U.S. Economic Comment

- The U.S. economy: early evidence on Q4 growth
- FOMC minutes: highly favorable views on QE and 13(3) facilities

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The U.S. Economy: Still Advancing

Revised data on GDP confirmed that the U.S. economy grew vigorously during the third quarter, retracing almost two-thirds of the drop in the first half of the year. The advance was driven by sharp rebounds in consumer spending and residential construction, supplemented by a jump in business fixed investment and a positive contribution from inventory investment. Softer government spending and slippage in net exports provided partial offsets (table).

While the results for the third quarter were encouraging, the economy faces challenges in the fourth quarter and early 2021 because of the recent acceleration in the spread of Covid-19. The tidal wave of data released today hinted that the virus was beginning to exert a drag, but thus far the restraint does not seem strong enough to derail the expansion.

The new report on claims for unemployment insurance suggested an easing in economic activity, as initial claims under regular state programs rose for the second consecutive week. The changes were not large, but consecutive shifts in the upward direction caught our attention. The increase could be the result of normal random volatility, but considering the potential effect of an acceleration in Covid cases, one has to be concerned about fundamental softening in the labor market.

Results for continuing unemployment claims (the number of individuals receiving benefits) were a bit less troubling, as recipients in regular state programs continued to decline. The drop is consistent with individuals being recalled to their previous jobs or finding new work, but it also could reflect individuals exhausting their regular benefits. Exhaustion of benefits seems sizeable, as the total number of recipients (those receiving benefits under regular programs, extended programs, new efforts established by the CARES Act) rose in the latest week. The change was not large, but it represented a break from the downward trend that had been in place and suggests a softening in the tone of the labor market.

Fortunately, the news elsewhere was generally favorable. We were most interested in the report on personal income and consumption, as it provides clues on the likely degree of support from consumers in the fourth quarter. Real consumer expenditures grew 0.5 percent in October after a strong finish in the third quarter. The results raise the prospect of growth in real outlays of approximately six

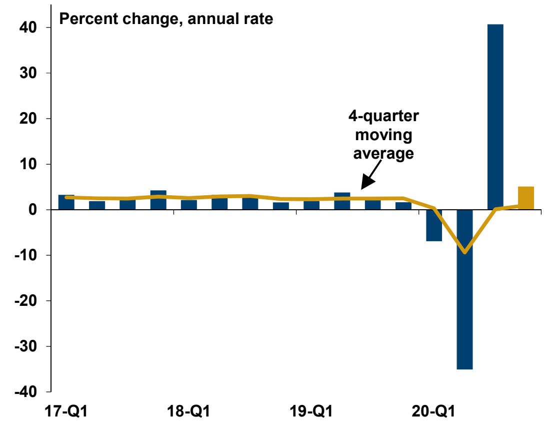
GDP and Related Items*

		20-Q2	20-Q3(a)	20-Q3(p)
1.	**Gross Domestic Product**	-31.4	33.1	33.1
2.	**Personal Consumption Expenditures**	-33.2	40.7	40.6
3.	**Nonresidential Fixed Investment**	-27.2	20.3	21.8
3a.	**Nonresidential Structures**	-33.6	-14.6	-15.8
3b.	**Nonresidential Equipment**	-35.9	70.1	66.6
3c.	**Intellectual Property Products**	-11.4	-1.0	6.0
4.	**Change in Business Inventories (Contribution to GDP Growth)**	-3.5	6.6	6.6
5.	**Residential Construction**	-35.6	59.3	62.3
6.	**Total Government Purchases**	2.5	-4.5	-4.9
6a.	**Federal Government Purchases**	16.4	-6.2	-6.2
6b.	**State and Local Govt. Purchases**	-5.4	-3.3	-4.0
7.	**Net Exports (Contribution to GDP Growth)**	0.6	-3.1	-3.2
7a.	**Exports**	-64.4	59.7	60.5
7b.	**Imports**	-54.1	91.1	93.1
	Additional Items			
8.	**Final Sales**	-28.1	25.5	25.6
9.	**Final Sales to Domestic Purchasers**	-27.1	29.2	29.4
10.	**Gross Domestic Income**	-33.5	--	25.5
11.	**Average of GDP & GDI**	-32.5	--	29.2
12.	**GDP Chained Price Index**	-1.8	3.6	3.6
13.	**Core PCE Price Index**	-0.8	3.5	3.5

