U.S. Economic Comment

- The U.S. economy: prospects for the fourth quarter
- Continued support from consumers
- An uneventful FOMC meeting

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What About Q4?

The economy grew briskly during the third quarter, advancing at an annual rate of 33.1 percent. Despite the surge, output has recouped only 66 percent of the ground lost in the first half of the year, and thus one wonders about prospects for completing the recovery. The U.S. will most likely not return to the pre-virus level of activity in the fourth quarter, as that would require annual growth of 15.2 percent in the closing months of the year, which seems like a reach given the recent acceleration in the number of new Covid cases and the deceleration in several recent economic statistics. Still, the economy appears to remain on a growth track that could return GDP to its pre-pandemic level in the latter part of next year.

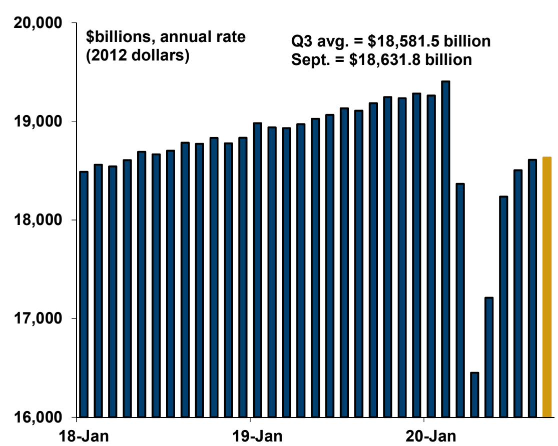
In assessing prospects for activity in the fourth quarter, we would first note that the economy entered Q4 with a fair degree of momentum. That is, the economy seems to have expanded throughout the third quarter, which left activity in October above the third quarter average. Thus, even if the economy expanded no further from the October level, GDP growth in the fourth quarter would remain in the plus column.

The chart below shows the arithmetic involved. The Commerce Department publishes only quarterly data on GDP, but a private-sector research group (IHS Markit) uses the broad array of economic statistics to convert the quarterly averages into monthly totals. The chart shows the tabulations from IHS through August along with a September reading implied by the latest GDP report. The September reading of $18.63 trillion exceeds the Q3 average by $50 billion. The compound annual growth formula used in the GDP statistics translates this difference into annual growth of 1.1 percent. This is an underwhelming advance, but any additional growth in the final months of the year will enhance the increase, which could leave a respectable, perhaps firm, result.

Various economic reports suggest that the economy is likely to continue growing during the fourth quarter. The National Activity Index published by the Chicago Fed suggests the economy is still expanding. This measure is geared to show a value of zero when the economy is growing at its potential rate, and the reading of 0.27 in September was in the upper portion of the range from the previous expansion and consistent with faster than potential growth. This figure can be volatile, and thus we would not rush to judgment on a single observation, but it certainly favors an optimistic view over a pessimistic one.

The index of high-frequency economic indicators developed by the New York Fed (the so-called Weekly Economic Index) also is pointing toward continued growth. This indicator is designed to measure GDP growth in the latest four quarters. The current reading of -3.3 percent after a drop of 4.6 percent in the first three quarters of the year implies an increase of approximately

Monthly GDP*



** The reading for September 2020 (gold bar) is calculated based on results for July and August and real quarterly average GDP reported by the Bureau of Economic Analysis.*

Source: IHS Markit and Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

0.7 percent in the final quarter of 2020. Such an advance would be viewed as disappointing by most observers, but keep in mind that it is based on high-frequency indicators, and thus is providing insights into very recent developments. Conditions can easily change, and we suspect that some indicators, beginning with the employment report on November 6, are likely to show favorable results.

We have been impressed by the recent movement in continuing claims for unemployment insurance (i.e. the number of individuals receiving unemployment benefits). The number of recipients in regular state programs has traced a clear downward trend since mid-May, and the pace of improvement has accelerated in the past two months, with more than 6.7 million leaving the support programs in the past nine weeks. Some of them have exhausted the usual 26 weeks of benefits, but total continuing claims (regular plus extended plus new pandemic-related efforts) also are moving lower (chart, below left). The pronounced shift suggests that individuals are either being recalled to their previous jobs or are finding new work, and the improvement opens the possibility of a strong employment report for October.

