Financial Market Weekly

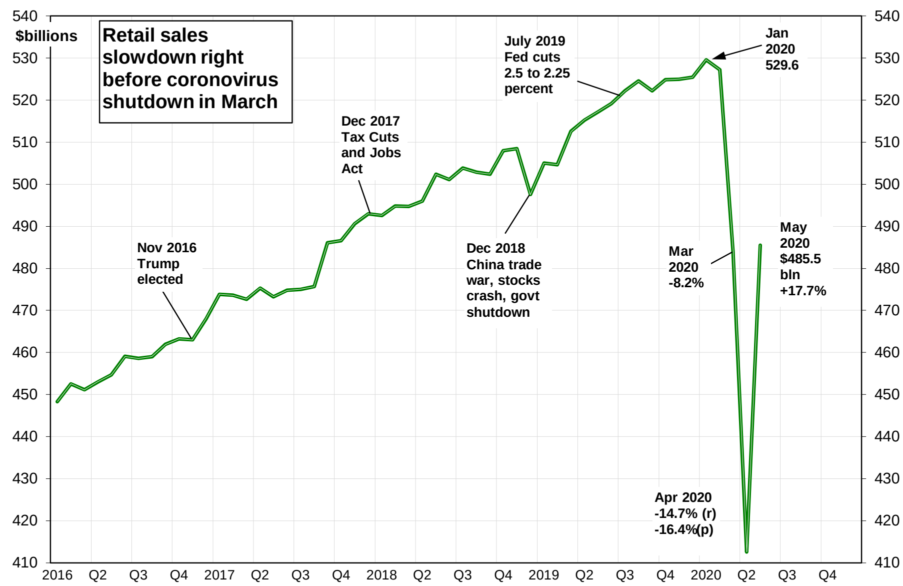
MUFG UNION BANK, N.A.
ECONOMIC RESEARCH (NEW YORK)
CHRISTOPHER S. RUPKEY, CFA
MANAGING DIRECTOR
CHIEF FINANCIAL ECONOMIST
(212) 782-5702
crupkey@us.mufg.jp

19 JUNE 2020

MUFG Bank, Ltd.
A member of MUFG, a global financial group

THE CONSUMER IS BACK. WILL IT BE ENOUGH TO CARRY THE RECOVERY?

Retail sales beat expectations jumping 17.7% in May which is a complete rebound from that 14.7% collapse in April. V-shaped for a day. The stock market is happy, though investors in the equity market are rarely unhappy for long these days. Dow stock futures were up about 630 points at 830am ET when the retail sales numbers were released on Tuesday, but the Dow industrials index closed up just 526 points on the day. That was it with three straight days of modest losses for stocks ending the week down 9.3% year-to-date.

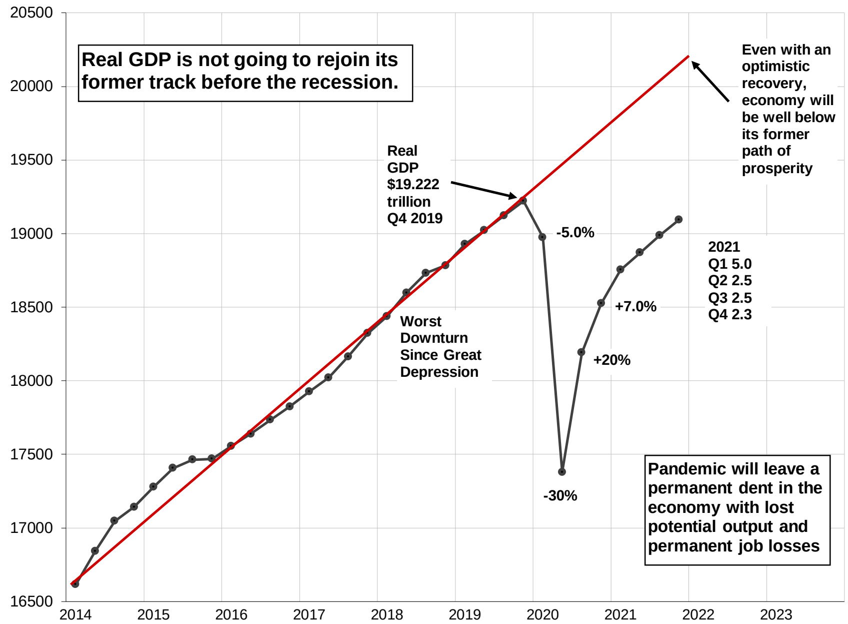


Retail sales up 17.7% was big. We have never seen store numbers like this in our career. Motor vehicles up 44.1%, furniture up 89.7%, electronics and appliances up 50.5%, clothing up 188.0%, sporting goods, hobbies and books up 88.2%, and bars and restaurants up 29.1%.