* *Percent change SAAR, except as noted*
(a) = advance (1st estimate of GDP); (p) = preliminary (2nd estimate of GDP)
Source: Bureau of Economic Analysis via Haver Analytics

percent in Q4, although we would dampen this view somewhat because of potential constraints from the virus (the chart is showing growth of five percent). The expected increase in Q4 seems trivial relative to recent swings, but it represents a solid performance relative to historical standards, and it would leave consumer spending close to the pre-virus level evident in Q4 of last year. After growth of 5.0 percent in Q4, consumer spending will have retraced 83 percent of the drop in the first half of the year. Spending would need to grow 8.2 percent (annual rate) thereafter to return to the 2019-Q4 level.

Real Consumer Spending*



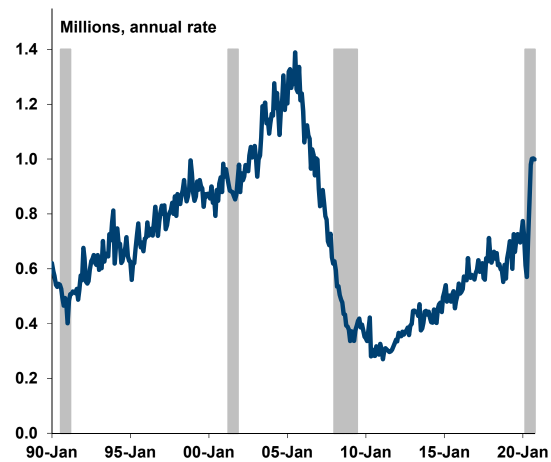
** The reading for 2020-Q4 (gold bar) is an estimate based on results for October.*

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

The results on personal income (a nominal decline of 0.7 percent) shows the nature of the risks. Most income categories were firm (wages up 0.7 percent; investment income up 0.7 percent, rental income up 0.5 percent). Farm income exploded in October, increasing more than 100 percent to a level far above all historical readings. However, we view this surge as a political gambit rather than a fundamental improvement. That is, the surge was probably the result of an effort to get subsidy payments out the door before the elections in November. These sources of strength were more than offset by a drop of 6.2 percent in government transfer payments, as support programs from the CARES Act were fading. We expect additional fiscal stimulus in early 2021, but if it is not forthcoming, consumer spending could falter.

Individuals are likely to be supporting additional growth in Q4 through consumer spending, and they are likely to be active in the housing market as well. A report on sales of existing homes published last week showed strong results, as activity moved into the range seen during the housing bubble. Today's report on sales of new homes also was firm. Sales dipped in October, but the change was modest and it occurred from an upwardly revised level in September. Sales in the past three months were above all observations in the previous expansion and the expansion in the 1990s (although shy of results during the bubble period, chart). The brisk sales pace is likely to generate a solid advance in new home building.

