Financial Market Weekly

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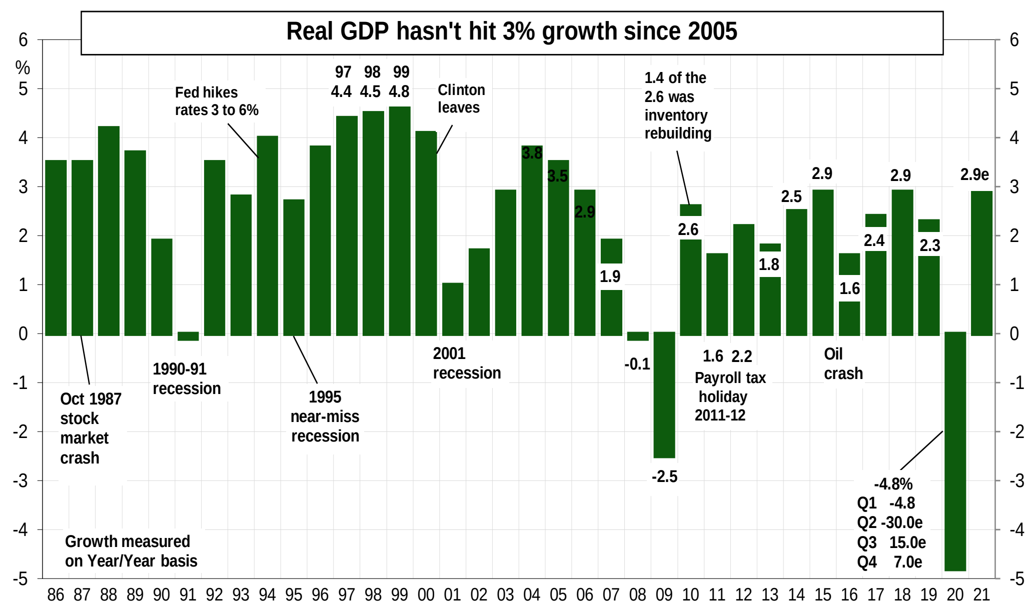
GDP ALREADY FELL 4.8% IN THE FIRST QUARTER WITH LESS THAN A MONTH OF A CORONAVIRUS LOCKDOWN



Real GDP fell 4.8% in the first quarter of the year which is quite a feat given the pandemic virus lockdown of the economy didn't start till the second week of March. Consumer spending, investment spending, exports were all down. The economy has fallen off the cliff and broken its neck where the only thing consumers are buying are nondurable goods like food and beverages for "off-premises consumption," and how! These purchases added 1.1 percentage points to real GDP. The economy will continue to fall until the country opens back up. If the economy fell this hard in the first quarter, with less than a month of pandemic lockdown for most states, don't ask how far it will crater in the second quarter because it is going to be a complete disaster.

	Q4 18	Q1 19	Q2 19	Q3 19	Q4 19	Q1 20p
REAL GDP	1.1	3.1	2.0	2.1	2.1	-4.8
REAL CONSUMPTION	1.4	1.1	4.6	3.2	1.8	-7.6
CONSUMPTION	1.0	0.8	3.0	2.1	1.2	-5.3
Durables	0.1	0.0	0.9	0.6	0.2	-1.2
Nondurables	0.2	0.3	0.9	0.5	-0.1	0.9
Services	0.7	0.5	1.3	1.0	1.1	-5.0
INVESTMENT	0.5	1.1	-1.2	-0.2	-1.1	-1.0
Business Plant	-0.3	0.1	-0.4	-0.3	-0.2	-0.3
& Equipment and	0.4	0.0	0.1	-0.2	-0.3	-0.9
Intellectual Property	0.5	0.5	0.2	0.2	0.1	0.0
Homes	-0.2	0.0	-0.1	0.2	0.2	0.7
Inventories	0.1	0.5	-0.9	0.0	-1.0	-0.6
EXPORTS	0.2	0.5	-0.7	0.1	0.2	-1.0
IMPORTS	-0.5	0.2	0.0	-0.3	1.3	2.3
GOVERNMENT	-0.1	0.5	0.8	0.3	0.4	0.1
Federal defense	0.2	0.3	0.1	0.1	0.2	0.0
Fed nondefense	-0.1	-0.2	0.4	0.1	0.1	0.1
State and local	-0.1	0.4	0.3	0.1	0.2	0.0