Maybe we should throw those dismal 50% GDP decline forecasts for the second quarter due to be reported on Thursday, July 30 out the window. The consumer is two-thirds of spending in the economy and right now consumer spending using retail sales is running -35% in the second quarter which assumes no change in June data. Before today's report with just that April plunge in retail sales, spending for the second quarter was down more than 60%.

<u>Trump twitter video 6-19-20</u>
As many of you know, our country is coming back very, very strong, economically. The jobs numbers from two weeks ago were record setting. Record setting increase. We've never had anything like it. Record from day one, nobody's ever beaten it. And now retail sales numbers are incredible.

Down 60% as in that's where all the 50% drop in real GDP forecasts came from. It is kind of interesting for some to speculate that the third quarter real GDP number could be a whopper. Retail sales don't have to grow all that much the next several months for real consumption expenditures in real GDP to increase 40% in the third quarter. The third quarter whopper comes out on Thursday, October 29 less than a week before the presidential election on Tuesday, November 3. Not all the American public will be impressed with the strong economic growth as millions and millions are likely to still be unemployed from the coronavirus pandemic recession. GDP growth is climbing but it will remain short of the path it was on before the recession and this means massive unemployment is likely to persist.



Net, net, the economy took a big step forward to recovery with consumers flooding into the shops and malls as the company reopened in May after the stay-at-home orders were lifted. This is looking like the shortest economic recession in history if consumer expenditures are the relevant guide to the economy's fortunes. There's no second wave fears for consumers at all. They are back! This is sure to make even Fed Chair Powell smile a little as the economic outlook is a little less uncertain and the long road to recovery has been shortened a little perhaps. A lot of little's in there, but this is great news. This is the greenest green news on the economy since the coronavirus pandemic shutdown in March. Bet on it. This economy is going up.

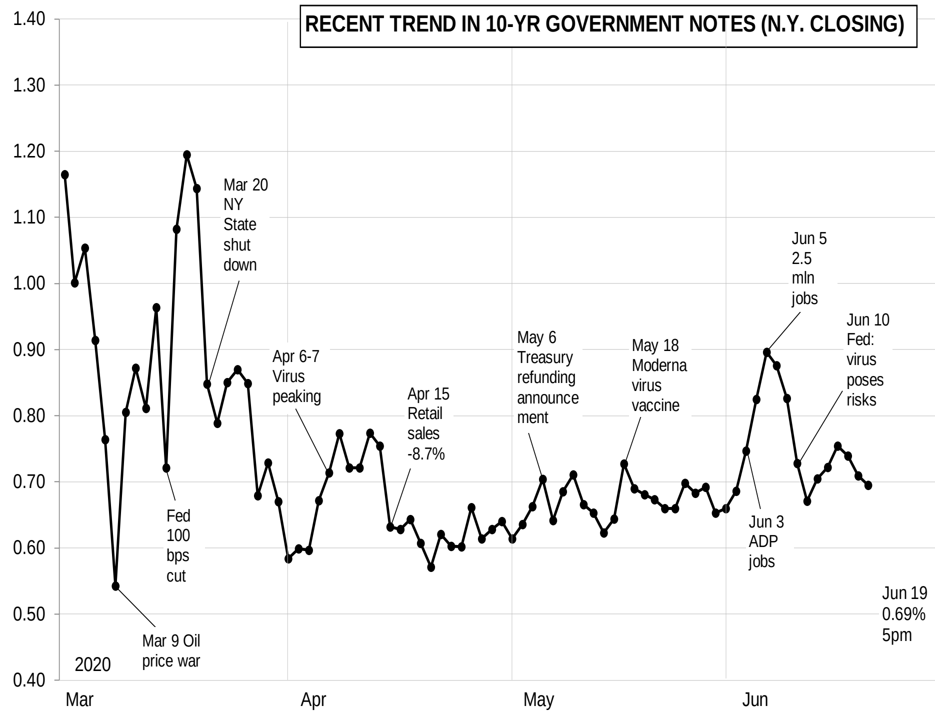
Monthly %Change	Retail Sales	$bln	Quarter Average	Percent SAAR	Real Consumer Spending	Real GDP
0.1	Dec 2019	525.467	525.111	2.2	1.8	2.1
0.8	Jan	529.616				
-0.4	Mar	527.273				
-8.2	Mar 2020	483.949	513.613	-8.5	-6.8	-5.0
-14.7	Apr	412.576				
17.7	May	485.545				
3.0	Jun 2020	500.300	466.140	-32.2	-25.0	-30.0
0.9	Jul	505.000				
1.0	Aug	510.000				
1.0	Sep 2020	515.000	510.000	43.3	25.0	20.0