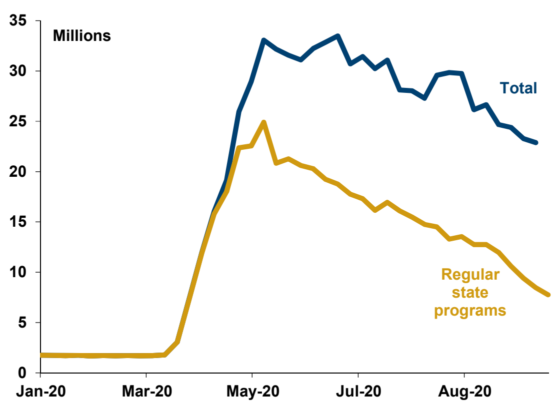
The Resilient Consumer

Perhaps the most important reason for expecting continued growth in Q4 is continued support from U.S. consumers. As is the case with overall GDP, consumer spending entered the fourth quarter with momentum. The level of spending in September was comfortably above the average in the third quarter. Even if real expenditures showed no further growth in the final months of the year, real consumer spending as measured by the GDP accounts would show growth of more than four percent; moderate growth of 0.2 percent per month would leave annual growth of six percent.

Moderate growth of consumer spending over the next three months seems easily achievable, as individuals are likely to have the wherewithal to spend more. Wage income has been moving steadily higher in recent months, and the above-noted improvement in continuing claims for unemployment insurance suggests that job and income growth are likely to continue.

In addition, another form of income has surged in the past few months: nonfarm proprietors' income. In last week's Economic Comment we noted a surge in applications for business tax identification numbers, which could be viewed as an application for a new business. The jump in proprietors' income suggests that many of the proposed businesses are up and running and generating income. This development is perhaps tied to the recent decline in continuing unemployment claims. Those dropping off the unemployment rolls may have

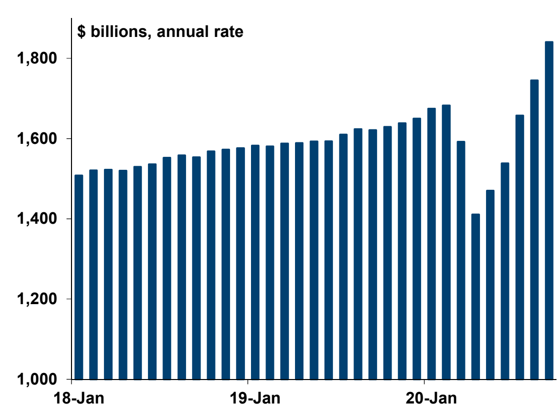
Continuing Claims for Unemployment Insurance*



** Total continuing claims include those filed under regular state programs, extended benefits programs, Pandemic Unemployment Assistance (PUA), and Pandemic Emergency Unemployment Compensation (PEUC). Continuing unemployment claims (regular state programs; gold line) are for the week of October 17th; the total is for the week of October 10th (latest available).*

Source: U.S. Department of Labor, Employment & Training Administration via Haver Analytics

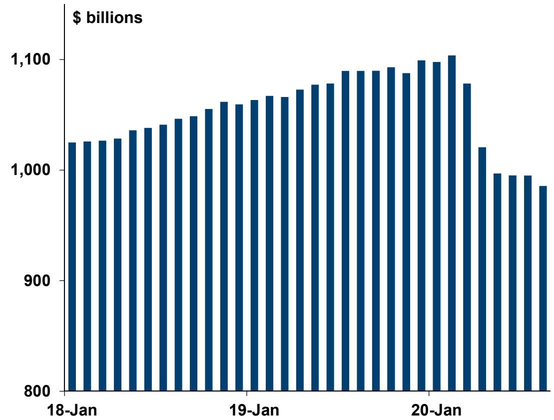
Nonfarm Proprietor's Income



Source: Bureau of Economic Analysis via Haver Analytics shifted to self-employment or started a new small business, which is now fueling proprietors' income.

Another interesting development related to consumers involves the use of credit. Traditional closed-end consumer loans have continued to move along an upward trend (except for a dip in the early stages of the pandemic), but revolving credit (credit-card debt and lines of credit) has declined steadily since the onset of the pandemic (chart). Some of the retreat, especially the declines in the spring, undoubtedly reflected virus-related lockdowns and the associated weakness in spending. However, revolving credit has continued to decline despite an easing in lockdowns and a pickup in consumer spending.