New Home Sales*



** The shaded areas on the chart indicate periods of recession.*

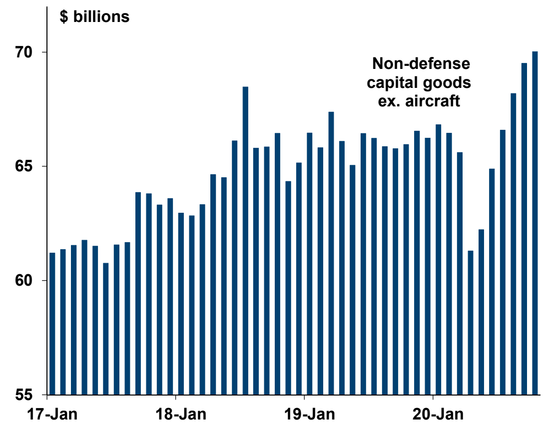
Source: U.S. Census Bureau and National Bureau of Economic Research via Haver Analytics

Today's reports showed favorable prospects for business fixed investment. New orders for durable goods were strong overall, showing growth of 1.3 percent and marking the sixth consecutive increase. The changes in the past several months have retraced 93 percent of the ground lost during the spring. Results for nondefense capital goods other than aircraft, a key series in the outlook for business investment, also rose for the sixth consecutive month, with the gains pushing bookings above the pre-virus readings (chart, next page). Shipments of nondefense capital goods other than aircraft also were firm, indicating favorable prospects in Q4. Shipments of domestically produced capital goods will be supplemented by imports of capital goods, which were strong in October (up 2.4 percent).

The above series relate to capital goods other than aircraft, but we should not ignore aircraft investment. The combination of safety issues at Boeing and reduced travel because of the pandemic has led to pronounced weakness in this sector, which was evident in negative orders for new aircraft (i.e. net cancellations) in five of the six months from March to August. Prospects are perhaps brightening, as both September and October showed positive order flows for commercial aircraft and parts. The magnitudes were not large, but results represented a notable shift from the cancellations in prior months.

Businesses seem to be shifting gears on inventory management. After drawing down stocks of goods sharply in the second quarter, businesses in the aggregate held them approximately steady in the third quarter (actually, another small drawdown). However, results for October suggest that firms will be adding to inventories in Q4, as wholesalers and retailers combined boosted inventories by 0.9 percent in October, and manufacturers of durable goods boosted their stocks of goods by 0.3 percent.

New Orders for Durable Goods



Source: U.S. Census Bureau via Haver Analytics

While prospects seem favorable for several components of GDP, the international trade sector is tilting on the negative side. The nominal trade deficit in goods improved slightly in October from the average in the third quarter, although the change was not large enough to be thinking of a noticeable positive contribution from net exports to GDP growth. Also, the outlook for trade in services is a concern. The U.S. surplus in service trade has diminished noticeably this year as restrictions on travel have weighed more heavily on the U.S. than they have on its major trading partners. With the spread of the virus accelerating in many places around the world, that will probably remain the case, raising the prospect of a drag from net exports. While a constraint on growth seems likely, it will probably be modest relative to the negative contribution of 3.2 percentage points in the third quarter (we are thinking of something in the neighborhood of 0.5 percentage point).

All told, while the acceleration in the number of new Covid-19 cases creates downside risks, the early data for Q4 suggest that the U.S. economy will expand again in the closing months of the year. The picture could change if activity falters in November or December, but at this point, we would look for Q4 economic growth in the neighborhood of four percent.

The FOMC: QE Infinity

As noted by Chair Powell at his latest press briefing, the Federal Open Market Committee had an extended discussion of the Fed's quantitative easing program at its November meeting. The effort received favorable reviews, as officials saw the program as promoting smooth market functioning and fostering accommodative financial conditions.

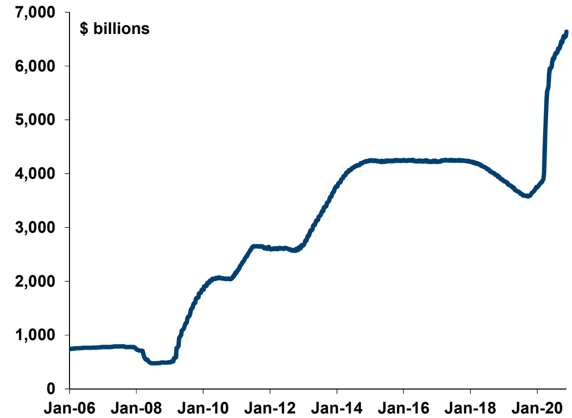
Officials gave little consideration to ending or tapering the effort in the near term. In fact, much of the discussion involved how the program could be altered if policymakers determined additional accommodation was warranted. They noted that the pace of purchases could be increased, or the existing pace could be maintained while shifting purchases to the longer end of the maturity spectrum. Alternatively, the Committee could lengthen the horizon over which the program would be maintained.

