Daiwa Capital Markets

U.S. Economic Comment

- The virus: hitting hard
- The stimulus package: welcome in the near term; a challenge in the long run

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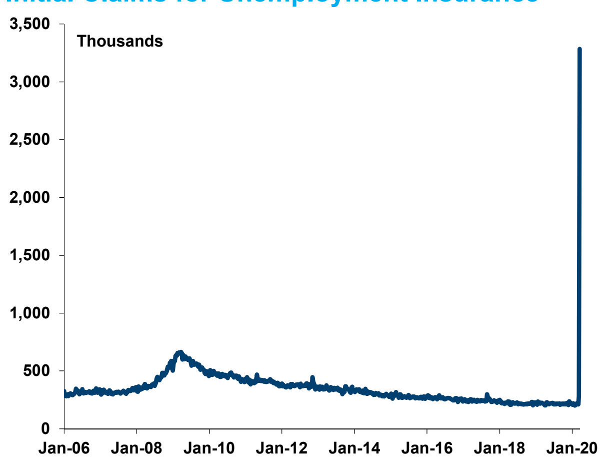
Early Evidence

The surge in claims for unemployment insurance has been well covered by the media, but the latest tally was so striking that we feel compelled to include a chart and a comment in our weekly review. The number of filers in the latest week -- 3.283 million -- was nearly five times larger than two other notable spikes: 695,000 in October 1982 and the 665,000 during the financial crisis (chart, left). The latest observation represents 2.0 percent of the labor force, versus the readings of 0.6 percent in 1982 and 0.4 percent during the financial crisis. The coronavirus is hitting the economy hard.

The striking results on unemployment claims might leave some market participants concerned about the employment report on April 3. The latest payroll and unemployment figures undoubtedly will be weak, but they are not likely to be as dreadful as the latest figure on unemployment claims. The claims figure was for the week ended March 21, which was after the survey period for the employment report. Thus, a surge in the unemployment rate and a collapse in nonfarm payrolls comparable to the shift in unemployment claims are not likely to be evident in the March report, although they will show up in the April data. (The monthly employment statistics represent a snapshot of the labor market in the pay period that contains the 12th day of the month; it is not a review of developments over the course of a given month.)

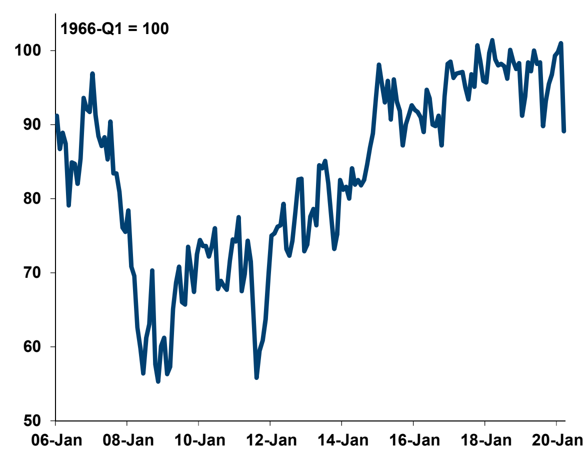
Another report this week also showed the effect of the virus deepening in the second half of March. The index of consumer sentiment published by the University of Michigan Survey Research Center slipped in early March, declining 5.0 percent in the first two weeks of the month. With new survey responses from the second half of the month included, the measure fell an additional 7.1 percent. The new level of the index was still within the range of observations from the past five years, but very much in the low portion of that range (only two observations were slightly lower; chart, right).

Initial Claims for Unemployment Insurance



Sources: U.S. Department of Labor via Haver Analytics

Consumer Sentiment



Source: University of Michigan Survey Research Center via Haver Analytics

With many individuals now out of work and with moods souring, consumer spending is likely to be the key factor pushing the economy lower. In this regard, pre-virus results for consumer spending were not especially encouraging. Each of the past three months (December through February) registered growth of only 0.1 percent in real consumer expenditures, which will probably leave soft results for the first quarter. Even if March were on track for a normal month, consumer spending in the first quarter would register one of its slowest advances of the current expansion. With households likely pulling back in March, growth will probably slip into negative territory (we view flat to -1.5 percent as the reasonable range, annual rate). The second quarter will be worse, with a double-digit decline in real consumer spending possible.

