

V FOR VEHICLES AND V FOR VACCINES WILL HELP

A V-Shaped Recovery, In Some Sectors

Major Obstacle: CARES Act Pays 68% of Unemployed More in Benefits than They Could Earn at Work

“Yeah, there’re letters. People are fascinated by the possibility of different letters.” – Fed Chairman Jay Powell, waiving off a “60 Minutes” question whether the grim COVID-19 recession will be followed by a classic V-shaped recovery where GDP quickly retraces its losses.

In the interview, Powell did allow that there was a “a reasonable assumption” that the economy would begin to recover in the second half of this year. But he also talked about downside risks, virus resurgence, and a crisis that could last years.

Yet despite the pessimism that has overtaken the Fed, **FMI does see clear indications of a V-shaped recovery... in some areas.** Perhaps the most noticeable will be the vehicle sector. After vehicle production fell to virtually zero in April, automakers planned to produce more than 8 mm units in May and in June (seasonally-adjusted at annual rate). While stubbornness by the Governors of Michigan and a few other states have slowed the re-opening for May, **several million vehicles should still roll off the assembly lines this month – an incalculable percentage increase over the near-zero April total – followed by another surge in June.** That will not be enough to salvage 20Q2 results for the sector. Nonetheless, we expect further improvement this summer.

Vehicle sales, which were a low-but-not-apocalyptic 8½ million units (SAAR) in April, should also be roaring back by this summer. **Vehicle sales may not return to the 17 mm unit pace early this year, but they should not be that far off.** Pessimists, including our Fed chairman, believe that consumers will be too shell-shocked to do little more than peak outside their windows when the shutdown orders end. Or we should say, when the *rest* of the shutdown orders end since all 50 states have now begun to lift restrictions and more than a few have made significant strides in “re-opening” already.

FMI has more confidence in the resilience of consumers and the economy. Plus, **with fiscal stimulus overflowing, the saving rate well into double-digits, and two months of pent-up demand, customers will be lined up in auto showrooms.** Six feet apart, of course.

Congress’ CARES-Less Folly Stimulus Program Keeps Jobless Rate High

While much of the recent news has been good, or at least better than expected, particularly on the particulars of COVID-19, **there are dark clouds on the horizon as well. They started on Capitol Hill.**

When Congress passed the CARES Act in April, an unprecedented \$2.2-trillion stimulus package, FMI had some words of praise. By sticking to cash transfers instead of brick-and-mortar boondoggles, CARES would be more timely and better targeted than most such efforts. However, FMI and others did point to one critical mis-step: **the incredibly generous boost to UI benefits was going to discourage the unemployed from returning to work.**

The logic was unassailable –so obvious even a Congressman should have understood. The law provides an extra \$600/week on top of regular UI benefits to anyone who claims COVID-19 contributed to their joblessness. The procedures, or lack thereof, guarantee that this will cover most everyone who files. Combined with the regular UI check, this bonus ensures that millions of workers earn more than they did in their former jobs. Now, *a deeper dive into the data shows that it is even worse than we expected.*

A new University of Chicago [analysis](#) found that a whopping **68% of eligible unemployed workers will receive benefits which exceed their lost earnings.** *The program does not discourage millions of people from working. It discourages 10+ million people.*

Congressional Democrats pitched the idea as replacing 100% of wages. It does, on average. But for the minority of high-wage earners, the new payment is less than 100%; for the majority, it is much more.

On average, this fortunate 68% group will make +34% more thanks to the program. In other words, **these workers would be hit with a -34% cut in earnings if they returned to their former low-wage food and service jobs.** Many are and will resist doing so as those establishments try to re-open. Businesses could report recalcitrant workers to state agencies, which would force a cut-off of all benefits. That is hardly a recipe for a healthy work environment.

The sole bright spot in this catastrophe is that the program expires on July 31. Until then, **CARES likely ensures that unemployment, near 15% in April, will remain high and possibly even increase through early summer.** Democrats are now trying to extend the job-killing program through December, coincidentally after the president election.

There is evidence that the virus has not choked off demand for big-ticket items. **New mortgage applications have surged in recent weeks.** In the latest week, applications were down only -1½% vs.



year-ago results. In early April, they had collapsed -35% vs. the 2019 mark. Some of this new strength is payback from homebuyers and institutions that were paralyzed last month. Still, it shows that the “true” housing base is not that low; it too will likely pick up nicely by this summer.

Not everything is so rosy, of course. **Some sectors will be slower to recover**, e.g., restaurants and bars will operate under tight capacity constraints for months. International trade will take a while to reset. Some sectors, especially airlines, tourism and large-scale entertainment (sports, concerts, etc.) will be *very* slow.

Overall, **FMI is tracking -40% plunge in real GDP for 20Q2, followed by a +25% or so rebound in 20Q3**. That is not a pure “V” but is not chopped liver either. With continued momentum, we anticipate a new GDP peak by summer 2021.

V FOR VACCINES & VICTORY

Reinforcing our confidence has been the **steady stream of good news on the COVID-19 front**. States that are re-opening are seeing stable-to-downward rates of positive tests for the virus. The initial justification for the shutdowns was the need to free up hospital beds. When those beds remained empty, the new standard proffered was the need to bring down the rate of positive tests. Recalcitrant governors are running out of excuses to lift their restrictions.

Even the last possible requirement – “we need a vaccine first” – is looking more likely each day. More than 100 versions are in development; several have begun human trials and, so far, they have reported good news. These results are very early and a lot could yet go wrong. But the skepticism in the headlines is groundless: caveats about the Moderna vaccine, for example, revolve

around the true fact that though the results are strong, few have been posted yet. As even the critics admit, however, this is because results take time to analyze. No one has suggested, let alone proved, that the company is cherry-picking its data.

We also note that **even a partially effective vaccine would be a great stride forward**. Any vaccine – and we may well have several to choose from or use together – will be more effective on younger people and less effective for the elderly. For example, flu shots do practically nothing for those over age 75, the cohort most vulnerable to COVID-19. However, like the herd immunity from those who recover from the disease, the greater the number of young people who are vaccinated, the harder it will be for the virus to spread through society.

We should also credit the Trump administration, corporations, Bill Gates and several other governments for planning ahead, at least in one key area. Before the end of the year, maybe before the end of summer, **production and distribution systems will be in place to mass produce and deliver any vaccines that are proven safe and effective**. FMI has argued that simply the announcement of a vaccine would be a major boost to the economy and the markets by instilling confidence. The ability to deliver said vaccine fast is a considerable added benefit.

We do not believe that a vaccine is a necessary condition for a solid recovery. The public will not allow the last few governors to stall re-opening waiting for one. Better treatments, better control tactics (wearing masks, protecting nursing homes) and the herd immunity which happens with every virus will enable the world to manage this problem. Still, **a vaccine would be a great help. And it is looking more likely**.

A Vaccine Is Not a Necessary Condition for a Solid Recovery, But One Would Help a Lot. And Now Seems More Likely