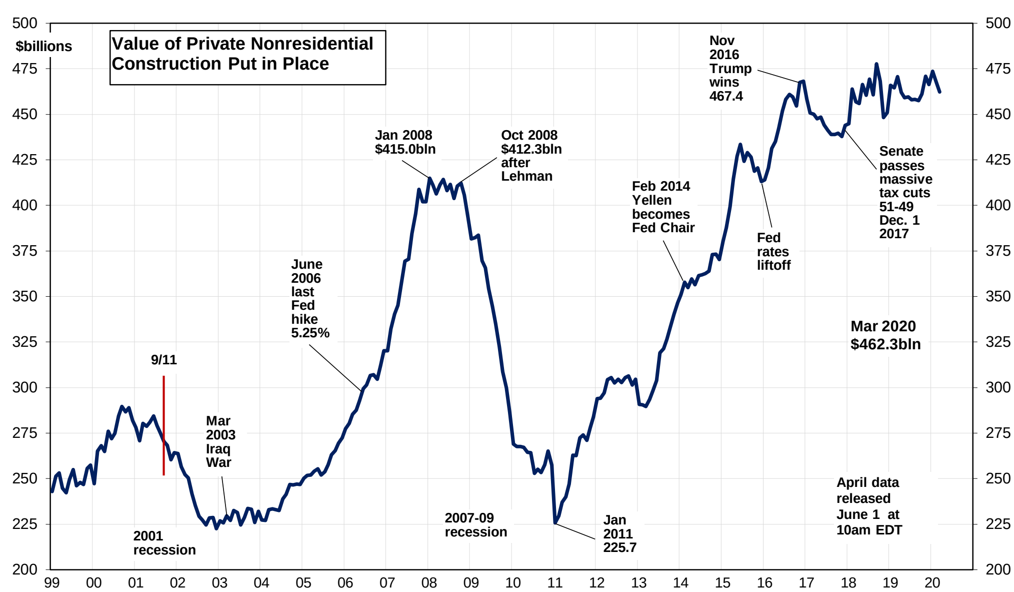
Below line: Percentage point contributions to Q1 2020 -4.8% real GDP
Second estimate for Q1 is Thursday, May 28

The consumer is two-thirds of the economy and the lockdown kept them from spending on anything that requires social distancing. This is one of the reasons why the consumer won't come back as quickly even if the economy indeed becomes one of the briefest in history and puts in its worst day, its lowest point, in April or May. After the Great Recession ended in 2009, it took the consumer forever to get reinvolved and even the payroll tax cuts in 2011 to 2012 did nothing to boost consumer spending. They saved it, didn't spend it. The consumer was in retreat in the first quarter. In actual dollars spent, motor vehicles fell 33.8% in Q1 2020. Clothing as well was down 34.3%. Transportation services were hit hard and fell 32.1%. In 2018, 41.0% of Transportation services was motor vehicle maintenance and repairs, and 22.5% was air travel. Recreation sevices also fell 30.3% and membership clubs, sports centers, parks, theaters and museums were 37.5% of 2018 recreation services expenditures.

Nominal Consumer Expenditures & GDP	Q1 2020	Q4 2019	Q3 2019	Level $bln Q1 2020	% Change Year/Year
Gross domestic product (GDP)	-3.5	3.5	3.8	21,537.9	2.1
Personal consumption expenditures (PCE)	-6.3	3.2	4.7	14,555.8	2.0
Goods	-2.3	0.2	4.5	4,532.1	3.1
Durable goods	-17.4	-0.5	6.7	1,475.4	-0.7
Motor vehicles and parts	-33.8	2.9	3.0	488.0	-5.0
Furnishings and durable household equipment	-4.3	-3.0	7.1	352.4	1.7
Recreational goods and vehicles	-4.6	-2.1	11.6	419.0	3.2
Other durable goods	-17.0	-2.1	6.6	215.9	-1.6
Nondurable goods	6.2	0.5	3.3	3,056.7	5.0
Food and beverages for off-premises consumption	29.0	-0.8	5.0	1,108.9	9.2
Clothing and footwear	-34.3	-1.7	3.0	360.7	-8.3
Gasoline and other energy goods	-22.1	4.3	-12.3	320.9	-0.3
Other nondurable goods	13.0	1.4	6.9	1,266.2	7.2
Services	-8.1	4.6	4.8	10,023.7	1.6
Household consumption expenditures (for services)	-9.8	5.2	4.8	9,543.8	1.2
Housing and utilities	3.9	3.3	4.9	2,735.6	4.1
Health care	-16.3	7.2	2.8	2,409.3	-0.7
Transportation services	-32.1	4.1	5.3	443.1	-4.6
Recreation services	-30.3	10.2	1.4	550.6	-4.2
Food services and accommodations	-28.0	2.0	5.6	953.5	-4.2
Financial services and insurance	6.7	5.3	6.4	1,201.8	6.4
Other services	-1.9	5.9	7.8	1,250.1	3.4
PCE excluding food and energy	-8.4	3.7	5.0	12,885.6	1.6

