U.S. economic forecast and COVID-19

Last updated July 17, 2020

(All information is for the U.S. and references to quarters are based on calendar years.)

Top economic news

- **Consumer prices rose 0.6% in June** after falling each of the previous three months according to the Labor Department.
  - Grocery prices rose 0.7%, apparel prices rose 17% and gasoline prices rose 12.3%.
- **Exports from the US fell 4.4% in May** and imports fell 0.9% according to the Commerce Department.
  - The seasonally adjusted trade deficit is now $54.6 billion, expanding by 9.7% in May.
- The **U.S. budget deficit reached $3 trillion** in the 12 months through June, due in large part to decreased tax revenue and increased government spending.
  - The federal government is on pace to register **the largest annual deficit as a share of GDP since World War II**.
  - In June alone, **the deficit widened to a monthly record of $864 billion** (according to the Treasury Department), nearly as much as the gap for the entire previous fiscal year, which totaled $984 billion.
- **The producer-price index fell 0.2% in June** according to the Labor Department, signaling subdued inflation that should allow the Federal Reserve to continue injecting money into the economy.
  - This pales in comparison to the 1.3% decline we saw in April, **the biggest decline in the PPI since December 2009**.
- The worst effects of the pandemic on global oil demand have passed according to the International Energy Agency. According to IEA's latest monthly report, **global oil demand was down roughly 11%** from last year.
  - The **West Texas Intermediate crude oil benchmark has increased over 250%** from its April low when oil prices briefly went negative.
- The Commerce Department reported that retail sales increased a seasonally adjusted 7.5% for the month of June. Retail sales totaled $524.3 billion in June, up from $487.7 billion in May and nearly back to pre-pandemic levels.

EXECUTIVE SUMMARY

- Governor Newsom signed the 2020-21 state budget that includes a **CARES Act COVID-19 relief fund of $9.5 billion.**
  - $500 million will be disbursed to cities and $1.3 billion to counties
  - Using data from the Department of Finance, GSEC has calculated that approximately **$410 million in total will be disbursed to Greater Sacramento** communities.
- Chief Executive published the results of their July CEO Confidence Index which shows **optimism on the economy is nearing pre-crisis levels.**
  - Chief Executive polled 326 U.S. CEOs on their confidence in business conditions. At 6.6 out of 10, CEO confidence levels were found to be nearing January's pre-pandemic levels (6.7).
  - The July results also showed a **111% increase in respondents projecting profits to increase over the coming year** since the bottom of the crisis in early April.
  - **Large companies remain the least optimistic in future business conditions.** CEOs in that group were weary of the upcoming election with concerns over tax increases and new regulations.
- The Harvard Business Review published tips for communicating with employees during a crisis:
  1. **Communicate frequently:** Frequent communication reduces fear and uncertainty and increases the likelihood that employees will hear the message.
  2. **Provide Safe Channels for Giving Feedback:** Employees must be able to express their concerns to leaders without fear of retribution. Leaders must periodically report what they are hearing from their employees to help build trust..
  3. **Help Employees Work at Home Effectively:** Employees who feel they have what they need to remain productive and successful while working remotely are more likely to be satisfied with their organization's overall response to the pandemic.
  4. **Address Concerns About Job Security:** Leaders should reassure their team members that their employment is secure, when this is the case. When it is not, employees appreciate knowing all they can as soon as possible so they can plan accordingly.
  5. **Provide a Plan for the Future:** Share as much as you can about your strategy and plans for the future while recognizing employees who have gone the extra mile to drive results.

UNEMPLOYMENT

United States

Initial unemployment claims fell by a seasonally adjusted 10,000 to 1.3 million for the week that ended on July 11 as reported in the latest news release from the Labor Department

Still, last week's levels **far surpass the week record before 2020, which was 695,000 in 1982.** Overall, the employment report for June showed a solid gain of 4.8 million jobs and an unemployment rate that fell to 11.1% from 13.3% at the beginning of the month. Employers added a combined 7.5 million jobs in May and June after shedding 21 million jobs in March and April.

According to the latest Bureau of Labor Statistics report, the unadjusted number of people claiming unemployment insurance benefits in state programs totaled over 17.3 million, an increase of 5.1% from the previous week.

California

California's unemployment rate stands **above the U.S. average.** According to the state series unemployment data released by the Bureau of Labor Statistics on July 17, **California's unemployment rate in June was 14.9%**, 3.8% greater than the U.S. rate of 11.1%.

