U.S. Economic Comment

- Recent economic data: mostly dreadful, but some positive developments
- Powell's view: worst case scenario, not the modal outlook

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Recent Economic Developments

The latest week brought several important data releases, and for the most part, the figures continued to show a severely depressed economy. Consider:

- The breadth of the decline in retail sales in April was perhaps more striking than the record plunge of 16.4 percent in total sales, as 12 of the 13 major store categories included in the report posted declines. Nonstore retailers (primarily on line) posted a gain of 8.4 percent, but this advance represented only a modest offset to weakness elsewhere.

- The drop of 11.2 percent in the industrial production index was the sharpest in the long history of the series, more pronounced than even the worst reading during the Great Depression (off 9.8 percent in November 1937). The manufacturing component accounted for most of the decline, as the level of production fell below the trough registered during the financial crisis.

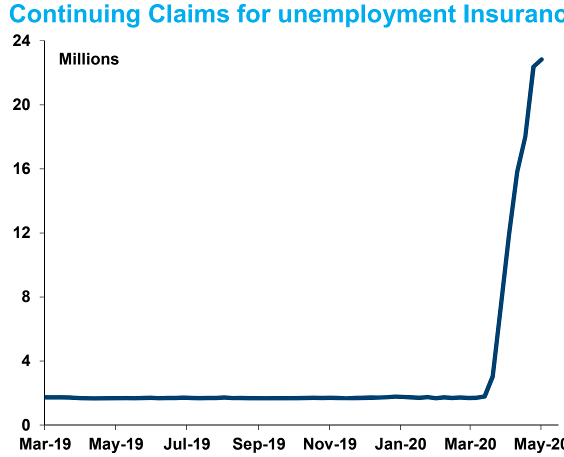
- The CPI and the PPI suggested a notably weak pricing environment, as the core components fell for the second and third consecutive months, respectively. The latest declines were sizeable (off 0.4 percent and 0.5 percent).

- Initial claims for unemployment insurance, while decelerating, continue to show a shocking volume of layoffs.

While the weight of recent statistics suggest a dire economic environment in the U.S., some recent reports have offered a hint of improvement. For example, so-called continuing claims for unemployment insurance (the number of individuals receiving jobless benefits) might be topping out, as the latest weekly tally showed a minuscule increase and the beginning of a bend in what had been a rocket-like advance in the prior six weeks (chart).

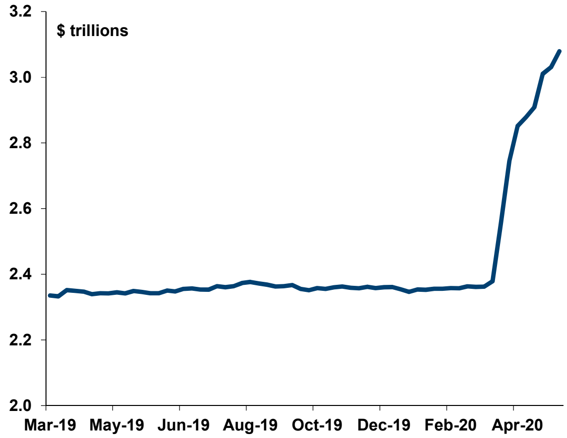
The increase of approximately 20 million individuals receiving unemployment benefits since mid-March is shy of the 30.8 million (not seasonally adjusted) that have filed initial claims, raising questions about the disconnect. Normal lags in processing an initial filing will explain a small portion of the difference, and some filers were no doubt declared ineligible for benefits because they did not work long enough before being furloughed (rules vary by state, but most states have a work-time requirement). From a more positive perspective, some of the difference probably reflects individuals finding other work or being recalled to their previous job.