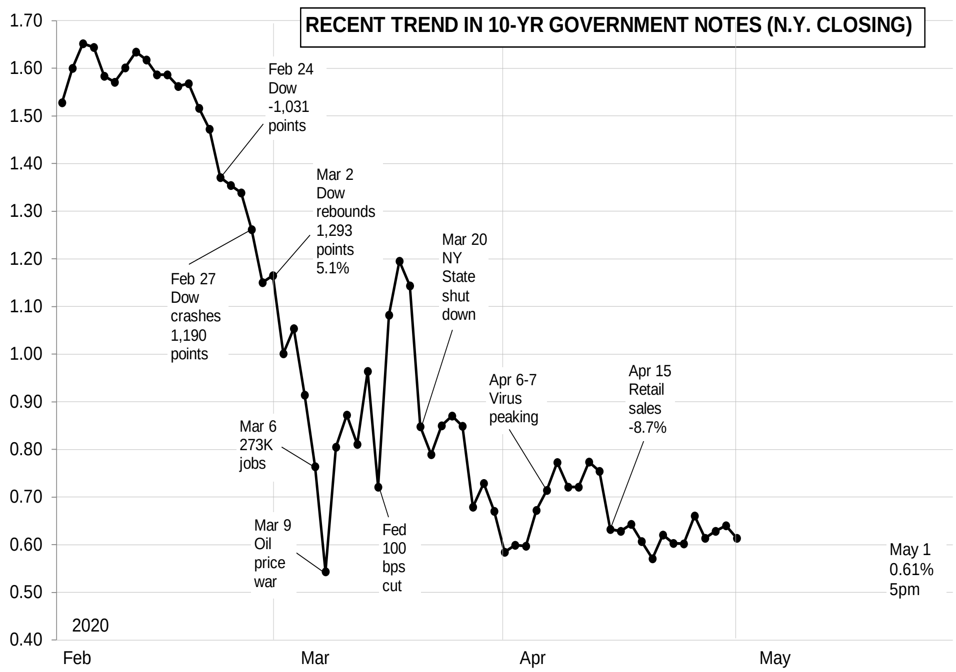
Pretty gloomy. On a lighter note. March business construction spending reported Friday was in decline as well but modestly. It's early yet, but the economy won't be needing a lot of new office space in the post-coronavirus world. Construction is part of business investment spending in GDP and many companies will be slow to ramp up investment: they have already borrowed to build up cash reserves given the uncertainty. There is talk that the cororonavirus pandemic could return later this year. The presidential election is dead ahead as well with many companies perhaps wondering whether the biggest corporate tax cut in history will go away. Reduced sales mean fixed costs are producing financial losses that will be hard to recover in the medium term.

Looking ahead, the future is clear as it always is. We expect the economy to bounce after a 30 (or 40) percent real GDP decline in the second quarter. If it falls 30% in Q2, then we would expect a 15% increase in the third quarter. The recovery will not get us back to the standard of living the country enjoyed earlier in the year however. Growth will be on a lower parallel path to where it would have been without the coronavirus pandemic.



MARKETS OUTLOOK

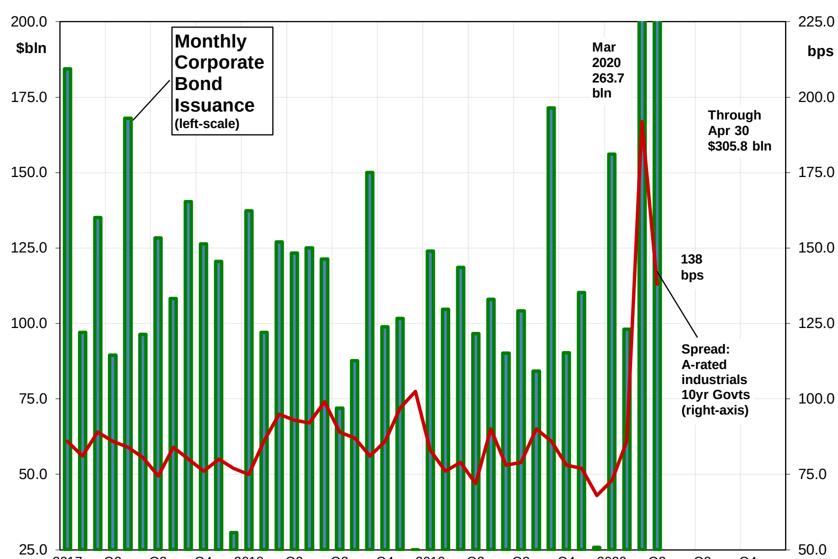
	29-Mar 2019	28-Jun 2019	30-Sep 2019	31-Dec 2019	31-Mar 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021
30-Yr Treasury	2.81	2.53	2.11	2.39	1.32	1.20	1.10	1.20	1.20	1.30
10-Yr Note	2.41	2.01	1.67	1.92	0.67	0.70	0.70	0.80	0.90	1.00
5-Yr Note	2.23	1.77	1.55	1.69	0.38	0.40	0.50	0.60	0.70	0.80
2-Yr Note	2.26	1.76	1.62	1.57	0.25	0.30	0.30	0.30	0.40	0.40
3-month Libor	2.60	2.32	2.09	1.90	1.45	1.10	1.00	0.80	0.60	0.50
Fed Funds Rate	2.50	2.50	2.00	1.75	0.25	0.25	0.25	0.25	0.25	0.25
2s/10s spread	15	25	5	35	42	40	40	50	50	60