Retail spending, actual dollars, each month

	$million May 2020	% to Total	Percent Changes % May	Apr	Year/year
Total Retail Sales	485,545	100.0	17.7	-14.7	-6.1
Motor vehicles/parts	98,621	20.3	44.1	-12.3	-3.9
Furniture/furnishings	7,722	1.6	89.7	-48.4	-21.5
Electronics/appliances	5,679	1.2	50.5	-43.2	-29.9
Building materials/garden	36,319	7.5	10.9	-2.4	16.4
Food & beverage	72,590	15.0	2.0	-12.8	14.5
Health/personal care	26,983	5.6	0.4	-14.8	-10.3
Gasoline stations	29,405	6.1	12.8	-24.4	-30.8
Clothing/accessories	8,116	1.7	188.0	-75.2	-63.4
Sporting goods, books	6,936	1.4	88.2	-33.7	4.9
General merchandise	59,530	12.3	6.0	-13.6	0.0
Department stores	8,472	1.7	36.9	-28.1	-25.8
Miscellaneous retailers	8,611	1.8	13.6	-25.9	-22.8
Nonstore retailers (internet)	86,406	17.8	9.0	9.5	30.8
Eating & drinking places	38,627	8.0	29.1	-34.6	-39.4

MARKETS OUTLOOK

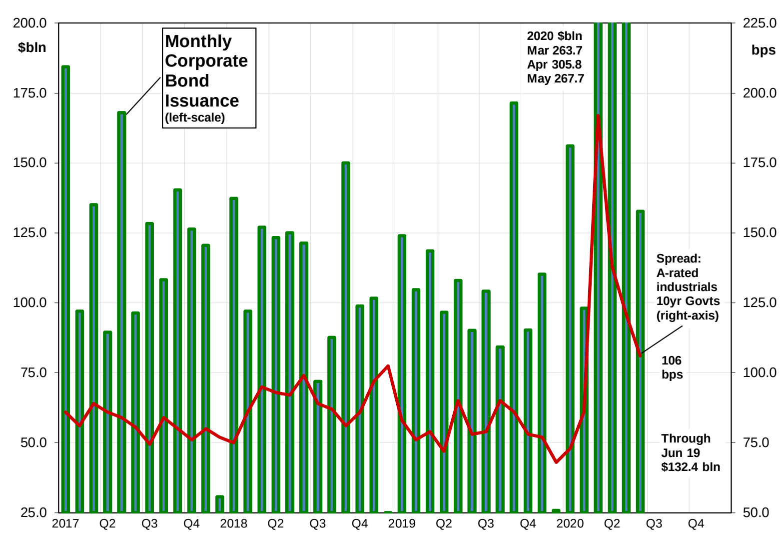
	29-Mar 2019	28-Jun 2019	30-Sep 2019	31-Dec 2019	31-Mar 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021
30-Yr Treasury	2.81	2.53	2.11	2.39	1.32	1.30	1.30	1.40	1.50	1.60
10-Yr Note	2.41	2.01	1.67	1.92	0.67	0.70	0.70	0.80	0.90	1.00
5-Yr Note	2.23	1.77	1.55	1.69	0.38	0.30	0.40	0.60	0.70	0.80
2-Yr Note	2.26	1.76	1.62	1.57	0.25	0.20	0.30	0.30	0.40	0.40
3-month Libor	2.60	2.32	2.09	1.90	1.45	0.40	0.30	0.20	0.20	0.20
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	50	40	50	50	60