Consumer Credit: Revolving Debt



Source: Federal Reserve Board via Haver Analytics

We view the reduction in revolving credit as partly the result of strong government support to households. The combination of recovery rebate payments and supplemental unemployment benefits left many households better off financially during the late spring and summer than they were before the onset of the pandemic. Some households apparently have used the government support to pare debt.

We have been wondering if the coronavirus might lead to long-lasting changes in consumer behavior, such as leading individuals to hold larger precautionary balances or to invest in less risky portfolios. The reduction in revolving credit lends support to the view that individuals are shifting to more cautious financial practices. Of course, it's early and individuals could revert to previous patterns of saving and investing, but recently there seems to be a tilt toward safety.

FOMC

The Federal Open Market Committee meets on Wednesday and Thursday in the coming week, but we do not expect any meaningful change in policy settings nor any substantive shift in the policy statement. It should be an uneventful meeting.

We see a chance, although a slim one, that the Committee (or Chair Powell in his press briefing) might provide some information on plans for the Fed's asset purchase programs. While the FOMC has provided guidance with respect to interest rates, the Committee has said little about its intentions for quantitative easing. Fed Governor Randal Quarles caused a stir in mid-October by suggesting an extended program of security purchases, and the attention this drew might lead officials to provide some clarification.

The Fed this week tweaked the terms of its Main Street lending facility, which might trigger some discussion of these programs at the press conference. Otherwise, we're not expecting much from the Fed.

Review

Week of Oct. 26, 2020	Actual	Consensus	Comments
New Home Sales (September)	**0.959 Million (-3.5%)**	**1.025 Million (+1.4%)**	Despite a decline in new home sales in September, activity can still be described as firm. Sales rose sharply in June and July, and August added moderately to these advances. The resulting level of activity in August was well above pre-pandemic results (peak of 744,000 annual rate in January), and that remained the case in September. Sales totals in the past three months were the highest since late 2006 (the late phase of the housing bubble).
Durable Goods Orders (September)	**1.9%**	**0.5%**	New orders for durable orders rose for the fifth consecutive month in September and moved into the low portion of the range in 2019 and early 2020. The transportation component contributed noticeably to the overall increase in September (up 4.1%), but bookings elsewhere also were firm, as shown by an increase of 0.8% ex-transportation. Bookings ex-transportation have now eclipsed their pre-virus level. New orders for nondefense capital goods other than aircraft, which provide insight into the outlook for capital spending by businesses, rose 1.0% and are now 2.8% above the pre-virus peak in January.
Consumer Confidence (October)	**100.9 (-0.4%)**	**102.0 (+0.2%)**	The Conference Board's index of consumer confidence dipped in October from a low level, leaving the measure well below results prior to the onset of the pandemic (off 23.9% from the pre-virus peak in February). The sub-par situation in the labor market seems to be affecting consumer attitudes, as the labor market question in this survey shows only a slight tilt toward favorable assessments. In October, 26.5% of respondents indicated that jobs were plentiful versus 19.9% indicating that jobs were hard to get. The net reading of 6.6% was far below readings of more than 35% not long ago.
U.S. International Trade in Goods (September)	**-$79.4 Billion ($3.7 Billion Narrower Deficit)**	**-$84.5 Billion ($1.4 Billion Wider Deficit)**	The trade deficit in goods narrowed noticeably in September, with both exports and imports contributing to the improvement (up 2.7% and down 0.2%, respectively). The increase in exports represented the fourth consecutive increase and kept activity on a recovery path, although below pre-virus totals (exports have thus far recouped 67% of the ground lost in the spring). The decline in imports was modest and followed strong results in other recent months. Imports have now recovered 98.5% of the spring decline.