10-year Treasury yields climbed on Monday after the weekend following the stock market rally that had something to do with optimism on the news some of the states in the country were opening back up. It didn't last, optimism never does, and bond yields fell from the 0.67% highs for the week at the Tuesday open in Asia which is about 8pm Monday night in New York. We were excited to think bond yields were rising Wednesday at 830 EDT on the -4.8% real GDP report, but yields were instead following the rally in stocks also at 830 EDT on the Gilead virus drug news. The Fed announced Friday afternoon it would cut QE government securities purchases to $8 billion a day next week from $10 billion this week and $15 billion the week before. We listened twice to Powell's press conference and didn't hear him say he would finance the Treasury's budget deficit.

CORPORATES: BOEING, AIR PRODUCTS, DELTA, BIOGEN, KOCH, DUPONT

Corporate bond offerings were $90.7 billion in the May 1 week versus $38.1 billion in the April 24 week. On Monday, Emerson Electric sold $1.5 billion 7s/10s/30s. It priced a $500 million 1.95% 10-yr (m-w +20bp) at 135 bps (A2/A). The manufacturer of electronic equipment, software and systems will use the proceeds to repay commercial paper borrowings. Corporate bond yields (10-yr Industrials rated A2) were 143 bps above 10-yr Treasuries Friday versus 140 bps last Friday.



FEDERAL RESERVE POLICY

The Fed met April 28-29, 2020 to consider its monetary policy. In the press conference Q&A, Powell was asked what were the medium term risks, over the next year or so, from the pandemic virus. (1) The virus itself, how long till it's gone? (2) There could be damage to the productive capacity of the economy from extended unemployment where workers lose skills and are unable to restart careers. Damage as well is possible from the thousands of medium and small sized businesses if there is a wave of "unnecessary" insolvencies. (3) This is a global phenomenon and the sharply negative economic growth abroad could weigh on any U.S. recovery. Whew. Powell is sounding more like a dismal science economist. Maybe we did find the right man to lead the Federal Reserve. It sounds like he thinks the economy might never get back to normal again. Medium term means a year or so.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	29-Apr	22-Apr	15-Apr	8-Apr	pre-LEH
Factors adding reserves					
U.S. Treasury securities	3971.419	3909.352	3788.858	3634.386	479.782
Federal agency debt securities	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	1604.720	1622.487	1568.171	1459.701	0.000
Repurchase agreements	158.202	157.500	181.100	192.751	126.750
Primary credit (Discount Window)	31.759	33.742	36.284	43.449	23.455
MMLF	46.277	48.810	50.656	53.171	
PDCF	25.504	31.526	33.409	33.018	
Commerical Paper Funding Facility	3.372	2.732	0.974		
Paycheck Protection Facility	19.488	8.009			
Central bank liquidity swaps	438.953	409.712	378.291	358.077	62.000
Federal Reserve Assets	6703.2	6621.4	6416.1	6131.4	961.7
3-month Libor %	0.69	1.02	1.13	1.31	2.82
Factors draining reserves					
Currency in circulation	1910.511	1895.994	1887.593	1883.487	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Reverse repurchases w/others	1.450	10.825	3.150	53.483	0.000
Reserve Balances (Net Liquidity)	3539.660	3521.444	3069.872	3356.860	24.964
Treasuries within 15 days	55.294	58.869	58.644	47.112	14.955
Treasuries 16 to 90 days	249.856	243.599	225.035	233.415	31.549
Treasuries 91 days to 1 year	535.821	528.185	527.601	500.589	69.272
Treasuries over 1-yr to 5 years	1572.472	1536.392	1493.336	1432.206	170.807
Treasuries over 5-yrs to 10 years	665.596	659.309	621.255	576.918	91.863
Treasuries over 10-years	892.381	882.997	862.987	844.146	101.337

