U.S. Economic Comment

- Virus update: mid stages
- Long-run implications of the coronavirus
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Michael Moran
Daiwa Capital Markets America
212-612-6392
michael.moran@us.daiwacm.com

The Coronavirus: Apparently Peaking, but Not Fading

The economic outlook for the United States (and the world) depends importantly on the path of the coronavirus, and thus close monitoring is warranted. The latest news is mildly encouraging, as the number of new cases recorded daily has started to turn a corner after surging in March (chart, left). However, the downward tilt is modest, and the number of new cases is far from the zero value that will exist when (if?) the virus is eradicated.

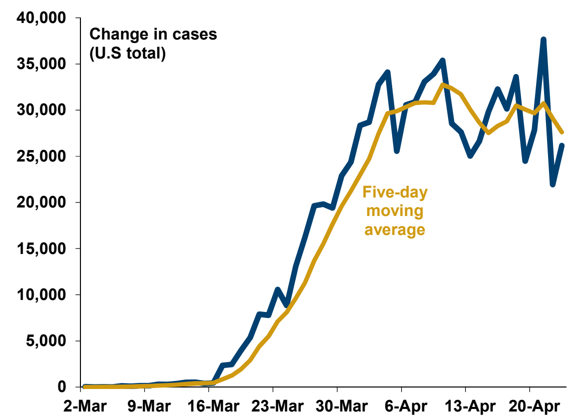
The news from New York is more favorable, as the number of new infections has taken a clear downward turn. The day-to-day variation is wide, but on average the number of new cases is diminishing (chart, right). However, even New York has considerable ground to cover before it reaches zero. In addition, the drop in the number of new cases in New York has a dark side, as it implies that the spread of the disease is picking up elsewhere. That is, if new cases are approximately stable nationwide while they are diminishing in New York, other areas must be showing a faster spread of the virus. All things considered, the available statistics suggest that the United States is in the middle portion of the likely time frame for fighting the coronavirus.

Long-Run Implications of the Virus.

COVID-19 is having obvious severe effects on the economy in the near term. Available data suggest that GDP fell in the first quarter, as the pullback that began in March more than offset a fine performance in the first two months of the year. With the softness persisting, the second quarter will most likely post a monumental decline.

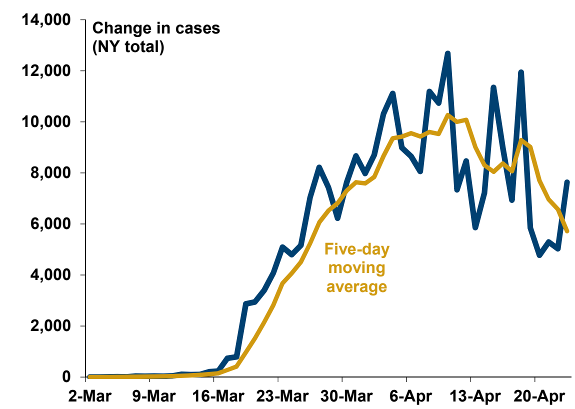
We suspect that the virus will do more than trigger a cyclical swing in the economy. This episode has the feel of a watershed event that will generate structural-like changes in the economy. One can only speculate about what might unfold, but we expect changes in the role of government and shifts in the behavior of businesses and consumers. We offer a few thoughts (not predictions, just thoughts) on possible long-run effects of the virus.

Daily Change in U.S. COVID-19 Cases



Sources: Johns Hopkins University and Medicine Coronavirus Resource Center via Bloomberg

Daily Change in N.Y. COVID-19 Cases



Source: Johns Hopkins University and Medicine Coronavirus Resource Center via Bloomberg

Government. The social safety net is likely to be lifted. Already, we have seen an increase in unemployment benefits. The federal government has increased eligibility for benefits and raised the amount provided to the unemployed. These changes will be difficult to reverse; the next downturn will probably involve a similar degree of support. We suspect that other efforts to help the disadvantaged will be adopted. The virus has generated disproportionate hardship among low-income earners and minorities and exposed challenges and inequalities faced by these individuals. The government will probably review, alter, and expand various support programs.

The virus also has exposed soft spots in the health-care system. The shortage of basic supplies such as protective equipment and test kits is shocking, and limited capacity for intensive care is troubling as well. The government will probably boost its spending for medical research and increase its investment in health-care infrastructure. The virus will probably intensify efforts to provide universal health insurance.