10-yr year yields 0.69% this week after closing 0.70% last week. Coronavirus headlines dominate the news for bonds. Yields fell immediately Sunday night at the week's open on reports of more virus cases in China and some states in the U.S. Dow stock futures fell 1,000 points by 2am early Monday morning before recovering. Bond yields fell to the low of the week early Monday at 0.65%. Stocks had another leg up at 2pm Monday afternoon when the Fed announced it would buy corporate bonds where before the purchases for the lending facility were ETFs. The next day Powell in the semiannual monetary policy report testimony downplayed the corporate bond purchases: they wouldn't be an "elephant" in the bond market. The yield high this week was 0.78% after retail sales on Tuesday.

CORPORATES: T-MOBILE, PG&E CORP, DANA INC, UPJOHN INC, AIR LEASE

Corporate bond offerings were $50.4 billion in the June 19 week versus $30.9 billion in the June 12 week. On Tuesday, Merck & Co. sold $4.5 billion 5s/10s/20s/30s. It priced a $1.25 billion 1.45% 10-yr (m-w +15bp) at 80 bps (A1/AA-). The global health care company will use the proceeds for general corporate purposes including repayment of commercial paper borrowings and other indebtedness. Corporate bond yields (10-yr Industrials rated A2) were 106 bps above 10-yr Treasuries Friday versus 113 bps last Friday.



FEDERAL RESERVE POLICY

The Fed meets July 28-29, 2020 to consider its monetary policy. Powell just had a press conference on June 10 and now this week he was back for more somehow with the semiannual monetary policy report. He gave his testimony and took a lot of questions Tuesday before the Senate and Wednesday before the House. Senator Tillis (R-NC) asked about yield curve control (ZZzzzz… the bond market is dead and even a poke with a stick couldn't waken it) and Powell said they were briefed at last week's FOMC meeting on the historical use of yield curve control in the U.S. This was meant just as an education for the committee and maybe they could consider later on whether it would be useful. He also remarked in answer to the Tillis question that they have "pretty much decided that" negative rates wouldn't be an attractive policy option here in this country. This was a second go at this topic as Senator Toomey (R-PA) asked earlier about Powell's thoughts about establishing yield targets on the Treasury curve. Powell did say if rates were to move up a lot for some reason and they wanted to keep rates low and monetary policy accommodative then one might think about using it, not on the whole curve, but maybe some part of the curve. No decision has been made; they are evaluating it.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	17-Jun	10-Jun	3-Jun	27-May	pre-LEH
Factors adding reserves					
U.S. Treasury securities	4169.340	4150.409	4134.356	4109.512	479.782
Federal agency debt securities	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	1918.741	1835.595	1835.594	1835.110	0.000
Repurchase agreements	79.053	167.300	211.550	181.101	126.750
Primary credit (Discount Window)	7.479	8.427	11.011	18.198	23.455
MMLF	24.680	26.977	29.859	33.244	
PDCF	5.306	5.829	5.847	6.241	
Commerical Paper Funding Facility	12.797	12.796	12.795	12.794	
Paycheck Protection Facility	57.552	56.983	55.230	49.211	
Corporate Credit Facility (CCF)	38.916	37.374	36.154	34.853	
Municipal Liquidity Facility	16.079	16.077	16.075	0.000	
Main Street Lending Program	31.876	31.875	0.000		
Central bank liquidity swaps	352.470	444.520	466.945	448.946	62.000
Federal Reserve Assets	7143.4	7217.6	7213.4	7145.9	961.7
3-month Libor %	0.32	0.32	0.33	0.36	2.82
Factors draining reserves					
Currency in circulation	1959.750	1955.861	1952.420	1948.196	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Treasury credit facilities contribution	104.000	104.000	104.000	66.500	
Reverse repurchases w/others	0.001	0.012	0.013	4.326	0.000
Reserve Balances (Net Liquidity)	3069.439	3190.654	3257.435	3317.688	24.964
Treasuries within 15 days	70.365	42.873	49.583	55.608	14.955
Treasuries 16 to 90 days	276.151	292.827	283.619	279.039	31.549
Treasuries 91 days to 1 year	587.886	586.718	589.247	564.220	69.272
Treasuries over 1-yr to 5 years	1581.775	1581.035	1575.173	1577.552	170.807
Treasuries over 5-yrs to 10 years	729.159	725.316	719.393	719.915	91.863
Treasuries over 10-years	924.006	921.640	917.341	913.177	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