The Committee also discussed altering the forward guidance on when the program might change, with the Committee apparently favoring a shift to "qualitative outcome-based guidance". That is, officials are keenly interested in describing the economic conditions that might lead them to alter the amount of asset purchases, but they did not reach any decisions on what those conditions might be. Perhaps they will make progress at their December meeting.

The minutes provided two bits of concrete information on the future of the QE effort. First, when the time comes to tighten monetary policy, the Committee will begin to taper its quantitative easing program before it considers hiking interest rates. Second, once the Committee ceases purchasing assets, it will reinvest maturing securities for a time rather than redeem them; such actions would maintain the size of the Fed's asset portfolio.

In general, we were struck by the dovish tone to the discussion at the November meeting. In reviewing quantitative easing, officials seemed fully on board for extended purchases. There was little thought given to excessive buying or potential distortions to markets. To the contrary, the minutes noted that "asset purchases could also help guard against undesirable upward pressure on longer-term rates that could arise, for example, from higher-than-expected Treasury debt issuance." In other, words, the Committee was fully on board with monetizing federal debt.

Federal Reserve Securities Portfolio*



** The chart shows the Fed's holdings of U.S. Treasury securities, agency securities and agency mortgage-backed securities.*
Source: Federal Reserve Board via Haver Analytics

Similarly with 13(3). There was full-throttled support at this meeting for these credit facilities, and a desire to extend them past the end of the year. It struck us as odd that no official questioned whether the programs had served their purpose and could now be rolled back. Minimal use of the programs might be viewed as prima facie evidence that the programs could be ended, but officials viewed them as important backstops to credit flows. The programs are supposed to be used only in unusual and exigent circumstances. To be sure, conditions in March and April were unusual and exigent, but that does not seem to be the case now. Nonetheless, the Fed wanted to carry on.

Review

Week of Nov. 23, 2020	Actual	Consensus	Comments
Consumer Confidence (November)	**96.1 (-5.3 Index Pts.)**	**98.0 (-2.9 Index Pts.)**	Consumer confidence fell 5.2% in November, continuing the disappointing performance after the pandemic-related drop in March and April. After the drop in November, the index has retraced only 22% of the ground lost in the spring. The surging number of new Covid cases undoubtedly has had a strong influence on attitudes, with sub-par conditions in the labor market probably playing a role as well. In November, the share of survey respondents indicating that jobs were plentiful totaled 26.7% down from a pre-virus average 46.9% in January/February; the share indicting that jobs were hard to get totaled 19.5%, up from 12.9% in January/February. The net response of 7.2% (plentiful less hard to get) was low by historical standards.
U.S. International Trade in Goods (October)	**-$80.3 Billion ($0.9 Billion Wider Deficit)**	**-$80.4 Billion ($1.0 Billion Wider Deficit)**	Imports and exports both rose sharply in October (up 2.2% and 2.8%, respectively), but the change in the dollar volume of imports exceeded that in exports and led to a widening in the goods trade deficit in October.
Durable Goods Orders (October)	**1.3%**	**0.8%**	New orders for durable goods jumped in October from an upwardly revised level in the prior month (results for September were 0.2% firmer than first reported). As of October, durable bookings recovered 93% of the ground lost during the Covid-related drop in the spring. Orders ex-transportation, which already surged above the pre-virus peak, increased 1.3%. Bookings for nondefense capital goods excluding aircraft, which provide insight into future capital spending by businesses, rose 0.7%. The latest move left bookings 4.7% above the pre-virus reading in January.
Revised GDP (2020-Q3)	**33.1% (Unrevised**	**33.1% (Unrevised)**	Modest offsetting adjustments to key components left the second estimate of Q3 GDP unrevised from the preliminary tally.
Personal Income, Consumption, Core Price Index (October)	**-0.7%, 0.5%, 0.0%**	**-0.1%, 0.4%, 0.0%**	Wages and salaries rose solidly in October (0.7%), but a sharp decline in government transfer payments provided an offset (-6.2%). Nominal outlays increased 0.5%. The results were favorable, although they trailed the torrid pace of spending in Q3 (average monthly advance of 1.3%). Both the headline and core price indexes for personal consumption expenditures showed no change on a month-to-month basis. On a year-over-year basis, both the headline and core price indexes slipped 0.2 percentage point to 1.2% and 1.4%, respectively.
New Home Sales (October)	**0.999 Million (-0.3%)**	**0.975 Million (+1.7%)**	Sales of new homes dipped in October, but the decline occurred from an upwardly revised level in the prior month (4.5% firmer than previously believed). Readings in the past few months were above all observations in the previous expansion and the expansion in the 1990s, although well shy of results during the bubble.