Review Continued

Week of Oct. 26, 2020	Actual	Consensus	Comments
GDP (2020-Q3)	**33.1%**	**32.0%**	The brisk increase in GDP in the third quarter offset 65.7% of the decline in the first half of the year. Consumer spending was strong in the latest quarter, with an increase of 40.7%. Households also were active in the housing market, as residential construction posted a striking advance of 59.3%. Business investment in new equipment also posted a huge increase (70.1%), but this change was partially offset by a decline in investment in new structures (off 14.6%). Businesses also contributed to economic growth by shifting inventory management (sharp cuts in Q2 to modest trimming in Q3), which translated to a contribution of 6.6 percentage points to GDP growth. Two areas constrained GDP (net exports and government spending). The federal government provided enormous support for the economy in Q3, but most of the outlays were transfer payments, which are not included in GDP.
Personal Income, Consumption, Core Prices (September)	**0.9%, 1.4%, 0.2%**	**0.4%, 1.0%, 0.2%**	Solid job growth in September boosted wage income (0.8%), and the improving economy helped to boost non-farm proprietors' income (5.5%). On the downside, farm income slipped 3.1% after a subsidy-related spike in August, and transfer payments to individuals fell for the fifth consecutive month, although the latest decline was minuscule (off 0.1%). On the spending side, outlays for durable goods were especially firm (3.0%), but spending on nondurable goods and services also were strong. The core PCE price index settled into a trend-like pace after virus-related volatility in prior months.
Employment Cost Index (2020-Q3)	**0.5%**	**0.5%**	Compensation growth posted a restrained increase of 0.5% (not annualized) for the second consecutive quarter after jumping 0.8% in Q1 and averaging 0.7% per quarter in 2019. Wages and benefits have become less sensitive to the degree of slack in the labor market, but elevated unemployment had an influence in the past two quarters.

Sources:; U.S. Census Bureau (New Home Sales, Durable Goods Orders, U.S. International Trade in Goods); The Conference Board (Consumer Confidence); Bureau of Economic Analysis (GDP, Personal Income, Consumption, Core Prices); Bureau of Labor Statistics (Employment Cost Index); Consensus forecasts are from Bloomberg

Preview

Week of Nov. 2, 2020	Projected	Comments
ISM Manufacturing Index (October) (Monday)	**56.0% (+0.6 Pct. Pt.)**	With order flows and employment gains signaling recovery in the manufacturing sector, the ISM index is likely to remain close to the elevated readings in August and September (56.0% and 55.4%, respectively). If the projection is realized, the average in the past three months will represent the best showing in 2019 and thus far in 2020 (although shy of the strong performance in 2018, an average of 58.9%).
Construction Spending (September) (Monday)	**1.5%**	Because of Covid-related uncertainty, businesses will probably remain hesitant to start new construction projects, and new building by state and local governments could be constrained by tight budgets. However, with the housing market in the midst of a brisk recovery, strong residential activity will probably lead to a gain in total construction.
Factory Orders (September) (Tuesday)	**0.7%**	The already reported increase of 1.9% in orders for durable goods should lead to a solid advance in total factory bookings despite a possible decline in orders for nondurable goods. The expected drop in the nondurable area reflects price-led softness in the petroleum and coal category. Orders for nondurable goods other than petroleum products are likely to be pulled higher by the recovery underway in manufacturing activity.
Trade Balance (September) (Wednesday)	**-$63.0 Billion ($4.1 Billion Narrower Deficit)**	The improvement of $3.7 billion in the goods trade balance accounts for most of the expected narrowing in the total trade deficit, but the surplus in service trade also is due for a pickup after disappointing results throughout the spring and summer.
ISM Services Index (October) (Wednesday)	**57.0% (-0.8 Pct. Pt.)**	With the economy in recovery mode, the ISM nonmanufacturing index should remain close to the average of 57.6 in the third quarter, although the acceleration in the spread of the coronavirus is likely to lead to some dampening in the measure.
Nonfarm Productivity (2020-Q3) (Thursday)	**8.0%**	The pronounced swings in output in recent quarters make for a difficult environment to project productivity, but the huge increase in output in Q3 was achieved with a noticeably smaller advance in labor input, which should leave a strong increase in productivity.
Payroll Employment (October) (Friday)	**900,000**	A sharp decline in the number of individuals receiving unemployment benefits suggests that many workers were recalled to their previous jobs or found other work, which should lead to a jump in payroll employment and a drop in joblessness.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