CCF: Corporate credit facility: Primary market (PMCCF) and Secondary Market (SMCCF)

The other noteworthy interest rates question was from Senator Perdue (R-GA) who asked whether the Fed was monetizing the debt. Powell said that wasn't their intention. The March and April debt purchases were for market functioning reasons. "It wasn't in any way about, you know, meeting Treasuries supply. And it continues not to be." We will have to wait for a while longer to see whether the Fed buys more Treasuries because the Federal budget deficits increase enough to push bond yields higher than Fed officials might want to see. Everything is fine right now with 10-y Treasury yields of 0.69% and the Fed QE Treasury purchases of $2.061 trillion in fiscal year 2020 and the Treasury auctions to fund the budget deficit running $3.545 trillion so far this fiscal year ending in September. No extra money was provided this week by the Fed's 11 lending facilities as the economy faces a second wave outbreak of the virus in several states: $187.2 billion on June 17 from $187.9 on June 10.

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	May	Jun	Total FY 2020
Fed QE	67.808	73.007	80.364	80.246	64.952	504.312	993.047	138.093	59.828	2,061.7
New Cash	166.8	112.5	50.9	38.5	199.8	238.7	1368.6	699.2	670.2	3,545.2
Bills	79.1	59.0	-98.2	-12.5	160.3	92.8	1344.3	628.2	434.7	2,687.6
Coupons	87.6	53.4	149.2	51.1	39.5	145.8	24.2	71.0	235.5	857.3

OTHER ECONOMIC NEWS THIS WEEK

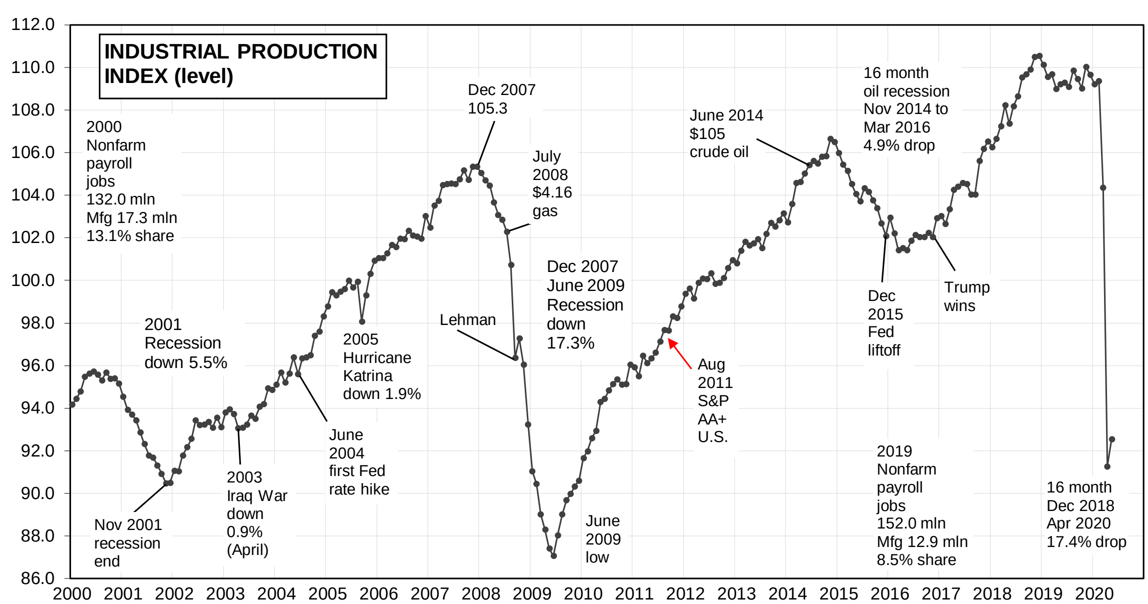
Factories are rebounding less than consumer spending in May (Tuesday)