**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08

MMLF: Money Market Mutual Fund Liquidity Facility: loans secured by assets bought by banks from money market funds

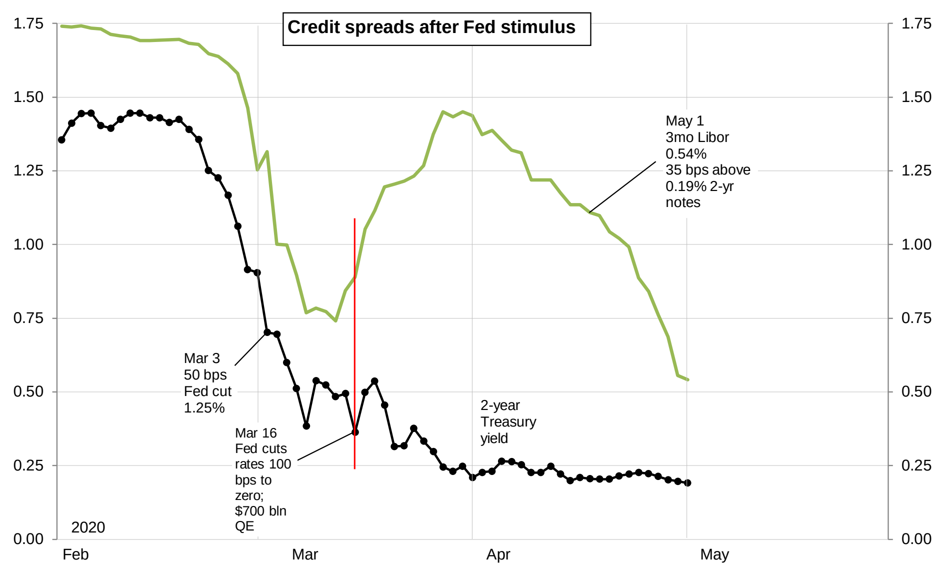
PDCF: Primary Dealer Credit Facility: o/n and term funding with maturities to 90 days

U.S. Treasury New Cash Needs and Fed Treasury Purchases (QE)

Monthly Changes ($ billions)

Fiscal Year (FY) Ending September 2020

	Oct	Nov	Dec	Jan	Feb	Mar	Apr	Total FY 2020
Fed QE	67.808	73.007	80.364	80.246	64.952	504.312	993.047	1,863.7
New Cash	166.8	112.5	50.9	38.5	199.8	238.7	1368.6	2,175.8
Bills	79.1	59.0	-98.2	-12.5	160.3	92.8	1344.3	1,624.8
Coupons	87.6	53.4	149.2	51.1	39.5	145.8	24.2	550.8



OTHER ECONOMIC NEWS THIS WEEK

U.S. exports (and factory jobs) machine is sputtering during pandemic lockdown (Tuesday)

Breaking economy news. Advance look at America's trade balance in March which happens to be in deficit. The deficit was $64.2 billion in March up from $59.9 billion in February.

Factory jobs are in peril with exports of autos falling 17.8% in March, capital goods fell 4.3% in March, in fact, every single category of exports was down. With the rest of the world in deep recession this year, U.S. exports to its trading partners are going to fall harder as well which leads one to wonder how on earth factories are going to open back up after the lockdown ends if there is nowhere in the world for companies to ship their products.

Imports always fall in a recession and consumer goods imports fell 8.3% in March to $47.1 billion, and autos imports fell 9.0% in March to $27.8 billion. Capital goods imports are still coming in, as we found in Friday's durable goods orders report, with capital goods increasing 2.7% to $53.1 billion.

Net, net, you can't have a Great Depression without a total breakdown in world trade between countries and that day is closer to becoming a reality today with U.S. exports and imports with the world tumbling in March. The deeper the hole the economy digs the harder it is going to be for consumers and businesses to climb back out. World trade volumes are going to come off further this year which reminds us of the Great Depression. The states are starting to plan for opening back up, but this is going to come too late to rescue world trade this year. Stay tuned. Story developing.