The Stimulus Package

The virus is spreading quickly through the country, but Congress also is moving reasonably fast (lagging the virus and playing catch-up, but moving quickly nonetheless). Consider developments in the past month or so. President Trump initially requested $2 billion to fight the virus, but Congress viewed this as inadequate and provided $8.3 billion. Congress quickly passed a second bill likely to involve $100 billion of support, and it approved a $2 trillion package on Friday (March 27th). From $2 billion to $2 trillion in one month -- remarkable.

We would not be surprised if the package exceeds $2 trillion. We suspect that legislators were able to sneak in numerous provisions that received little scrutiny, which could add noticeably to the total. Even if this is not the case, the bill is sizeable -- representing 9.2 percent of GDP, heftier than the 5.7 percent boost from the 2009 legislation triggered by the financial crisis.

The new bill will not preempt a sharp downturn in the second quarter, but it will be helpful. The increase in unemployment benefits and the cash assistance to households will keep many on (perhaps) sufficient financial ground. Consumer spending will still be weak because many will be sheltering in place, but individuals will be better equipped to keep pace with fixed obligations such as rent and mortgages. Loans and grants to businesses should help prevent layoffs in coming weeks; conceivably, some of those who filed for unemployment benefits in the past two weeks could be recalled quickly.

Long-Run Effects. While the legislation provides welcome relief in the near-term, we wonder about the long-run implications. Is it possible for Congress to go on a spending spree without adverse consequences down the road? Probably not. An analysis of the 2009 stimulus package by the Congressional Budget Office concluded the government's effort provided near-term benefits, but it would most likely reduce output slightly in the long run ("Estimated Impact of the American Recovery and Reinvestment Act on Employment and Economic Output in 2014," February 2015.).

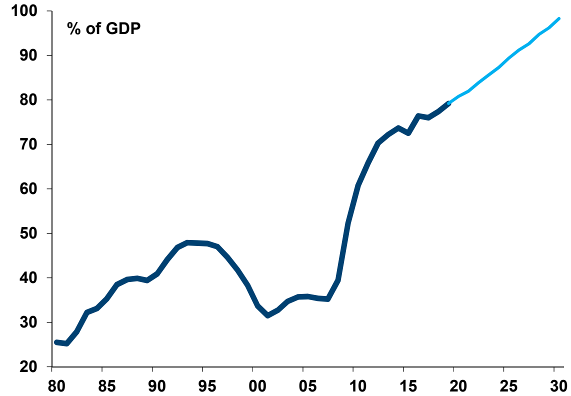
The likely restraint on growth occurred because of the burden of the debt associated with the fiscal support. The outstanding debt of the federal government nearly doubled from the end of 2008 to the end of 2013, moving from $6.4 trillion to $12.4 trillion; as a share of GDP, federal debt over this span rose from 44 percent to 72 percent. (The stimulus flowed into the economy slowly. This five-year period saw 90 percent of the ultimate support). The debt burden left interest rates higher than they would be otherwise, which crowded out private investment and thereby dampened the economy's potential.

The estimated effect was not large (GDP possibly 0.2 percent lower than it would be otherwise), but it also was not trivial. The drag will compound over time and eventually leave standards of living noticeably below where they would be otherwise. One would hope that Congress would take steps in firm economic years to ease debt burdens amassed during recessions, but that has not been the case. In fact, Congress and the Trump Administration have worsened the situation. Wide budget deficits in recent years have pushed debt as a share of GDP to 79 percent at the end of 2019, and the CBO estimates that this ratio (pre-virus) will jump to 98 percent in 2030 (chart, next page). The current stimulus package will lift the CBO projection of the Debt/GDP ratio by nearly 10 percentage points.

Against this background, the earlier estimate of the drag from debt is now irrelevant. With the debt burden now more pronounced, the consequences undoubtedly will be more severe. The slowdown in the rate of economic growth and the constraints on standards of living will be more noticeable and occur sooner than they would have in the past.

Many observers will argue that today's low interest rate environment leaves the debt burden manageable. We do not subscribe to this view. Equilibrium interest rates are low, but wide budget deficits and the accumulation of debt will still push them higher than they would be otherwise. Crowding out will still occur, the nation's capital stock will be lower than it would be otherwise, and economic growth will be slower.

Debt Held by the Public*



** Debt held by the public as a share of GDP calculated on a fiscal year basis. Readings for 2020-2030 (thin blue line) are projections by the Congressional Budget Office.*

Source: Congressional Budget Office via Haver Analytics

We do not mean to be critical of the current legislation. To the contrary, Congress had no choice but to act, and the measures will provide a substantial cushion. However, there will be a price to be paid in terms of slower economic growth in the future if steps are not taken to reduce the existing and coming debt burdens. There is little hope for a reduction in outstanding debt, but reducing debt as a share of GDP (i.e. GDP grows faster than debt) would represent progress.