Breaking economy news. Industrial production rose 1.4% in May after collapsing 12.5% in April and 4.6% in March. April was revised down 1.3 percentage points so the manufacturing sector is still in a bit of a rut. Factories are harder to restart than retail spending in the economy, that's for sure. Mining is still falling by 6.8% in May as the collapse in oil prices, negative briefly in April, is still taking a toll on the oil & gas industry. The biggest jump was in motor vehicle production, although a lot of the recovery is going to depend on whether consumers buy more cars and SUVs: May sales were still only 12.6 million in May down from 17.3 million in January/February, all months are annual rates.

Net, net, the nation's manufacturing sector says the economy is not heading back to normal as fast as the consumer says it is. It is harder and much more complicated for factories to restart after being shut down than it is for consumers to start up their cars and drive over to the mall. Not for all consumers as our car's battery was dead after not being driven for three months.

Percent changes			Industrial Production May 2020		
Mar	Apr	May	YOY		Weight
-4.6	-12.5	1.4	-15.3	Total Index	100.0
-5.3	-15.5	3.8	-16.5	Manufacturing	75.3
-1.9	-6.1	-6.8	-14.1	Mining	14.2
-3.1	0.1	-2.3	-8.0	Utilities	10.4
			Manufacturing payroll jobs 11.7 million -1122K YOY 10.5% of Private Payroll Jobs		

Today's data mix on consumer spending and industrial production point out that there are still challenges ahead for the economy to get back to normal health where it was at the start of the year. Washington can't just snap their fingers and bring the country back to the best economy in 50 years seen at the start of 2020. Factories don't produce goods unless consumers are buying them, but at the same time, many companies have seen severe financial damage and may not quickly resume the investment spending the economy needs for growth in the future. We need the economic recovery to fire on both cylinders of consumer spending and business investment, and right now, companies, with financial losses on the books and with greater debts to pay, may be slow to resume investing in the economy's future.

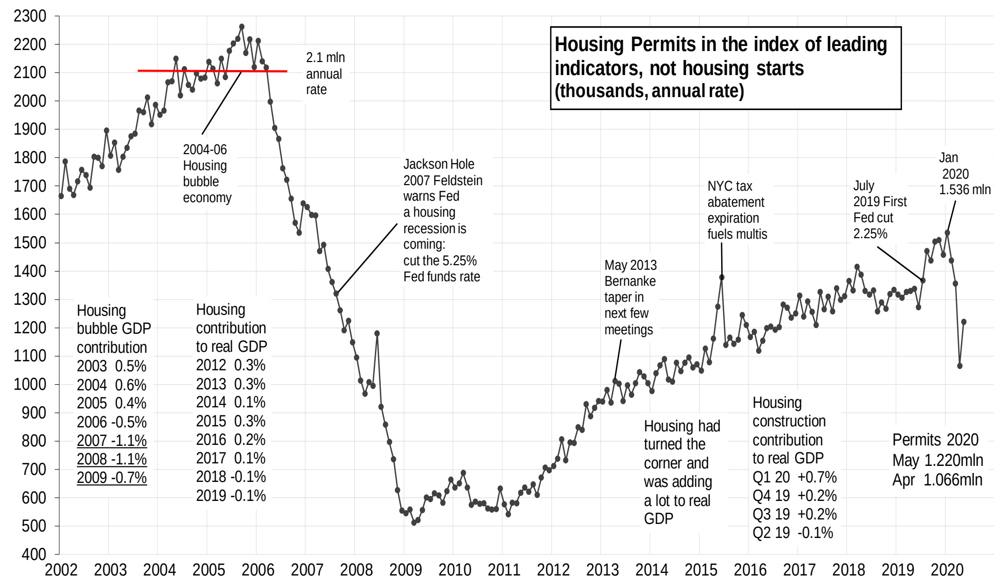


Jump in housing permits looks V-shaped (Wednesday)

Breaking economy news. Housing starts rose 4.3% to 974 thousand in May, but housing permits are future housing starts and permits jumped 14.4 percent to 1.220 million in May and apartment permits are up 18.3 percent which is a stronger rebound than the 11.9 percent gain in single unit housing permits.

