2.1	-0.1	-9.1	1.8	2.8
Australia	2.8	2.6	3.6	2.4	2.6	2.5	2.4	2.4	2.7	1.8	-6.9	4.4	3.8
Russia	4.0	4.3	3.4	1.3	0.6	-2.8	-0.2	1.6	2.5	1.3	-7.5	2.9	3.3
World	4.2	3.1	2.5	2.6	2.8	2.8	2.6	3.4	3.2	2.9	-4.7	3.3	4.2