Continuing Claims for unemployment Insurance



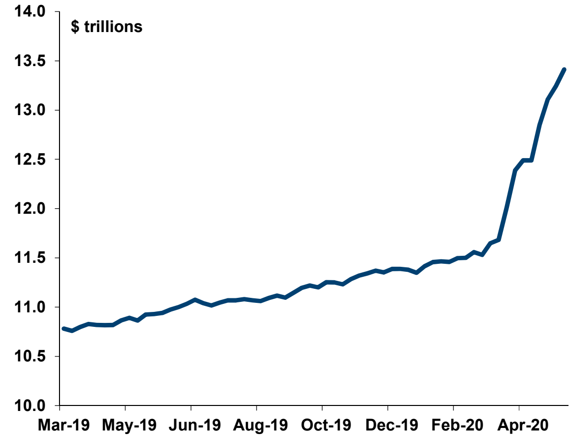
Source: U.S. Department of Labor via Haver Analytics

Commercial and Industrial Loans



Source: Federal Reserve Board via Haver Analytics

Other Bank Deposits



Source: Federal Reserve Board via Haver Analytics

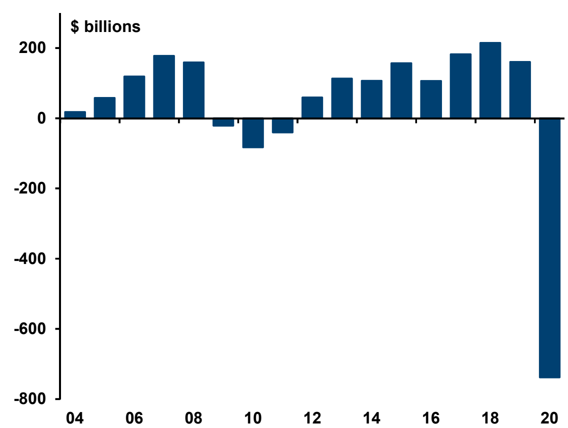
Many observers will scoff at the possibility of worker recalls in the current environment, but we suspect it is an important factor. A recent survey of households conducted by the Federal Reserve in early April showed that some workers had indeed already been recalled (Board of Governors, Report on the Economic Well-Being of U.S. Households in 2019, featuring Supplemental Data from April 2020). In addition, many states have eased stay-at-home restrictions, which would naturally lead to worker recalls.

Possibly most important, the Paycheck Protection Program has probably achieved some success in boosting payrolls. A recent surge in business loans at commercial banks offers prima facie evidence that the program is stirring activity (chart, above left; the loans under this program, which will turn to grants if used to support payrolls and other key expenses, are advanced through private-sector lending institutions). Some of this increase probably reflects the drawdown of lines of credit by businesses to remain liquid during a challenging environment, but the increase since late April is probably PPP related. The Fed's holdings of $40 billion under its PPP credit facility also supports the notion of worker recalls.

The liability side of commercial bank balance sheets also offers an element of hope, as data published by the Federal Reserve shows a surge in "other" deposits (chart, above right; other deposits exclude large time deposits). The recent jump most likely reflects the combined influence of little spending by households because of the lockdown and large volumes of funds flowing from the federal government to individuals and businesses. Unemployment benefits began to swell in late March, and government expenditures authorized by the CARES Act followed soon afterward. The pickup in deposits, totaling $1.7 trillion since mid-March, shows the deep support provided by the federal government.

The flip side of strong government support is a ballooning federal budget deficit. The Treasury Department this week published budget results for April, which showed a deficit of $738 billion. As shown on the chart, April usually involves a budget surplus because of estimated tax payments by corporations and final settlements by individuals on obligations from the prior year. The rare deficits for April during the financial crisis (2009-2011) pale in comparison to the shortfall registered this year.

Federal Budget Balance for April



Source: U.S. Treasury Department via Haver Analytics

Some of the pronounced slippage in this instance was the result of the postponement of the April 15 filing deadline. Final payments from individuals plus estimated payments by corporations totaled $24 billion this April, down from $257 billion in the same month last year. The majority of the deterioration, though, reflected the pickup in financial support from the federal government that normally accompanies slowdowns in the economy plus the new spending authorized by four rounds of anti-virus legislation. The deterioration will continue in the months ahead, as the Congressional Budget Office estimates that the deficit for the full fiscal year will total $3.7 trillion, which would involve an additional shortfall of $2.2 trillion over the next five months.