October/November 2020

Monday 26

CHICAGO FED NATIONAL ACTIVITY INDEX

	Monthly	3-Mo. Avg.
July	2.61	4.25
Aug	1.11	3.22
Sept	0.27	1.33

NEW HOME SALES

July	0.965 million
Aug	0.994 million
Sept	0.959 million

Tuesday 27

DURABLE GOODS ORDERS

July	11.8%
Aug	0.4%
Sept	1.9%

FHFA HOME PRICE INDEX

June	1.0%
July	1.1%
Aug	1.5%

S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX

	SA	NSA
June	0.0%	0.3%
July	0.7%	0.8%
Aug	0.5%	1.1%

CONFERENCE BOARD CONSUMER CONFIDENCE

Aug	86.3
Sept	101.3
Oct	100.9

Wednesday 28

U.S. INTERNATIONAL TRADE IN GOODS

July	-$80.0 billion
Aug	-$83.1 billion
Sept	-$79.4 billion

ADVANCE INVENTORIES REPORT

	Wholesale	Retail
July	-0.2%	1.2%
Aug	0.3%	0.5%
Sept	-0.1%	1.6%

Thursday 29

UNEMPLOYMENT CLAIMS

	Initial	Continuing
	(Millions)	
Oct 03	0.767	9.398
Oct 10	0.842	8.465
Oct 17	0.791	7.756
Oct 24	0.751	N/A

GDP

	GDP	Chained Price
20-Q1	-5.0%	1.4%
20-Q2	-31.4%	-1.8%
20-Q3	33.1%	3.6%

PENDING HOMES SALES

July	5.9%
Aug	8.8%
Sept	-2.2%

Friday 30

PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX

	Inc.	Cons.	Core
July	0.9%	1.5%	0.3%
Aug	-2.4%	1.0%	0.3%
Sept	0.9%	1.4%	0.2%

EMPLOYMENT COST INDEX

	Comp.	Wages
20-Q1	0.8%	0.9%
20-Q2	0.5%	0.4%
20-Q3	0.5%	0.4%

CHICAGO PURCHASING MANAGERS' INDEX

	Index	Prices
Aug	51.2	55.0
Sept	62.4	64.7
Oct	61.1	64.6

REVISED CONSUMER SENTIMENT

Aug	74.1
Sept	80.4
Oct(p)	81.2
Oct(r)	81.8

Monday 2

ISM MANUFACTURING INDEX (10:00)

	Index	Prices
Aug	56.0	59.5
Sept	55.4	62.8
Oct	**56.0**	**62.0**

CONSTRUCTION SPEND. (10:00)

July	0.7%
Aug	1.4%
Sept	**1.5%**

Tuesday 3

FACTORY ORDERS (10:00)

July	6.5%
Aug	0.6%
Sept	**0.7%**

VEHICLE SALES

Aug	15.2 million
Sept	16.3 million
Oct	**16.5 million**

Wednesday 4

ADP EMPLOYMENT REPORT (8:15)

	Private Payrolls
Aug	481,000
Sept	749,000
Oct	--

TRADE BALANCE (8:30)

July	-$63.4 billion
Aug	-$67.1 billion
Sept	**-$63.0 billion**

ISM SERVICES INDEX (10:00)

	Index	Prices
Aug	56.9	64.2
Sept	57.8	59.0
Oct	**57.0**	**59.0**

FOMC MEETING

Thursday 5

INITIAL CLAIMS (8:30)

PRODUCTIVITY & COSTS (8:30)

	Productivity	Unit Labor Costs
20-Q1	-0.3%	9.6%
20-Q2	10.1%	9.0%
20-Q3	**8.0%**	**-12.0%**

FOMC DECISION (2:00)

POWELL PRESS CONFERENCE (2:30)

Friday 6

EMPLOYMENT REPORT (8:30)

	Payrolls	Un. Rate
Aug	1,489,000	8.4%
Sept	661,000	7.9%
Oct	**900,000**	**7.5%**

WHOLESALE TRADE (10:00)

	Inventories	Sales
July	-0.2%	4.8%
Aug	0.3%	1.4%
Sept	**-0.1%**	**1.0%**

CONSUMER CREDIT (3:00)