These potential changes in the role of the federal government will involve considerable expenditures at a time when budget deficits are unusually wide and federal debt as a share of GDP will be approaching a record level. Many pundits viewed the pre-virus fiscal path of the United States as unsustainable, and the situation is likely to be more challenging in the future. Major shifts in the tax code are likely to be needed. The situation could well require more than the elimination of tax deductions and the raising of rates. Congress might need to explore new sources of revenue. Carbon taxes are a possibility, or perhaps a value added tax. Some legislators favor a financial transactions tax; perhaps the wealth tax will be debated more seriously.

This world of heavy government involvement and higher taxes leads us to wonder about the potential growth rate of the U.S. economy. An expanded role of the government would involve a shift of resources from the private sector to the government sector, and such a shift would most likely leave the economy less vibrant and on a path of slower underlying growth.

Monetary Policy. The Federal Reserve has responded aggressively to the economic contraction by reducing interest rates, restarting quantitative easing, and introducing or reintroducing credit programs. The balance sheet of the Fed in a few short weeks has increased almost as much as it did over a period of three years during the recession and early portion of the recovery. The strong effort may have set a precedent for the Fed to lead all efforts in stabilizing the economy. What were once viewed as unconventional policies (quantitative easing and providing credit to entities other than depository institutions) might become normal operating procedures. A heightened role for the Fed might be viewed as a welcome development because central banks in most cases can react to adverse developments more quickly than legislatures can.

At the same time, such a role by the Fed is worrisome. Many of the efforts of the central bank this year have involved fiscal-like activities, such as providing direct support to businesses and state and local governments. Such efforts, if used frequently, would most likely pull the Fed more fully into the political realm. The credit programs of the Fed, to a degree, involve picking winners and losers, which will naturally generate heavy lobbying by potential beneficiaries. Congressional leaders and the president also might pressure the Fed in certain directions. We can envision situations where presidents will seek to pack the Fed Board of Governors with individuals that have certain political views or certain leanings in favor of, or against, businesses. Nominations for the Board of Governors could become as politicized as nominations to the Supreme Court.

International Linkages. The tariff wars and America-first posture adopted by President Trump already were affecting trade relationships between the United States and other nations, and the pandemic will probably add momentum to this shift. U.S. producers will wish to establish diverse supply chains that have redundancies, which will weaken trade flows with some countries while strengthening them with others. The net result could involve more or less international trade, but we suspect less is more likely. Shifts away from China could be pronounced.

Businesses. A large share of the workforce, perhaps one-third, is now working remotely. Our experience shows that such arrangements are slightly less efficient than concentrating employees in a centralized work place, but business nevertheless is close to normal. Technology has advanced to such a degree that communication and transactions can proceed smoothly despite marked spatial separations. We suspect that remote working will be used more frequently.

A pickup in remote working could have implications for commercial real estate, as it could dampen demand for office space. The ability to work remotely also could alter more broadly the value placed on face-to-face business dealings, which could reduce the amount of business travel. Heightened sensitivity to the potential spread of pathogens on airplanes also could lead to a drop in business travel.

We wonder about business investment. It could receive a boost from the reworking of supply chains, but a shift of resources to an enlarged government sector could come at the expense of businesses. Enhanced government would need to be financed either through taxes or borrowing, and both would probably have negative consequences for business investment.

Households. We see the potential for a pickup in the personal saving rate. We have heard numerous comments from individuals on the nightly news that they never envisioned using government support programs such as unemployment benefits or loans from the Small Business Administration. Many of these individuals are likely to make an effort to establish or enlarge a precautionary saving balance. It is not hard to imagine spending reductions that might allow individuals to save more. At least for a time, many consumers will avoid events that involve large crowds (concerts, movies and plays, sporting events). Many individuals will probably shy away from air travel.

Any increase in savings balances is likely to be invested in conservative instruments. Many might avoid the equity market because of marked volatility in the past two years or so (a drop of 17 percent in late 2017 and a decline of 33 percent this year).

Living arrangements might change. Both young individuals and those close to or in retirement have shown a preference for city dwelling in recent years because of the richer cultural experience relative to that in the suburbs. However, dense living conditions in cities allow for the easy spread of viruses, which could enhance the appeal of the suburbs.

These are just some thoughts. We do not know what will unfold, but we sense that the coronavirus will generate some enduring changes.

Previews

Q1 GDP (released April 29). The U.S. economy performed well in the first two months of the year before falling off a cliff in March. That pattern leaves a murky outlook for the first quarter; it is not perfectly clear which will dominate, the firm results in January and February or the troubling results in March. As we crunch the numbers, the softness in March will carry the day, leaving a drop in GDP of 2.0 to 2.5 percent (annual rate). In terms of components, consumer spending is likely to be decidedly weak, and business investment is likely to show troubling results as well. Inventory investment should make a sizeable negative contribution. Residential construction and net exports are likely to provide partial offsets to these soft areas.