ADVANCE TRADE STATISTICS FOR MARCH

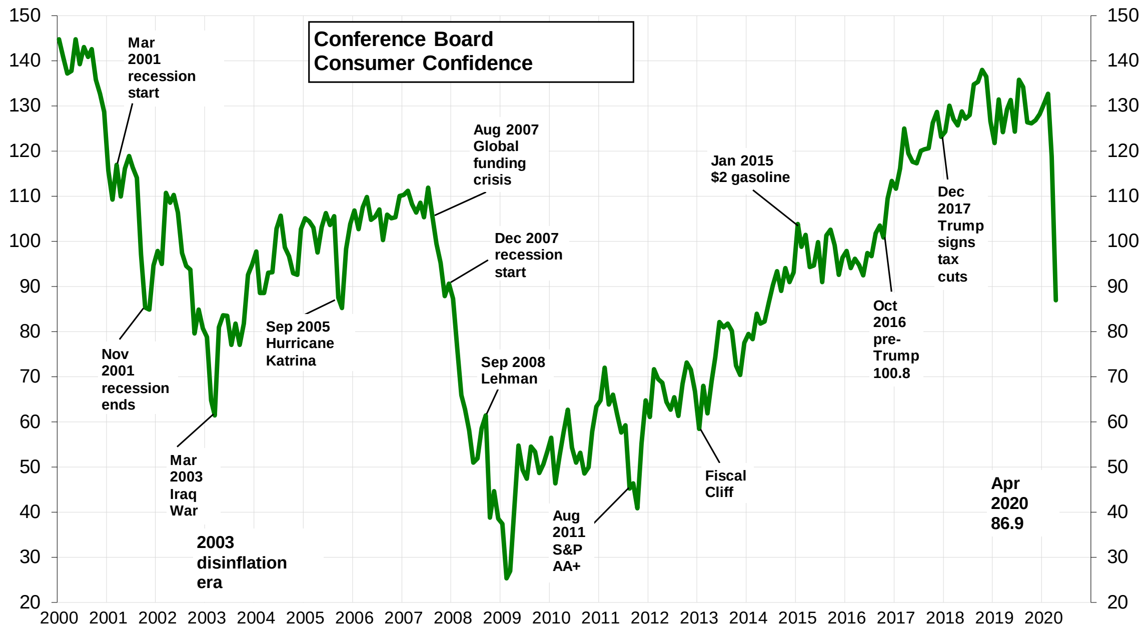
	Monthly				Percent changes		
Trade	Mar 2020	Feb 2020	Jan 2020	Mar 2019	Mar 20 Feb 20	Feb 20 Jan 20	Mar 20 Mar 19
Balance	-64,219	-59,887	-66,014	-72,235			
Exports	127,647	136,741	135,741	140,074	-6.7	0.7	-8.9
Foods, Feeds, & Beverages	10,872	10,878	10,970	10,799	-0.1	-0.8	0.7
Industrial Supplies (1)	42,350	45,796	45,077	44,608	-7.5	1.6	-5.1
Capital Goods	42,690	44,624	44,383	47,327	-4.3	0.5	-9.8
Automotive Vehicles, etc.	11,311	13,759	13,222	13,934	-17.8	4.1	-18.8
Consumer Goods	15,061	15,850	16,548	17,809	-5.0	-4.2	-15.4
Other Goods	5,363	5,833	5,542	5,598	-8.1	5.3	-4.2
Imports	191,866	196,627	201,755	212,310	-2.4	-2.5	-9.6
Foods, Feeds, & Beverages	12,910	12,488	12,891	12,981	3.4	-3.1	-0.5
Industrial Supplies (1)	40,926	40,770	42,369	45,229	0.4	-3.8	-9.5
Capital Goods	53,108	51,719	55,406	57,358	2.7	-6.7	-7.4
Automotive Vehicles, etc.	27,772	30,509	29,107	31,844	-9.0	4.8	-12.8
Consumer Goods	47,071	51,330	52,456	55,327	-8.3	-2.1	-14.9
Other Goods	10,079	9,811	9,526	9,570	2.7	3.0	5.3

(1) Includes petroleum and petroleum products.

Consumer has lost all the confidence built up during the Trump years (Tuesday)

Breaking economy news. Consumer confidence collapsed in April as the coronavirus self-isolation has made Americans fearful of what the future holds for them. The goodwill and tax cuts from the changes brought in by the president starting election night in October 2016 have evaporated overnight. It's going to take a lot of government pep talks to get Americans more confident about the outlook and it will be an uphill battle unless the 26 million applying for unemployment benefits the last five weeks find jobs again.