Chair Powell's View: Perhaps Too Pessimistic

Fed Chair Jerome Powell this week delivered a dour view of the economic outlook -- one that caused a bit of a stir in the stock market. He talked of potentially severe long-run consequences that could evolve because of the coronavirus. He noted that worker skills and network connections would fade if spells of unemployment were long lasting, and he noted that liquidity strains at businesses could develop into insolvency risks. For firms that survive, he wondered about their willingness to invest and the damage to productivity and potential economic growth that would follow cutbacks in capital spending. The Fed Chair seemed to be thinking in terms of the dreaded L-pattern.

This portion of his speech was indeed gloomy, but we should not ignore the earlier part of his talk, where he argued that the current downturn is different than those in the past. Previous recessions, Mr. Powell noted, were triggered either by efforts to fight inflation or by the unwinding of economic imbalances (such as asset bubbles). This recession is virus-related, and accordingly, the speed and pattern of the recovery will depend on the course of the virus. If the virus were to die out during the spring and early summer, the recovery would probably be V-shaped. If it lingers or reaccelerates, the economy will trace a U or W pattern. It's all about the virus.

Given the virus-related nature of the current downturn, Chair Powell cannot possibly have a clear view on the economic outlook (nor can anyone else). We view his talk as an effort to outline the worst case scenario, and to establish a defense for the aggressive policy stance being pursued by the Fed. He was signaling that policy errors will be on the side of too much support rather than too little.

Review

Week of May 11, 2020	Actual	Consensus	Comments
CPI (April)	**-0.8% Total, -0.4% Core**	**-0.8% Total, -0.2% Core**	Food prices jumped 1.5% in April, driven by a surge of 2.6% in prices for food at home (i.e. purchased at a grocery store), but energy prices and core prices both declined. The energy component fell 10.1%, driven by a plunge of 20.6% in gasoline prices. The coronavirus played a strong role in restraining the core CPI, which posted the largest month-to-month decline on record. Costs of airline tickets (-15.2%), hotel stays (-8.1%), and apparel (-4.7%) all fell in the face of slack demand spurred by lockdowns. The latest results left the year-over-year change in the headline index at 0.3%, down from a recent high of 2.5% in January. Core prices also have decelerated, increasing 1.4% in the past year, down from 2.1% in the prior month and 2.4% in February.
Federal Budget (April)	**$737.9 Billion Deficit**	**$737.0 Billion Deficit**	Net receipts collected by the federal government plunged 54.8% year-over-year in April, largely because of the postponement of the due date for final payment on 2019 obligations. Outlays surged 161.1% from the prior year, boosted by efforts to fight the coronavirus and to provide relief to businesses and individuals. The surge in the deficit in April left the shortfall for the first seven months of FY2020 at $1.48 trillion versus $531 billion in the same period in FY2019.
PPI (April)	**-1.3% Total, -0.9% Core***	**-0.5% Total, -0.1% Core***	The energy component led the retreat in the PPI with a month-to-month drop of 19.0%, but the food and core components also contributed with declines of 0.5% and 0.9%, respectively. In the core component, core goods prices slipped 0.4%. Service prices included in the core component were quite weak, falling 1.2% on average. Trade services (i.e. services provided by vendors) rose 1.6%, but this volatile area is not included in the PPI definition of core. The April results left the year-over-year change in the headline index at -1.2%, only slightly better than the record low of -1.4% in 2015. The core component fell 0.3% on a year-over-year basis, its first reading in negative territory, although the series only goes back to late 2013.