Review

Week of March 23, 2020	Actual	Consensus	Comments
New Home Sales (February)	**0.765 Million (-4.4%)**	**0.750 Million (-1.8%)**	Sales of new homes were strong in February. Although activity slipped 4.4%, the change occurred from upwardly revised readings in the prior three months, with the combined revisions leaving the level of sales in January 4.7% higher than previously believed. The new level of sales in February represented the second best of the current expansion, trailing only the lofty level in January.
Durable Goods Orders (February)	**1.2%**	**-0.9%**	While new orders for durable goods rose in February, the internals of the report carried a soft tone. All of the advance was a result of a jump of 4.6% in the volatile transportation category, which was heavily influenced by a jump of 32.0% in orders for miscellaneous transportation items (often ships and boats). Results excluding transportation declined 0.6%, continuing a downward drift. New orders for nondefense capital goods excluding aircraft fell 0.8%, offsetting nearly all of the increase in the prior month and reinforcing the downward trend of the past year.
U.S. International Trade in Goods (February)	**$59.9 Billion Deficit ($6.0 Billion Narrower Deficit)**	**$63.5 Billion Deficit ($2.4 Billion Narrower Deficit)**	The merchandise trade deficit improved considerably in February, with exports rising 0.5% and imports falling 2.6%. Some of the decline in imports was the result of the food category giving back some of a surge in January, but sharp declines in imports of consumer goods, industrial supplies, and capital goods were suggestive of soft domestic demand. The results in the first two months of the year raise the possibility of a positive contribution to GDP growth from net exports, but the boost reflects soft imports rather than strong exports.
Revised GDP (2019-Q4)	**2.1% (Unrevised)**	**2.1% (Unrevised)**	Modest adjustments to various components of GDP left growth in the fourth quarter of last year unrevised. The economy performed well in the closing months of 2019, as moderate growth in consumer spending and solid housing activity more than offset weak business investment. Net exports also contributed substantially in Q4.
Personal Income, Consumption, Core Price Index (February)	**0.6%, 0.2%, 0.2%**	**0.4%, 0.2%, 0.2%**	A firm increase in wages boosted personal income in February, as did gains in proprietors' income and rental income. Outlays rose modestly after adjusting for inflation (0.1%), reflecting slow spending on both durable and nondurable goods. The core PCE price index rose 1.8% year-over-year, up one tick from the January reading but below the recent peak of 2.1% in July 2018.
Revised Consumer Sentiment (March)	**89.1 (-6.8 Index Pt. Revision)**	**90.0 (-5.9 Index Pt. Revision)**	The spread of the coronavirus and plunge in equity markets spurred a sharp downward revision to the University of Michigan measure of consumer sentiment in late March (-7.1%). The latest reading pushed the measure to the bottom of the range of the past few year and the lowest monthly print since the fall of 2016.

Sources: U.S. Census Bureau (New Home Sales, Durable Goods Orders, U.S. International Trade in Goods); Bureau of Economic Analysis (Revised GDP, Personal Income, Consumption, Core Price Index); University of Michigan Survey Research Center (Revised Consumer Sentiment); Consensus forecasts are from Bloomberg