Net, net, the consumer has lost all the confidence built up during the Trump years where the best economy in history now lies in ruins as the coronavirus lockdown has taken down the economy. The job losses are nearing Great Depression levels if they aren't there already and the consumer's dismal outlook shows it. The stock market rally continues, perhaps seeing better days a year or two from now, but the consumer doesn't see any daylight at the end of the tunnel at all. Time will tell if the consumer's reduced appetite for goods and services can keep corporate earnings at levels that justify current stock market valuations. The earth is shaking the ground under the consumer's feet in a way not seen in 100 years, and they know it, even if sky-high stock market prices do not. Stay tuned. It won't be better days ahead for the economy if you can't get the consumer to cheer up. Bet on it.

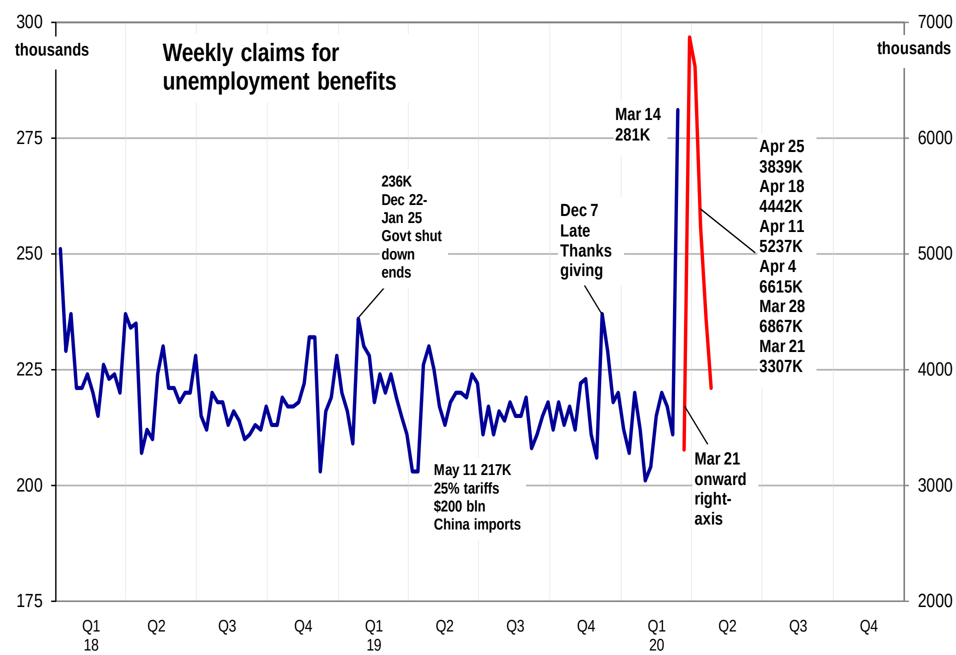


Another day another 3.8 million sacked, the others saving not spending. Buy stocks. (Thursday)

Breaking economy news. The economy continues to print numbers that scare the living daylights out of everyone in the world but stock market investors. Washington is winning the coronavirus pandemic war for the economy and bending the curve of job losses from 4.442 million last week to just 3.389 million Americans this week. The worst is over. Buy stocks. Buy them all. This market's going up. Small matter really that 30 million have lost their jobs the last six weeks which puts the unemployment rate at 23.0% versus 4.4% in last month's report. Forget about it. Better days lie ahead. Buy stocks.

We got some inflation data too today. Guess it fits the story hand and glove. 23% unemployment is Great Depression kind of stuff and sure enough there's some deflation too with headline PCE inflation dropping 0.3% in March, dropping as in an economic depression where demand for goods and services plummets, dropping for the month although still rising (for now) by 1.3% on a year-to-year basis. Whew.

Personal saving as a percentage of disposable income jumped to 13.1% in March from 8.0% in February as Americans are waking up to the need to have some cold, hard cash stashed away just in case this pandemic virus never goes away or returns later this year or in 2021. With the unemployment rate approaching the 25% level of the Great Depression many are unable to save and wages and salaries tumbled 3.1% to $9.217 trillion in March. No wonder consumer spending fell so much in the first quarter and could fall three times as hard in the second quarter.



Net, net, the economy hit the skids in March with Great Depression kind of losses in incomes and spending, and job losses that border on frightening over the last six weeks. The unemployment rate could be an astounding 23% with 37 million out of work, and it is naïve to think everyone is going to get their jobs back when this pandemic virus goes away. The Great Depression was three and a half years long and it will be just as long again before the country gets back to the best economy in fifty years where we were at the start of 2020.

Consumers can't spend it if they've not got it, and right now consumers' two-thirds contribution to economic growth has all but disappeared and the economy is staring into the abyss of the sharpest decline in history this quarter. Stay tuned. Don't go anywhere. It's not safe outside. Bet on it.