FOMC (meeting concludes on April 29). We do not expect any new initiatives from the Federal Open Market Committee. The Fed has already pushed short-term interest rates to the zero lower bound, and officials have expressed strong resistance to negative rates. The Fed restarted quantitative easing in mid-March, but it has eased this effort in recent weeks and it will most likely remain on a path of gradual deceleration. The Fed might offer a new credit program, but policymakers and staff seem fully occupied with the 10 programs already announced, as only a few of these efforts are up and running. The weekly Fed balance sheet shows balances for only four programs (Primary Dealer Credit Facility, Money Market Mutual

Fund Liquidity Facility, Paycheck Protection Program Liquidity Facility, and the Commercial Paper Funding Facility), and balances in these efforts total only $91 billion, a pittance relative to potential support in the trillions. We suspect policymakers will focus on developing and enlarging these facilities rather than introducing new ones.

Review

Week of April 20, 2020	Actual	Consensus	Comments
Existing Home Sales (March)	**5.27 Million (-8.5%)**	**5.25 Million (-9.0%)**	The drop in sales of existing homes occurred from an elevated level in February, and thus activity remained within the range seen in the past year or two (only slightly below the average of 5.33 million homes in both 2019 and 2018). This resiliency in the face of the coronavirus might seem surprising, but sales of existing homes are based on closed transactions, and closings in March to a large degree would be based on contracts signed in January and February, before the virus was a major issue in the U.S.
New Home Sales (March)	**0.627 Million (-15.4%)**	**0.642 Million (-16.1%)**	Like other economic indicators, sales of new homes showed notable softening in response to the coronavirus. However, the decline was not as shocking as results in other economic reports. The new level of sales in March trailed the average from last year (684,000), but it remained above results in other years of the latest expansion (e.g. 615,000 in 2018). We suspect that activity was reasonably well maintained in the early portion of the month, when the spread of the virus was in its early stages and low interest rates induced many individuals to sign a purchase contract (new home sales are based on contracts signed rather than closings).
Durable Goods Orders (March)	**-14.4%**	**-12.0%**	The drop in durable goods orders was concentrated in the transportation category, where bookings plunged 41.0%. The weakness in the transportation category was heavily influenced by net cancellations in bookings for commercial aircraft, but it also reflected softness in orders for motor vehicles and miscellaneous items (probably ships and boats). Excluding the transportation component, bookings eased 0.2%, a surprisingly modest change given the potential influence of the coronavirus.
Revised Consumer Sentiment (April)	**71.8 (+0.8 Index Pt. Revision)**	**68.0 (-3.0 Index Pts. Revision)**	Although the consumer sentiment index for April was revised slightly higher, it still posted a record month-to-month decline (off 19.4% versus the previous record of -18.1% in October 2008). The sharp decline pushed the index to the low portion of its historical range, but numerous observations from the past have been lower. The latest reading was well above the record low of 51.7 in 1980 and firmer than the trough of 55.3 during the financial crisis (the index has a base of 100 in 1966-Q1).

Sources: National Association of Realtors (Existing Home Sales); U.S. Census Bureau (New Home Sales, Durable Goods Orders); University of Michigan Survey Research Center (Revised Consumer Sentiment); Consensus forecasts are from Bloomberg