Preview

Week of March 29, 2020	Projected	Comments
Conference Board Consumer Confidence (March) (Tuesday)	**110.0 (-15.8%)**	Weekly measures of consumer attitudes showed little deterioration in the first half of March, but slippage intensified in the second half. The early responses to the Conference Board survey will probably prevent a massive decline in the index, although the swoon in the stock market and the growing risks from the coronavirus most likely led to a sizeable drop.
Construction Spending (February) (Wednesday)	**1.0%**	A marked step-up in housing starts in the past three months should lead to a strong advance in residential construction. Private nonresidential activity has been moving along a flat trend, but favorable weather might give a boost in February. Government-related building could ease after a spurt in January.
ISM Manufacturing Index (March) (Wednesday)	**45.0% (-5.1 Pct. Pts.)**	The outlooks and attitudes of purchasing managers most likely slipped because of the coronavirus and the drop in equity values, but various regional measures, as well as the IHS Markit index, suggest a moderate drop rather than a precipitous one.
Trade Balance (February) (Thursday)	**-$40.0 Billion ($5.3 Billion Narrower Deficit)**	The normally stable surplus in service trade is likely to give back some of its surprising increase in January, but the full trade report is likely to be dominated by the already reported narrowing of $6.0 billion in the goods trade deficit.
Factory Orders (February) (Thursday)	**0.3%**	An expected drop of 0.8% in orders for nondurable goods is likely to offset much of the already reported increase of 1.2% in bookings for durable goods. The drop in nondurable orders, while sizeable, will probably be driven primarily by a price-led decline in bookings for petroleum products. Nondurable orders ex-petrol will probably continue the pattern that has been in place since last summer (modest month-to-month change and net sideways movement). The increase in durable orders reflected primarily a jump in bookings for miscellaneous transportation items; durable orders ex-transportation fell 0.6%.
Payroll Employment (March) (Friday)	**-20,000**	Claims for unemployment insurance suggest that layoffs began in the reference period for the monthly employment report (the pay period containing the 12th of the month), and thus the upcoming report is likely to be weak. However, massive layoffs did not begin until the second half of March, suggesting that the payroll results will be less than dreadful.
ISM Nonmanufacturing Index (March) (Friday)	**42.0% (-15.3 Pct. Pts.)**	With most individuals limiting their activity during March, consumption of services most likely plummeted, which will probably lead to a sharp decline in the ISM nonmanufacturing index.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

March/April 2020

Monday	Tuesday	Wednesday	Thursday	Friday
23	**24**	**25**	**26**	**27**
CHICAGO FED NATIONAL ACTIVITY INDEX Monthly / 3-Mo. Avg. Dec -0.46 / -0.22 Jan -0.33 / -0.11 Feb 0.16 / -0.21	**NEW HOME SALES** Dec 0.724 million Jan 0.800 million Feb 0.765 million	**DURABLE GOODS ORDERS** Dec 2.8% Jan 0.1% Feb 1.2% **FHFA HOME PRICE INDEX** Nov 0.3% Dec 0.7% Jan 0.3%	**INITIAL CLAIMS** Mar 07 211,000 Mar 14 282,000 Mar 21 3,283,000 **U.S. INTERNATIONAL TRADE IN GOODS** Dec -$68.5 billion Jan -$65.9 billion Feb -$59.9 billion **ADVANCE INVENTORIES REPORT** Wholesale / Retail Dec 0.0% / -0.1% Jan -0.5% / -0.1% Feb -0.5% / -0.3% **REVISED GDP** GDP / Chained Price 19-Q3 2.1% / 1.8% 19-Q4(p) 2.1% / 1.3% 19-Q4(r) 2.1% / 1.3%	**PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** Inc. / Cons. / Core Dec 0.2% / 0.4% / 0.2% Jan 0.6% / 0.2% / 0.2% Feb 0.6% / 0.2% / 0.2% **REVISED CONSUMER SENTIMENT** Jan 99.8 Feb 101.0 Mar(p) 95.9 Mar(r) 89.1
30	**31**	**1**	**2**	**3**
PENDING HOMES SALES (10:00) Dec -4.3% Jan 5.2% Feb --	**S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX (9:00)** SA / NSA Nov 0.5% / 0.1% Dec 0.4% / 0.0% Jan -- / -- **CHICAGO PURCHASING MANAGERS' INDEX (9:45)** Index / Prices Jan 42.9 / 56.1 Feb 49.0 / 52.9 Mar -- / -- **CONFERENCE BOARD CONSUMER CONFIDENCE (10:00)** Jan 130.4 Feb 130.7 **Mar 110.0**	**ADP EMPLOYMENT REPORT (8:15)** Private Payrolls Jan 209,000 Feb 183,000 Mar -- **CONSTRUCTION SPEND. (10:00)** Dec 0.2% Jan 1.8% **Feb 1.0%** **ISM INDEX (10:00)** Index / Prices Jan 50.9 / 53.3 Feb 50.1 / 45.9 **Mar 45.0 / 45.0** **VEHICLE SALES** Jan 16.9 million Feb 16.8 million **Mar 15.5 million**	**INITIAL CLAIMS (8:30)** **TRADE BALANCE (8:30)** Dec -$48.6 billion Jan -$45.3 billion **Feb -$40.0 billion** **FACTORY ORDERS (10:00)** Dec 1.9% Jan -0.3% **Feb 0.3%**	**EMPLOYMENT REPORT (8:30)** Payrolls / Un. Rate Jan 273,000 / 3.6% Feb 273,000 / 3.5% **Mar -20,000 / 3.8%** **ISM NON-MFG INDEX (10:00)** Index / Prices Jan 55.5 / 55.5 Feb 57.3 / 50.8 **Mar 42.0 / 45.0**
6	**7**	**8**	**9**	**10**
	JOLTS DATA **CONSUMER CREDIT**	**FOMC MINUTES**	**INITIAL CLAIMS** **PPI** **CONSUMER SENTIMENT** **WHOLESALE TRADE**	***GOOD FRIDAY*** **CPI**
13	**14**	**15**	**16**	**17**
FEDERAL BUDGET	**NFIB SMALL BUSINESS OPTIMISM INDEX** **IMPORT/EXPORT PRICES**	**RETAIL SALES** **EMPIRE MFG INDEX** **IP & CAP-U** **BUSINESS INVENTORIES** **NAHB HOUSING INDEX** **BEIGE BOOK** **TIC DATA**	**INITIAL CLAIMS** **HOUSING STARTS** **PHILLY FED INDEX**	**LEADING INDICATORS**