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

Preview

Week of Nov. 30, 2020	Projected	Comments
ISM Manufacturing Index (November) (Tuesday)	**57.0% (-2.3 Pct. Pts.)**	The manufacturing sector is continuing to recover, but the elevated reading of the ISM index in October (59.3%) is probably overstating the degree of vigor involved. A moderate correction to a still-firm reading in November seems likely.
Construction Spending (October) (Tuesday)	**1.0%**	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.
ISM Services Index (November) (Thursday)	**56.0% (-0.6 Pct. Pt.)**	High-frequency data suggest that the economy is holding up reasonably well despite an acceleration in the number of new Covid cases, but the service sector is especially vulnerable to the virus, and thus the ISM service index could ease in November.
Payroll Employment (November) (Friday)	**500,000**	A continued downward trend 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 another sizeable increase in nonfarm payrolls. Job growth as measured by the household survey is likely to be well shy of the 2.2 million registered in October, but it should be firm enough to nudge the unemployment rate lower (expecting a decline of 0.2 percentage point to 6.7%).
Trade Balance (October) (Friday)	**-$64.5 Billion ($0.6 Billion Wider Deficit)**	The widening of $933 million in the goods trade balance will probably dominate the full trade report. A dip in the surplus on service trade could add to the shortfall, as continued restrictions on travel weigh more heavily on the U.S. than its major trading partners. A shift in the balance of payments adjustment in favor of the U.S. could provide a partial offset to the expected slippage in goods and service trade.
Factory Orders (October) (Friday)	**0.7%**	The already reported increase of 1.3% in orders for durable goods should account for most of the change in total factory bookings, as the nondurable component is likely to show little change. The expected flat showing in the nondurable area reflects a price-led drop in orders for petroleum and coal products that offsets a moderate advance in nondurable orders ex-petroleum and coal.

Source: Forecasts provided by Daiwa Capital Markets America

Daiwa Capital Markets

Economic Indicators

November/December 2020

Monday 23

CHICAGO FED NATIONAL ACTIVITY INDEX

	Monthly	3-Mo. Avg.
Aug	1.10	3.22
Sept	0.32	1.37
Oct	0.83	0.75

Tuesday 24

FHFA HOME PRICE INDEX

July	1.2%
Aug	1.5%
Sept	1.7%

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

	SA	NSA
July	0.8%	0.8%
Aug	1.4%	1.2%
Sept	1.3%	1.2%

CONFERENCE BOARD CONSUMER CONFIDENCE

Sept	101.3
Oct	101.4
Nov	96.1

Wednesday 25

UNEMPLOYMENT CLAIMS

	Initial	Continuing (Millions)
Oct 31	0.757	6.798
Nov 07	0.711	6.370
Nov 14	0.748	6.071
Nov 21	0.778	N/A