Preview

Week of April 27, 2020	Projected	Comments
U.S. International Trade in Goods (March) (Tuesday)	**-$57.0 Billion ($2.9 Billion Narrower Deficit)**	Slow economic growth in foreign countries is likely to constrain exports, but virus-related disruptions in China are likely to have a greater effect on U.S. imports, leaving a slight improvement in the monthly trade deficit.
Consumer Confidence (April) (Tuesday)	**90.0 (-30.0 Index Pts.)**	Early responses to the March survey probably did not fully reflect the impact of the coronavirus. Further adjustment seems likely in April.
GDP (2020-Q1) (Wednesday)	**-2.5%**	Notable softening in consumer spending, business fixed investment, and inventory investment are likely to more than offset positive contributions from residential construction and net exports, leaving a contraction in Q1 GDP.
Personal Income, Consumption, Core Prices (March) (Thursday)	**-1.0%, -5.0%, -0.1%**	Virus-related layoffs probably led to notable weakness in wages and salaries, and farm income is likely to fall sharply from an elevated, subsidy-driven level in February. On the spending side, stay-at-home restrictions most likely led to a pronounced decline in consumer activity. Results on the CPI suggest that inflation will be tame.
Employment Cost Index (2020-Q1) (Thursday)	**0.7%**	Monthly readings on average hourly earnings suggest a recent pickup in labor compensation, but the advance probably reflected a change in the composition of employment (disproportionate layoffs among low-wage workers) rather than an increase in wage rates. The increase in the employment cost index will probably remain close to the recent average.
ISM Manufacturing Index (April) (Friday)	**40.0% (-9.1 Pct, Pts.)**	Orders, production, and employment were probably further constrained by the coronavirus, which should drive the ISM index well below the neutral level of 50%. The supplier delivery component is likely to remain elevated, reflecting supply-chain disruptions rather than strong demand, which would temper the decline in the headline measure.
Construction Spending (March) (Friday)	**-2.5%**	Continued work on the large number of new homes started in recent months, along with steady building by governments and businesses, ordinarily would lead to a projection of moderate growth in construction. However, the lockdown associated with the coronavirus probably limited activity.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

April/May 2020

Monday	Tuesday	Wednesday	Thursday	Friday
20	21	22	23	24
CHICAGO FED NATIONAL ACTIVITY INDEX Monthly 3-Mo. Avg. Jan -0.27 -0.06 Feb 0.06 -0.20 Mar -4.19 -1.47	**EXISTING HOME SALES** Jan 5.42 million Feb 5.76 million Mar 5.27 million	**FHFA HOME PRICE INDEX** Dec 0.8% Jan 0.5% Feb 0.7%	**UNEMPLOYMENT CLAIMS** Initial Continuing (Millions) Mar 28 6.867 7.446 Apr 04 6.615 11.912 Apr 11 5.237 15.976 Apr 18 4.427 N/A **NEW HOME SALES** Jan 0.777 million Feb 0.741 million Mar 0.627 million	**DURABLE GOODS ORDERS** Jan 0.1% Feb 1.1% Mar -14.4% **REVISED CONSUMER SENTIMENT** Feb 101.0 Mar 89.1 Apr(p) 71.0 Apr(r) 71.8
27	28	29	30	1
27	**U.S. INTERNATIONAL TRADE IN GOODS (8:30)** Jan -$66.0 billion Feb -$59.9 billion **Mar -$57.0 billion** **ADVANCE INVENTORIES REPORT (8:30)** Wholesale Retail Jan -0.6% -0.1% Feb -0.7% -0.3% Mar -- -- **S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX (9:00)** SA NSA Dec 0.4% 0.0% Jan 0.3% 0.0% Feb -- -- **CONFERENCE BOARD CONSUMER CONFIDENCE (10:00)** Feb 132.6 Mar 120.0 **Apr 90.0** **FOMC MEETING**	**GDP (8:30)** GDP Chained Price 19-Q3 2.1% 1.8% 19-Q4 2.1% 1.3% **20-Q1 -2.5% 1.0%** **PENDING HOMES SALES (10:00)** Jan 5.3% Feb 2.4% Mar -- **FOMC DECISION (2:00)**	**INITIAL CLAIMS (8:30)** **PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX (8:30)** Inc. Cons. Core Jan 0.6% 0.2% 0.2% Feb 0.6% 0.2% 0.2% **Mar -1.0% -5.0% -0.1%** **EMPLOYMENT COST INDEX (8:30)** Comp. Wages 19-Q3 0.7% 0.9% 19-Q4 0.7% 0.7% **20-Q1 0.7% 0.7%** **CHICAGO PURCHASING MANAGERS' INDEX (9:45)** Index Prices Feb 49.0 52.9 Mar 47.8 56.7 Apr -- --	**ISM INDEX (10:00)** Index Prices Feb 50.1 45.9 Mar 49.1 37.4 **Apr 40.0 35.0** **CONSTRUCTION SPEND. (10:00)** Jan 2.8% Feb -1.3% **Mar -2.5%** **VEHICLE SALES** Feb 16.7 million Mar 11.4 million **Apr 8.0 million**
4	5	6	7	8
FACTORY ORDERS	**TRADE BALANCE** **ISM NON-MFG INDEX**	**ADP EMPLOYMENT REPORT**	**INITIAL CLAIMS** **PRODUCTIVITY & COSTS** **CONSUMER CREDIT**	**EMPLOYMENT REPORT** **WHOLESALE TRADE**
11	12	13	14	15
	NFIB SMALL BUSINESS OPTIMISM INDEX **CPI** **FEDERAL BUDGET**	**PPI**	**INITIAL CLAIMS** **IMPORT/EXPORT PRICES**	**RETAIL SALES** **EMPIRE MFG. INDEX** **IP & CAP-U** **BUSINESS INVENTORIES** **JOLTS DATA** **CONSUMER SENTIMENT** **TIC DATA**