July	$14.7 billion
Aug	-$7.2 billion
Sept	--

Monday 9

Tuesday 10

NFIB SMALL BUSINESS OPTIMISM INDEX

JOLTS DATA

Wednesday 11

VETERANS DAY

Thursday 12

INITIAL CLAIMS

CPI

FEDERAL BUDGET

Friday 13

PPI

CONSUMER SENTIMENT

Monday 16

EMPIRE MFG INDEX

Tuesday 17

RETAIL SALES

IMPORT/EXPORT PRICES

IP & CAP-U

BUSINESS INVENTORIES

NAHB BUILDER SENTIMENT INDEX

TIC DATA

Wednesday 18

HOUSING STARTS

Thursday 19

INITIAL CLAIMS

PHILLY FED INDEX

EXISTING HOME SALES

LEADING INDICATORS

Friday 20

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

Treasury Financing

October/November 2020

Monday	Tuesday	Wednesday	Thursday	Friday
26	27	28	29	30
AUCTION RESULTS: Rate Cover 13-week bills 0.100% 2.90 26-week bills 0.110% 3.49	**AUCTION RESULTS:** Rate Cover 2-year notes 0.151% 2.41 42-day CMB 0.080% 3.44 119-day CMB 0.100% 3.26 **ANNOUNCE:** $30 billion 4-week bills for auction on October 29 $35 billion 8-week bills for auction on October 29 $25 billion 105-day CMBs for auction on October 28 $30 billion 154-day CMBs for auction on October 28 **SETTLE:** $30 billion 4-week bills $35 billion 8-week bills $25 billion 105-day CMBs $30 billion 154-day CMBs	**AUCTION RESULTS:** Spread Cover 2-year FRN 0.055% 3.22 Rate Cover 5-year notes 0.330% 2.38 105-day CMB 0.095% 4.08 154-day CMB 0.105% 3.23	**AUCTION RESULTS:** Rate Cover 4-week bills 0.080% 3.30 8-week bills 0.085% 3.45 7-year notes 0.600% 2.24 **ANNOUNCE:** $105 billion 13-,26-week bills for auction on November 2 $34 billion 52-week bills for auction on November 3 $30 billion 42-day CMBs for auction on November 3 $30 billion 119-day CMBs for auction on November 3 **SETTLE:** $105 billion 13-,26-week bills $30 billion 42-day CMBs $30 billion 119-day CMBs	**SETTLE:** $17 billion 5-year TIPS
2	3	4	5	6
AUCTION: $105 billion 13-,26-week bills **SETTLE:** $22 billion 20-year bonds $26 billion 2-year FRNs $54 billion 2-year notes $55 billion 5-year notes $53 billion 7-year notes	**AUCTION:** $34 billion 52-week bills $30 billion 42-day CMBs $30 billion 119-day CMBs **ANNOUNCE:** $30 billion* 4-week bills for auction on November 5 $35 billion* 8-week bills for auction on November 5 **SETTLE:** $30 billion 4-week bills $35 billion 8-week bills $25 billion 105-day CMBs $30 billion 154-day CMBs	**ANNOUNCE MID-QUARTER REFUNDING:** $54 billion* 3-year notes for auction on November 9 $38 billion* 10-yr notes for auction on November 10 $26 billion* 30-yr bonds for auction on November 12	**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on November 9 **SETTLE:** $105 billion 13-,26-week bills $34 billion 52-week bills $30 billion 42-day CMBs $30 billion 119-day CMBs	
9	10	11	12	13
AUCTION: $105 billion* 13-,26-week bills $54 billion* 3-year notes	**AUCTION:** $38 billion* 10-yr notes **ANNOUNCE:** $30 billion* 4-week bills for auction on November 12 $35 billion* 8-week bills for auction on November 12 **SETTLE:** $30 billion* 4-week bills $35 billion* 8-week bills	***VETERANS DAY***	**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills $26 billion* 30-yr bonds **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on November 16 $25 billion* 20-year bonds for auction on November 18 $12 billion* 10-year TIPS for auction on November 19 **SETTLE:** $105 billion* 13-,26-week bills	
16	17	18	19	20
AUCTION: $105 billion* 13-,26-week bills **SETTLE:** $54 billion* 3-year notes $38 billion* 10-yr notes $26 billion* 30-yr bonds	**ANNOUNCE:** $30 billion* 4-week bills for auction on November 19 $35 billion* 8-week bills for auction on November 19 **SETTLE:** $30 billion* 4-week bills $35 billion* 8-week bills	**AUCTION:** $25 billion* 20-year bonds	**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills $12 billion* 10-year TIPS **ANNOUNCE:** $105 billion* 13-,26-week bills for auction on November 23 $22 billion* 2-year FRNs for auction on November 24 $54 billion* 2-year notes for auction on November 23 $55 billion* 5-year notes for auction on November 23 $53 billion* 7-year notes for auction on November 24 **SETTLE:** $105 billion* 13-,26-week bills	

**Estimate*