The state's unemployment rate now stands **as one of the highest of all U.S. states.** The three states that had the highest unemployment in June are the northeastern cluster of Massachussetts at 17.4%, New Jersey at 16.6% and New York at 15.7%. All three states, like California, have been amongst those hit hardest by the pandemic and have all enacted similarly stringent lockdown measures.

There were some signs of optimism in California, however. The state added 558,200 jobs from May, representing an increase of 3.7% and leading to **an overall decrease in the unemployment rate of 1.5%** from May's rate of 16.4%.

Nonethless, the state has lots of work to do in order to restore the unemployment levels we observed just a year ago of 4%. In total, **there are over 1.7 million less employed people today in California than there were in June 2019,** representing a 10% decrease from today's state job count.

Economic Growth

Forecasts of economic growth are continuously evolving as various factors that alter the landscape of the U.S. economy continue to arise. Currently, a second wave of infections has worsened the economic outlook for Q2 and the rest of the fiscal year. Having had some of the worst spikes in cases in the U.S., California has reintroduced a restriction lasting three weeks that is expected to further slow economic growth and recovery.

We will mostly focus on predictions for the following fiscal quarter. Due to the volatile and ever-changing nature of our current economy, long-term predictions can be rendered obsolete thanks to new developments in a span of days. Below is a summary of the latest forecasts from the top forecasting entities in the economic landscape. We use an average across the forecasts to generate a GSEC prediction of Q3 GDP contraction.

WELLS FARGO

In their most recent economic update on July 9, **Wells Fargo predicted we'd see a 35% shrinkage in GDP for Q2** when the official data is released at the end of the month. Projections for GDP growth in Q3 have been **dialed back from 24% to 18%** due to the steps many states, including California, have taken to slow the process of re-opening due to surging cases.

In the monthly outlook, Wells Fargo stated that **monthly data seems to suggest that the economy hit bottom in May.**

It is important to note that two fundamental assumptions behind their predictions:

- The eventual development of an effective vaccine that would allow economic life to gradually return to "normal"
- That the generalized lockdown of the economy that occurred in March and April does not re-occur.
- Should one or both of these assumptions be violated, a major downside risk to this forecast may be realized.

JP MORGAN

In their weekly economic update posted on July 13, JPMorgan Asset Management cited gains in production and employment over the past month to support their **Q2 forecast of -35% GDP shrinkage**, rather than a previously predicted -40%, **followed by a Q3 rebound of 20%** with much slower growth thereafter.

THE CONFERENCE BOARD

The Conference Board economic think tank makes two presumptions for their baseline forecast:

- There will not be a large second wave of cases in the fall
- The presence of weak consumer demand due to persistently high unemployment and the expiration of various government stimulus programs

They predict a **Q2 GDP contraction of nearly 40%** driven by a fall in consumer spending of nearly 40%, **followed by a large rebound of over 20% in Q3** and a slowdown in GDP growth of 1% in Q4.

FEDERAL RESERVE BANK OF ATLANTA

The Federal Reserve Bank of Atlanta provides a "nowcast" titled "GDPNow" that is a running estimate of real GDP growth based on available data for the current measured quarter. They employ methodology similar to the one used by the Bureau of Economic Analysis.

As of July 9th, **the GDPNow model estimates real GDP growth in Q2 to be -35.5%.**

WALL STREET JOURNAL (WSJ)

The Wall Street Journal's Economic Forecasting Survey surveys nearly 80 economists on more than 10 major economic indicators on a monthly basis, including GDP.

In their latest update on July 9, the WSJ projection average reveals **GDP shrinkage of -31.9% in Q2 and a projected GDP increase of 15.2%** in Q3 of 2020.

In their forecasting survey Q&A, 25.5% of respondents said they expected the economic recovery to start in Q2, 63.8% said in Q3 and 4.3% said in Q4. About 6.5% of the respondents don't expect the recovery to begin until 2021.

CONGRESSIONAL BUDGET OFFICE (CBO)

The CBO predicts that after a strong contraction of **39.6% in Q2**, economic growth is expected to **increase 23.5%** in Q3 and 10.5% in Q4. Increases in consumer spending are expected to more than offset further declines in business investment during that period.

The CBO notes challenges in the economy and the labor market are expected to persist for some time and interest rates on federal borrowing are expected to remain low in relation to rates in recent decades.