Forecasts in Bold. (p) = preliminary); (r) = revised

Treasury Financing

April/May 2020

Monday	Tuesday	Wednesday	Thursday	Friday
20	21	22	23	24
AUCTION RESULTS: Rate Cover 13-week bills 0.125% 2.93 26-week bills 0.145% 3.17 43-day CMB 0.120% 2.89	**AUCTION RESULTS:** Rate Cover 52-week bills 0.165% 3.38 119-day CMB 0.110% 3.51 **ANNOUNCE:** $90 billion 4-week bills for auction on April 23 $70 billion 8-week bills for auction on April 23 $30 billion 103-day CMBs for auction on April 22 $30 billion 154-day CMBs for auction on April 22 **SETTLE:** $90 billion 4-week bills $70 billion 8-week bills $30 billion 154-day CMBs	**AUCTION RESULTS:** Rate Cover 103-day CMB 0.105% 3.10 154-day CMB 0.135% 3.08 **SETTLE:** $65 billion 43-day CMBs	**AUCTION RESULTS:** Rate Cover 4-week bills 0.090% 2.92 8-week bills 0.120% 2.53 5-year TIPS -0.320% 2.74 **ANNOUNCE:** $105 billion 13-,26-week bills for auction on April 27 $22 billion 2-year FRNs for auction on April 28 $42 billion 2-year notes for auction on April 27 $43 billion 5-year notes for auction on April 27 $35 billion 7-year notes for auction on April 28 $55 billion 43-day CMBs for auction on April 28 $25 billion 119-day CMBs for auction on April 29 $25 billion 273-day CMBs for auction on April 29 **SETTLE:** $105 billion 13-,26-week bills $28 billion 52-week bills $25 billion 119-day CMBs $30 billion 103-day CMBs	
27	28	29	30	1
AUCTION: $105 billion 13-,26-week bills $42 billion 2-year notes $43 billion 5-year notes	**AUCTION:** $22 billion 2-year FRNs $35 billion 7-year notes $55 billion 43-day CMBs **ANNOUNCE:** $90 billion* 4-week bills for auction on April 30 $70 billion* 8-week bills for auction on April 30 **SETTLE:** $90 billion 4-week bills $70 billion 8-week bills $30 billion 154-day CMBs	**AUCTION:** $25 billion 119-day CMBs $25 billion 273-day CMBs **SETTLE:** $55 billion 43-day CMBs	**AUCTION:** $90 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on May 4 **SETTLE:** $105 billion 13-,26-week bills $22 billion 2-year FRNs $17 billion 5-year TIPS $42 billion 2-year notes $43 billion 5-year notes $35 billion 7-year notes $25 billion 119-day CMBs $25 billion 273-day CMBs	
4	5	6	7	8
AUCTION: $105 billion* 13-,26-week bills	**ANNOUNCE:** $90 billion* 4-week bills for auction on May 7 $70 billion* 8-week bills for auction on May 7 **SETTLE:** $90 billion* 4-week bills $70 billion* 8-week bills	**ANNOUNCE MID-QTR REFUNDING:** $42 billion* 3-year notes for auction on May 11 $29 billion* 10-year notes for auction on May 12 $20 billion* 30-year bonds for auction on May 13	**AUCTION:** $90 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on May 11 **SETTLE:** $105 billion* 13-,26-week bills	
11	12	13	14	15
AUCTION: $105 billion* 13-,26-week bills $42 billion* 3-year notes	**AUCTION:** $29 billion* 10-year notes **ANNOUNCE:** $90 billion* 4-week bills for auction on May 14 $70 billion* 8-week bills for auction on May 14 **SETTLE:** $90 billion* 4-week bills $70 billion* 8-week bills	**AUCTION:** $20 billion* 30-year bonds	**AUCTION:** $90 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on May 18 $30 billion* 52-week bills for auction on May 19 $13 billion* 10-year TIPS for auction on May 21 **SETTLE:** $105 billion* 13-,26-week bills	**SETTLE:** $42 billion* 3-year notes $29 billion* 10-year notes $20 billion* 30-year bonds

**Estimate*