U.S. INTERNATIONAL TRADE IN GOODS

Aug	-$83.1 billion
Sept	-$79.4 billion
Oct	-$80.3 billion

ADVANCE INVENTORIES REPORT

	Wholesale	Retail
Aug	0.5%	0.5%
Sept	0.7%	1.7%
Oct	0.9%	0.8%

REVISED GDP

	GDP	Chained Price
20-Q2	-31.4%	-1.8%
20-Q3(a)	33.1%	3.6%
20-Q3(p)	33.1%	3.6%

DURABLE GOODS ORDERS

Aug	0.4%
Sept	2.1%
Oct	1.3%

PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX

	Inc.	Cons.	Core
Aug	-2.5%	1.2%	0.3%
Sept	0.7%	1.2%	0.2%
OCT	**-0.7%**	**0.5%**	**0.0%**

NEW HOME SALES

Aug	1.001 million
Sept	1.002 million
Oct	0.999 million

REVISED CONSUMER SENTIMENT

Sept	80.4
Oct	81.8
Nov(p)	77.0
Nov(r)	76.9

FOMC MINUTES

Thursday 26

THANKSGIVING

Friday 27

Monday 30

CHICAGO PURCHASING MANAGERS' INDEX (9:45)

	Index	Prices
Sept	62.4	64.7
Oct	61.1	64.6
Nov	--	--

PENDING HOMES SALES (10:00)

Aug	8.8%
Sept	-2.2%
Oct	--

Tuesday 1

ISM MANUFACTURING INDEX (10:00)

	Index	Prices
Sept	55.4	62.8
Oct	59.3	65.5
Nov	**57.0**	**65.0**

CONSTRUCTION SPEND. (10:00)

Aug	0.8%
Sept	0.3%
Oct	**1.0%**

VEHICLE SALES

Sept	16.3 million
Oct	16.2 million
Nov	**16.1 million**

Wednesday 2

ADP EMPLOYMENT REPORT (8:15)

	Private Payrolls
Sept	753,000
Oct	365,000
Nov	--

BEIGE BOOK (2:00)

October Beige Book

"Economic activity continued to increase across all Districts, with the pace of growth characterized as slight to modest in most Districts."

Thursday 3

INITIAL CLAIMS (8:30)

ISM SERVICES INDEX (10:00)

	Index	Prices
Sept	57.8	59.0
Oct	56.6	63.9
Nov	**56.0**	**63.0**

Friday 4

EMPLOYMENT REPORT (8:30)

	Payrolls	Un. Rate
Sept	672,000	7.9%
Oct	638,000	6.9%
Nov	**500,000**	**6.7%**

TRADE BALANCE (8:30)

Aug	-$67.0 billion
Sept	-$63.9 billion
Oct	**-$64.5 billion**

FACTORY ORDERS (10:00)

Aug	0.6%
Sept	1.2%
Oct	**0.7%**

Monday 7

CONSUMER CREDIT

Tuesday 8

NFIB SMALL BUSINESS OPTIMISM INDEX

REVISED PRODUCTIVITY & COSTS

Wednesday 9

WHOLESALE TRADE

JOLTS DATA

Thursday 10

INITIAL CLAIMS

CPI

FEDERAL BUDGET

Friday 11

PPI

CONSUMER SENTIMENT

Monday 14

Tuesday 15

EMPIRE MFG. INDEX

IMPORT/EXPORT PRICES

IP & CAP-U

TIC DATA

FOMC MEETING

Wednesday 16

RETAIL SALES

BUSINESS INVENTORIES

NAHB HOUSING MARKET INDEX

FOMC DECISION

Thursday 17

INITIAL CLAIMS

HOUSING STARTS

PHILLY FED INDEX

Friday 18

CURRENT ACCOUNT

LEADING INDICATORS

Forecasts in Bold. (a) = advance (1st estimate of GDP); (p) = preliminary (2nd estimate of GDP); (r) = revised