Housing starts were held back by a large 16.0% drop in the biggest market down South and a 1.5% decline in the Midwest. Starts in the Northeast rose 12.8% and a 69.8% gain in the West.

Net, net, homebuilders remain confident that if they build it they will come as new permits jumped 14.4 percent in May. Housing starts are lagging the recovery a little where the country was still opening back up in May. But with permits running 1.220 million in May we are confident that housing starts at 974 thousand in May are on their way back up as the housing sector has weathered the pandemic recession. There's concern about a second wave of the virus in the markets, but home builders plainly aren't worried as they apply for the permits to build more homes and apartment complexes.



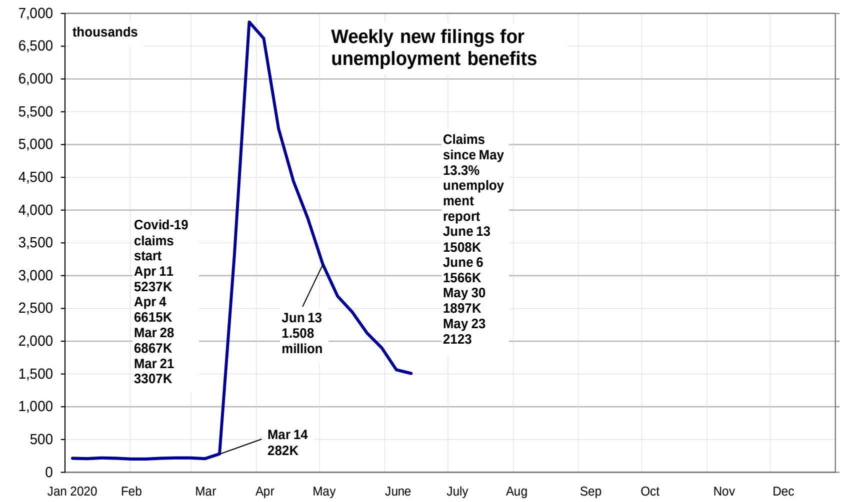
Residential housing construction is in a strong V-shaped recovery for now, just like overall retail sales at shops and malls, but this is driven primarily by pent-up demand after the gates opened and the public was let loose after the stay-at-home orders were lifted. We expect construction to fall back somewhat before moving higher again by the end of the year making the recovery in residential housing construction more of a W-shape. Housing is a leading economic indicator and it is pointing the way forward but there is a limit to growth when the economy has to drag along the millions and millions of unemployed workers displaced in this pandemic recession who won't be seeing paychecks anytime soon. Stay tuned. Story developing.

Housing Permits Total, Single-Family, Multi-Family

	United States			Northeast		Midwest		South		West	
000s	Total	1 unit	Multi	Total	1 unit	Total	1 unit	Total	1 unit	Total	1 unit
May 20	1220	745	434	111	48	167	101	659	431	283	165
Apr 20	1066	666	367	61	32	141	90	612	408	252	136
May 19	1338	827	474	104	50	175	111	713	470	470	196
% Chgs											
May/Apr	14.4	11.9	…	82.0	50.0	18.4	12.2	7.7	5.6	12.3	21.3
May/May	-8.8	-9.9	…	6.7	-4.0	-4.6	-9.0	-7.6	-8.3	-18.2	-15.8

Green shoots for growth will wither on the vine if joblessness continues (Thursday)

Breaking economy news. The number of workers fired in the June 13 week are still almost double the worst of the last recession. 1.508 million applied for regular program unemployment benefits in the June 13 week and 760 thousand gig workers filed in their own Pandemic Unemployment Assistance program for unemployment compensation. The stock market can't stick its head in the sand and say everything is okay when over 2.2 million people applied for jobless benefits this week.



We are guessing at the week ahead figures for gig workers, but it looks like 28.6 million are out of work and getting a check in the June 6 week under both programs. The BLS said the number of unemployed in May were just 20.985 million. It looks like it is hard to pick up in a survey of Americans how bad it is out there, but 28.6 million receiving benefits is a big number and a big deal. It's still bad out there in June. The recent sightings of green shoots for economic growth are going to fade in a hurry if workers can't return to the jobs they lost during the pandemic recession and right now tens of millions remain unemployed and are collecting benefits and hundreds of thousands more are making first time applications for jobless benefits because they were let go just in the last week.