Forecasts in Bold. *(p) = preliminary (2nd estimate of GDP); (r) = revised (3rd estimate of GDP)*

Treasury Financing

March/April 2020

Monday	Tuesday	Wednesday	Thursday	Friday
23	24	25	26	27
AUCTION RESULTS: Rate / Cover 13-week bills 0.000% 3.11 26-week bills 0.080% 2.50	**AUCTION RESULTS:** Rate / Cover 52-week bills 0.260% 2.53 2-year notes 0.398% 2.36 **ANNOUNCE:** $60 billion 4-week bills for auction on March 26 $50 billion 8-week bills for auction on March 26 **SETTLE:** $50 billion 4-week bills $40 billion 8-week bills $20 billion 79-day CMBs	**AUCTION RESULTS:** Margin / Cover 2-year FRN 0.220% 2.91 Rate / Cover 5-year notes 0.535% 2.53	**AUCTION RESULTS:** Rate / Cover 4-week bills 0.000% 4.74 8-week bills 0.000% 3.77 7-year notes 0.680% 2.76 **ANNOUNCE:** $93 billion 13-,26-week bills for auction on March 30 $60 billion 42-day CMBs for auction on March 31 **SETTLE:** $84 billion 13-,26-week bills $26 billion 52-week bills	**SETTLE:** $18 billion 2-year FRNs
30	31	1	2	3
AUCTION: $93 billion 13-,26-week bills	**AUCTION:** $60 billion 42-day CMBs **ANNOUNCE:** $65 billion* 4-week bills for auction on April 2 $55 billion* 8-week bills for auction on April 2 **SETTLE:** $60 billion 4-week bills $50 billion 8-week bills $12 billion 10-year TIPS $40 billion 2-year notes $41 billion 5-year notes $32 billion 7-year notes		**AUCTION:** $65 billion* 4-week bills $55 billion* 8-week bills **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on April 6 $38 billion* 3-year notes for auction on April 7 $24 billion* 10-year notes for auction on April 8 $16 billion* 30-year bonds for auction on April 9 **SETTLE:** $93 billion 13-,26-week bills $60 billion 42-day CMBs	
6	7	8	9	10
AUCTION: $99 billion* 13-,26-week bills	**AUCTION:** $38 billion* 3-year notes **ANNOUNCE:** $70 billion* 4-week bills for auction on April 9 $60 billion* 8-week bills for auction on April 9 **SETTLE:** $65 billion* 4-week bills $55 billion* 8-week bills	**AUCTION:** $24 billion* 10-year notes	**AUCTION:** $70 billion* 4-week bills $60 billion* 8-week bills $16 billion* 30-year bonds **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on April 13 **SETTLE:** $99 billion* 13-,26-week bills	***GOOD FRIDAY***
13	14	15	16	17
AUCTION: $99 billion* 13-,26-week bills	**ANNOUNCE:** $70 billion* 4-week bills for auction on April 16 $60 billion* 8-week bills for auction on April 16 **SETTLE:** $70 billion* 4-week bills $60 billion* 8-week bills	**SETTLE:** $38 billion* 3-year notes $24 billion* 10-year notes $16 billion* 30-year bonds	**AUCTION:** $70 billion* 4-week bills $60 billion* 8-week bills **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on April 20 $28 billion* 52-week bills for auction on April 21 $17 billion* 5-year TIPS for auction on April 23 **SETTLE:** $99 billion* 13-,26-week bills	

**Estimate*