Review Continued

Week of May 11, 2020	Actual	Consensus	Comments
Retail Sales (April)	**-16.4% Total, -17.2% Ex-Autos**	**-12.0% Total, -8.5% Ex-Autos**	The magnitude of the decline in retail sales was striking, but the breadth of the retreat was perhaps more telling, as 12 of the 13 store categories published in the report lost ground in April. Only nonstore retailers (primarily online vendors) posted an advance, and the increase of 8.4%, while sizeable, represented a modest offset to weakness elsewhere. Restaurants and bars naturally saw dreadful results (off 29.5% in April and 50.5% in the past two months). In addition, activity at clothing stores fell 89.3 percent in the past two months and sales at furniture stores and at electronics and appliance stores were almost as weak (off 67.4% and 64.9% in the past two months, respectively). Sales at food stores and general merchandise stores were less alarming, but declines were tempered by frenetic buying at grocery stores and big-box outlets in the early stages of the pandemic.
Industrial Production (April)	**-11.2%**	**-12.0%**	The drop in industrial production was the sharpest in the long history of the series, softer than even the worst reading during the Great Depression (off 9.8% in November 1937). Manufacturing activity plunged 13.7%, with all 20 major industries in the report contributing. The broad-based retreat pushed the level of production 1.8% below the trough registered during the financial crisis. Mining activity has slowed in response to low oil prices, declining 6.1% in April after a combined drop of 2.5% in the prior two months. The recent adjustment in mining, while notable, has been less pronounced than the retreats in other sectors of the economy. Utility output, driven primarily by shifts in the weather, fell 0.9%.
Consumer Sentiment (May)	**73.7 (+1.9 Index Pts.)**	**68.0 (-3.8 Index Pts.)**	The University of Michigan sentiment index wiggled higher in early May, an unexpected but welcome development. The index has declined 27.0% from its elevated level in February, but it is still above readings seen in the early years of the latest expansion and above most readings during the financial crisis. The shifts in the components of the headline index in early May were mildly surprising, as the current conditions index rose 11.7% despite the dismal economic setting. The expectations component, in contrast, fell 3.4%. The expectations component had been holding up better than the current conditions component, but they have now posted similar-sized declines from pre-virus readings.

** The core PPI excludes food, energy, and trade services.*

Sources Bureau of Labor Statistics (CPI, PPI); U.S. Treasury Department (Federal Budget); U.S. Census Bureau (Retail Sales); Federal Reserve Board (Industrial Production); University of Michigan Survey Research Center (Consumer Sentiment); Consensus forecasts are from Bloomberg

Preview

Week of May 18, 2020	Projected	Comments
Housing Starts (April) (Tuesday)	**0.980 Million (-19.4%)**	A plunge in the sentiment index of the National Association of Home Builders suggests that construction companies are wary of starting new homes during the pandemic. The expected drop of 19.4% in April follows a cumulative decline of 24.9% in the prior two months. The recent and expected changes, while striking, follow strong results in January and thus the expected level of starts is still above readings during the financial crisis and early years of the recovery. The low reading during the financial crisis was 478,000 units (April 2009).
Existing Home Sales (April) (Thursday)	**4.70 Million (-10.8%)**	A drop of 20% in pending home sales in March suggests a marked retreat in sales of existing homes in April. After a decline of 8.5% in March, the expected drop of 10.8% in April would push activity to its lowest level since the summer of 2012, although still above the low of 3.77 million units during the financial crisis. The record low for this series of 3.45 million homes occurred in July 2010, when sales tumbled after strength in the prior several months stirred by a tax credit for a home purchase.
Leading Indicators (April) (Thursday)	**-3.5%**	Stock prices and consumer expectations have improved recently and are likely to make positive contributions to the leading indicator index. However, pronounced weakness in other measures, especially the manufacturing workweek, unemployment claims, and the ISM new orders index, should easily provide offsets and lead to a sharp decline. The still unpublished results for building permits represent a wild card. The Conference Board usually assumes no change in this component when the results have not been published, but in the current setting we suspect that analysts at the Conference Board will build in a decline. Our estimate assumes a drop of 20% in building permits.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