Treasury Financing

November/December 2020

Monday	Tuesday	Wednesday	Thursday	Friday
23	24	25	26	27
AUCTION RESULTS: Rate Cover 13-week bills 0.085% 2.67 26-week bills 0.090% 3.57 2-year notes 0.165% 2.71 5-year notes 0.397% 2.38	**AUCTION RESULTS:** Margin Cover 2-year FRN 0.053% 2.90 Rate Cover 7-year notes 0.653% 2.37 41-day CMB 0.075% 3.15 118-day CMB 0.090% 3.48 **ANNOUNCE:** $30 billion 4-week bills for auction on November 25 $35 billion 8-week bills for auction on November 25 $25 billion 105-day CMBs for auction on November 25 $30 billion 154-day CMBs for auction on November 25 **SETTLE:** $30 billion 4-week bills $35 billion 8-week bills $25 billion 105-day CMBs $30 billion 154-day CMBs	**AUCTION RESULTS:** Rate Cover 4-week bills 0.080% 3.38 8-week bills 0.080% 3.47 105-day CMB 0.085% 4.35 154-day CMB 0.090% 4.35 **ANNOUNCE:** $105 billion 13-,26-week bills for auction on November 30 $34 billion 52-week bills for auction on December 1 $30 billion 42-day CMBS for auction on December 1 $30 billion 119-day CMBs for auction on December 1	***THANKSGIVING***	**SETTLE:** $105 billion 13-,26-week bills $24 billion 2-year FRNs $30 billion 41-day CMBs $30 billion 118-day CMBs
30	1	2	3	4
AUCTION: $105 billion 13-,26-week bills **SETTLE:** $27 billion 20-year bonds $12 billion 10-year TIPS $56 billion 2-year notes $57 billion 5-year notes $56 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 December 3 $35 billion* 8-week bills for auction on December 3 **SETTLE:** $30 billion 4-week bills $35 billion 8-week bills $25 billion 105-day CMBs $30 billion 154-day CMBs		**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction December 7 $56 billion* 3-year notes for auction on December 8 $38 billion* 10-year notes for auction on December 9 $24 billion* 30-year bonds for auction on December 10 **SETTLE:** $105 billion 13-,26-week bills $34 billion 52-week bills $30 billion 42-day CMBs $30 billion 119-day CMBs	
7	8	9	10	11
AUCTION: $105 billion* 13-,26-week bills	**AUCTION:** $56 billion* 3-year notes **ANNOUNCE:** $30 billion* 4-week bills for auction on December 10 $35 billion* 8-week bills for auction on December 10 **SETTLE:** $30 billion* 4-week bills $35 billion* 8-week bills	**AUCTION:** $38 billion* 10-year notes	**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills $24 billion* 30-year bonds **ANNOUNCE:** $105 billion* 13-,26-week bills for auction December 14 **SETTLE:** $105 billion* 13-,26-week bills	
14	15	16	17	18
AUCTION: $105 billion* 13-,26-week bills	**ANNOUNCE:** $30 billion* 4-week bills for auction on December 17 $35 billion* 8-week bills for auction on December 17 **SETTLE:** $30 billion* 4-week bills $35 billion* 8-week bills $56 billion* 3-year notes $38 billion* 10-year notes $24 billion* 30-year bonds		**AUCTION:** $30 billion* 4-week bills $35 billion* 8-week bills **ANNOUNCE:** $105 billion* 13-,26-week bills for auction December 21 $24 billion* 2-year FRNs for auction on December 23 $24 billion* 20-year bonds for auction on December 21 $15 billion* 5-year TIPS for auction on December 22 **SETTLE:** $105 billion* 13-,26-week bills	

**Estimate*