Net, net, the green shoots for growth will all wither on the vine if joblessness continues at this rate. Over 20 million out of work without a paycheck is a lot of spending missing from the economy. Part of the reason stock market investors think this is a normal recovery and are buying shares is that they are mistaken in just how deep the hole the economy is in and how long the road to recovery will be for companies to make money again given the debt they took on to weather the storm.

Unemployment Rolls Total				
	Total getting Jobless Benefits	Total "Continuing" Claims	Pandemic gig worker claims	Pandemic Emergency claims
Mar 13	2,074,800	2,074,800	0	0
Apr 25	25,175,004	21,772,595	3,402,409	
May 2	27,000,032	20,879,704	6,120,328	
May 9	30,809,511	22,794,145	7,793,066	222,300
May 16	30,010,508	18,861,428	10,926,386	222,694
May 23	29,344,530	19,098,624	9,725,386	520,520
May 30	28,985,978	18,628,015	9,280,644	1,077,319
Jun 6		18,654,001	10,079,153	gig est.

The stock market can't have it both ways. Investors bought the shares of companies like Facebook, Apple, Microsoft, Amazon, Alphabet because they were the future in a stay-at-home economy shuttered by the coronavirus pandemic. If the lockdown is all but over, except for a second wave in a handful of states, then these are the wrong stocks and the entire market is overvalued because the economy is normalizing. On the other hand, if this is the biggest downturn since the Great Depression then stocks are too high because it all happened so quickly that they haven't reported their full-on recession earnings yet. Keep buying for now on your smartphone apps because you won't want to in July when the earnings reports start to roll in and we get the report of the biggest drop in GDP in history on July 30. It will be like a bomb going off. Don't ask for whom the bell tolls, it tolls for thee.

Analyst Certification

The views expressed in this report accurately reflect the personal views of **Christopher S. Rupkey**, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and no part of such analyst's compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed herein.

About Mitsubishi UFJ Financial Group, Inc.'s U.S. Operations including MUFG Americas Holdings Corporation

The U.S. operations of Mitsubishi UFJ Financial Group, Inc. (MUFG), one of the world's leading financial groups, has total assets of $341.4 billion at December 31, 2019. As part of that total, MUFG Americas Holdings Corporation (MUAH), a bank holding company and intermediate holding company, has total assets of $170.8 billion at December 31, 2019. MUAH's main subsidiaries are MUFG Union Bank, N.A. and MUFG Securities Americas Inc. MUFG Union Bank, N.A. provides a wide range of financial services to consumers, small businesses, middle-market companies, and major corporations. As of December 31, 2019, MUFG Union Bank, N.A. operated 349 branches, consisting primarily of retail banking branches in the West Coast states, along with commercial branches in Texas, Illinois, New York and Georgia. MUFG Securities Americas Inc. is a registered securities broker-dealer which engages in capital markets origination transactions, private placements, collateralized financings, securities borrowing and lending transactions, and domestic and foreign debt and equities securities transactions. MUAH is owned by MUFG Bank, Ltd. and Mitsubishi UFJ Financial Group, Inc. MUFG Bank, Ltd., a wholly owned subsidiary of Mitsubishi UFJ Financial Group, Inc., has offices in Argentina, Brazil, Chile, Colombia, Peru and Canada as well as branches, agencies and representative offices in the U.S.
Visit https://www.unionbank.com/ or https://www.mufgamericas.com/ for more information.

About MUFG

Mitsubishi UFJ Financial Group, Inc. (MUFG) is one of the world's leading financial groups. Headquartered in Tokyo and with over 360 years of history, MUFG has a global network with over 3,000 locations in more than 50 countries. The Group has over 180,000 employees and offers services including commercial banking, trust banking, securities, credit cards, consumer finance, asset management, and leasing. The Group aims to "be the world's most trusted financial group" through close collaboration among our operating companies and flexibly respond to all of the financial needs of our customers, serving society, and fostering shared and sustainable growth for a better world. MUFG's shares trade on the Tokyo, Nagoya, and New York stock exchanges. For more information, visit https://www.mufg.jp/english.