May/June 2020

Monday	Tuesday	Wednesday	Thursday	Friday
11	12	13	14	15
	NFIB SMALL BUSINESS OPTIMISM INDEX Feb 104.5 Mar 96.4 Apr 90.9 **CPI** Total / Core Feb 0.1% 0.2% Mar -0.4% -0.1% Apr -0.8% -0.4% **FEDERAL BUDGET** 2020 / 2019 Feb -$235.3B -$234.0B Mar -$119.0B -$146.9B Apr -$737.9B $160.3B	**PPI** Final Demand / Core* Feb -0.6% -0.1% Mar -0.2% -0.2% Apr -1.3% -0.9%	**UNEMPLOYMENT CLAIMS** Initial / Continuing (Millions) Apr 18 4.442 18.011 Apr 25 3.867 22.377 May 02 3.176 22.833 May 09 2.981 N/A **IMPORT/EXPORT PRICES** Non-fuel Imports / Nonagri. Exports Feb 0.2% -1.1% Mar 0.0% -1.7% Apr -0.5% -3.3%	**RETAIL SALES** Total / Ex.Autos Feb -0.4% -0.5% Mar -8.3% -4.0% Apr -16.4% -17.2% **EMPIRE MFG** Mar -21.5 Apr -78.2 May -48.5 **IP & CAP-U** IP / Cap.Util. Feb 0.1% 76.7% Mar -4.5% 73.2% Apr -11.2% 64.9% **BUSINESS INVENTORIES** Inventories / Sales Jan -0.3% 0.6% Feb -0.4% -0.5% Mar -0.2% -5.2% **JOLTS DATA** Openings (000) / Quit Rate Jan 7,012 2.3% Feb 7,004 2.3% Mar 6,191 1.8% **CONSUMER SENTIMENT** Mar 89.1 Apr 71.8 May 73.7 **TIC DATA** Total / Net L-T Jan $127.1B $21.8B Feb -$14.3B $49.6B Mar $349.9B -$112.6B
18	19	20	21	22
NAHB HOUSING INDEX (10:00) Mar 72 Apr 30 May --	**HOUSING STARTS (8:30)** Feb 1.564 million Mar 1.216 million **Apr 0.980 million**	**FOMC MINUTES (2:00)**	**INITIAL CLAIMS (8:30)** **PHILLY FED INDEX (8:30)** Mar -12.7 Apr -56.6 May -- **EXISTING HOME SALES (10:00)** Feb 5.76 million Mar 5.27 million **Apr 4.70 million** **LEADING INDICATORS (10:00)** Feb -0.2% Mar -6.7% **Apr -3.5%**	
25	26	27	28	29
MEMORIAL DAY	**CHICAGO FED NATIONAL ACTIVITY INDEX** **FHFA HOME PRICE INDEX** **CORELOGIC CASE-SHILLER HOME PRICE INDEX** **CONSUMER CONFIDENCE** **NEW HOME SALES**	**BEIGE BOOK**	**INITIAL CLAIMS** **REVISED GDP** **DURABLE GOODS ORDERS** **PENDING HOME SALES**	**U.S. INTERNATIONAL TRADE IN GOODS** **ADVANCE INVENTORIES** **PERSONAL INCOME, SPENDING, PRICES** **CHICAGO PURCHASING MANAGERS' INDEX** **REVISED CONSUMER SENTIMENT**
1	2	3	4	5
ISM MFG INDEX **CONSTRUCTION SPEND.**	**VEHICLE SALES**	**ADP EMPLOYMENT REPORT** **ISM NON-MFG INDEX** **FACTORY ORDERS**	**INITIAL CLAIMS** **TRADE BALANCE** **REVISED PRODUCTIVITY & COSTS**	**EMPLOYMENT REPORT** **CONSUMER CREDIT**