CNBC AND MOODY'S ANALYTICS

With each major report that impacts GDP, these two entities calculate the new median quarterly GDP tracking forecast among a select group of Wall Street economist. **Their data shows a median GDP estimate of -35.4% for Q2 and +16.1% in Q3.**

FANNIE MAE

On July 14 Fannie Mae issued a revised GDP forecast with an upward trend despite infection resurgence. Due to faster than anticipated consumer recovery, as reflected in the personal consumption expenditure data (PCE), **Fannie Mae predicts a 34.8% drop in GDP for Q2.**

They cite a combination of higher consumption expenditures and a comparatively lower need to draw down inventories in **Q3 that translates to 27.4% annualized growth in GDP for Q3.**

GSEC PREDICTION

Overall, we expect a decline in GDP for Q2, at an annualized rate, **of approximately 34.9%,** up from our last Q2 projection of -39.7%, and **a subsequent increase of 19.4% in Q3.**

TABLE 1: 2020 ECONOMIC GROWTH FORECASTS

Source	Quarter 2	Quarter 3
Wells Fargo	-35%	18%
JP Morgan	-35%	20%
Conference Board	-40%	20%
The Wall Street Journal	-31.9%	15.2%
Congressional Budget Office	-39.6%	23.5%
CNBC & Moodys	-35.4%	16.1%
Fannie Mae	-34.8%	27.4%
Atlanta Fed	-35.5%	N/A
GSEC (Average)	**-35.9%**	**20.02%**

REAL ESTATE

We are highlighting two major reports published by the National Association of Realtors with information that has been published within a week or less of July 16.

Highlights from the NAR's July 2020 Commercial Market Insights:

- Sales of properties of $2.5 million+ in May are down 79% from a year ago
- Nareit reported **a negative year-to-date return for the All Equity REITS Index** of about -16%, compared to the S&P 500 +2% return.
  - Lodging/resort was the **worst performing at -51%** while data centers were the highest performing property class with **a +17.3% return** over the same period.
- CMBS **delinquency rates have also spiked,** with rates **rising from just 2.07% in March to 10.32% in June.** Again, the worst performing industry was lodging (24.3%) while the lowest delinquency rates were found in industrial (1.57%).
- **The value of construction spending declined for the second straight month** in May, down 4.5% from May of last year. The largest contraction was observed in lodging (-14.7%). For now, the decline in construction spending is modest relative to declines in employment, retail sales and commercial acquisition volume.
- A silver lining in the commercial market outlook was the strong job recovery. Although a subsequent slowdown is imminent with the recent resurgence in cases, **the economy created 7.5 million net new payroll jobs in May and June, half of which were in the industries hardest hit by the pandemic: leisure and hospitality.**

Highlights from the NAR's 2020 Market Recovery Survey:

- Of a survey of 2,302 NAR members, **45% of respondents reported their market is slowly entering recovery and 28% stated their market is hotter than normal.**
  - 49% of those in urban areas reported their market is slowly entering recovery compared to 40% of those who live in rural areas, suggesting rural areas have been slower to recover from the pandemic.
- Over 60% of respondents believe the demand for virtual tours, Zoom or other video technology, live virtual tours (conducted by agent using video) and virtual open houses will see an increase in demand for the following year.
- There also appears to be **variation in safety precautions among different property types with condos having the most precautions.** For example, **24% of condos are requiring masks in public areas** while this number is **under 20%** for both HOA and apartment rental communities.
- Of those who are currently working with buyers, 54% reported their buyers' timeline has remained the same, 27% cited more urgency to buy a home and 18% reported less urgency.
  - A larger share of respondents working in urban areas reported less urgency (21%), while the share for rural and suburban respondents was the same (16%), suggesting an increased wariness towards living in densely populated urban areas.
- 26% of respondents reported working with buyers who put offers on homes without physically seeing them in person, showing that about 1/5 offers were done on an entirely virtual basis.
- In commercial real estate, **74% have reported that leases have been terminated or tenants are needing to delay their rent payments**.

Freddie Mac

The average fixed 30-year mortgage rate has now reached its lowest level ever, 2.98%, as reported by Freddie Mac.

- Mortgage rates tend to move in the same direction as the 10-year treasury note. Therefore, mortgage rates falling signifies consumer weariness about future economic prospects as they move out of riskier assets like common stocks.
- Why? Lowering yield rates is a signal of increased demand for safe assets, like a 30-year fixed mortgage asset. Since more consumers demand this asset, the issuer is able to lower the yield needed to entice buyers, thus explaining the low rates.
- What does this mean for the economy? In short **"it's an indication that we remain in a crisis"** as said by Jeff Tucker, an economist at Zillow.