Purchasing managers at factories say we are in a recession. We forecast one too. (Friday)

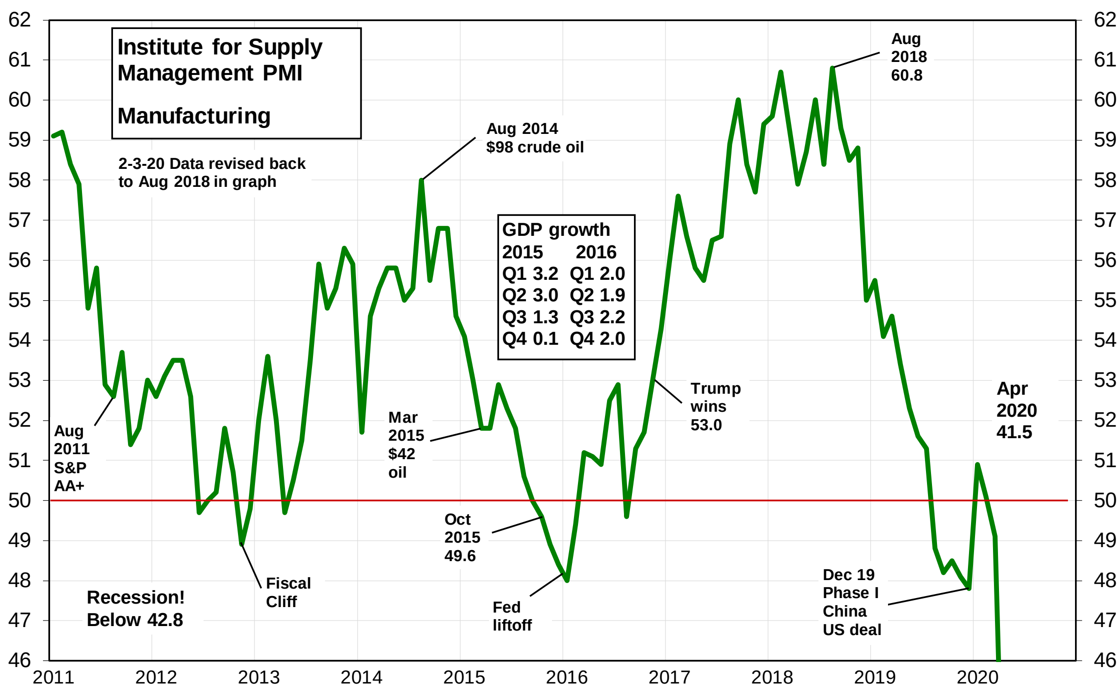
Breaking economy news. The Institute of Supply Management (ISM) survey for manufacturing fell sharply, down 7.6 percentage points to 41.5 in April. Any index reading below 42.8 means a recession for the broader economy according to ISM. Purchasing managers said manufacturing was in a recession from August to December last year which pushes back on the idea that this was the best economy in fifty years before the coronavirus pandemic sent people home and led to a sharp drop in real GDP in the first quarter.

ISM manufacturing index

	Apr 20	Mar 20	Feb 20	Jan 20	Dec 19	Nov 19
PMI index	41.5	49.1	50.1	50.9	47.8	48.1
Prices	35.3	37.4	45.9	53.3	51.7	46.7
Production	27.5	47.7	50.3	54.3	44.8	48.0
New orders	27.1	42.2	49.8	52.0	47.6	46.8
Supplier deliveries	76.0	65.0	57.3	52.9	52.2	51.7
Employment	27.5	43.8	46.9	46.6	45.2	46.8
Export orders	35.3	46.6	51.2	53.3	47.3	47.9

Net, net, purchasing manager executives in manufacturing say the entire country has sunk into a recession now. It isn't as if markets needed the additional confirmation as the news comes a couple of days late after GDP was reported down 4.8% in the first quarter on Wednesday. It is still shocking to read that only 2 out of 18 industries are growing: paper products, and food and beverage products. And even this news needs to be tempered by a paper products industry executive saying activity was slowing down in May after a strong March and April. Funny, we still can't buy any paper towels.

The ISM manufacturing survey has come late to the recession forecasting party this time as this recession is the quickest deterioration in economic activity ever recorded. Most of the country was still at work in mid-March before workers were sent home into self-isolation. For those economists selling leading economic indicators, thank you for your efforts, but Main Street already knows they are doomed. Even the Federal Reserve Chairman sees risks of a slow restart with business activity potentially facing a difficult economic recovery for the next year or so. Stay tuned. Story developing.



Analyst Certification

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