Forecasts in Bold. * *The core PPI excludes food, energy, and trade services*

Treasury Financing

May/June 2020

Monday	Tuesday	Wednesday	Thursday	Friday
11	12	13	14	15
AUCTION RESULTS: Rate Cover 13-week bills 0.125% 2.97 26-week bills 0.155% 2.97 3-year notes 0.230% 2.54	**AUCTION RESULTS:** Rate Cover 42-day CMB 0.110% 2.93 119-day CMB 0.145% 3.38 10-yr notes 0.700% 2.69 **ANNOUNCE:** $80 billion 4-week bills for auction on May 14 $70 billion 8-week bills for auction on May 14 $35 billion 105-day CMBs for auction on May 13 $40 billion 154-day CMBs for auction on May 13 **SETTLE:** $80 billion 4-week bills $70 billion 8-week bills $35 billion 154-day CMBs $30 billion 105-day CMBs	**AUCTION RESULTS:** Rate Cover 105-day CMB 0.140% 3.51 154-day CMB 0.155% 2.97 30-yr bonds 1.342% 2.30	**AUCTION RESULTS:** Rate Cover 4-week bills 0.090% 2.93 8-week bills 0.110% 2.90 **ANNOUNCE:** $117 billion 13-,26-week bills for auction on May 18 $31 billion 52-week bills for auction on May 19 $20 billion 20-year bonds for auction on May 20 $12 billion 10-year TIPS for auction on May 21 $65 billion 42-day CMBs for auction on May 19 $40 billion 119-day CMBs for auction on May 19 **SETTLE:** $117 billion 13-,26-week bills $65 billion 42-day CMBs $35 billion 119-day CMBs	**SETTLE:** $42 billion 3-year notes $32 billion 10-year notes $22 billion 30-year bonds
18	19	20	21	22
AUCTION: $117 billion 13-,26-week bills	**AUCTION:** $31 billion 52-week bills $65 billion 42-day CMBs $40 billion 119-day CMBs **ANNOUNCE:** $80 billion* 4-week bills for auction on May 21 $70 billion* 8-week bills for auction on May 21 **SETTLE:** $80 billion 4-week bills $70 billion 8-week bills $35 billion 105-day CMBs $40 billion 154-day CMBs	**AUCTION:** $20 billion 20-year bonds	**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills $12 billion 10-year TIPS **ANNOUNCE:** $117 billion* 13-,26-week bills for auction on May 26 $20 billion* 2-year FRNs for auction on May 27 $44 billion* 2-year notes for auction on May 26 $45 billion* 5-year notes for auction on May 27 $38 billion* 7-year notes for auction on May 28 **SETTLE:** $117 billion 13-,26-week bills $31 billion 52-week bills $65 billion 42-day CMBs $40 billion 119-day CMBs	
25	26	27	28	29
MEMORIAL DAY	**AUCTION:** $117 billion* 13-,26-week bills $44 billion* 2-year notes **ANNOUNCE:** $80 billion* 4-week bills for auction on May 28 $70 billion* 8-week bills for auction on May 28 **SETTLE:** $80 billion* 4-week bills $70 billion* 8-week bills	**AUCTION:** $20 billion* 2-year FRNs $45 billion* 5-year notes	**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills $38 billion* 7-year notes **ANNOUNCE:** $117 billion* 13-,26-week bills for auction on June 1 **SETTLE:** $117 billion* 13-,26-week bills	**SETTLE:** $12 billion 10-year TIPS $20 billion 2-year FRNs
1	2	3	4	5
AUCTION: $117 billion* 13-,26-week bills **SETTLE:** $44 billion* 2-year notes $45 billion* 5-year notes $38 billion* 7-year notes $20 billion 20-year bonds	**ANNOUNCE:** $80 billion* 4-week bills for auction on June 4 $70 billion* 8-week bills for auction on June 4 **SETTLE:** $80 billion* 4-week bills $70 billion* 8-week bills		**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $117 billion* 13-,26-week bills for auction on June 8 $44 billion* 3-year notes for auction on June 8 $29 billion* 10-year notes for auction on June 9 $19 billion* 30-year bonds for auction on June 11 **SETTLE:** $117 billion* 13-,26-week bills	

**Estimate*