



Covid 19 Response – Short and Long Run Implications

June 26th, 2020

- Covid 19 policy response in context
- Budget implications and other near term costs
- Will monetary and fiscal policy be inflationary?
- Capital market impact of Fed programs
- Long run implications



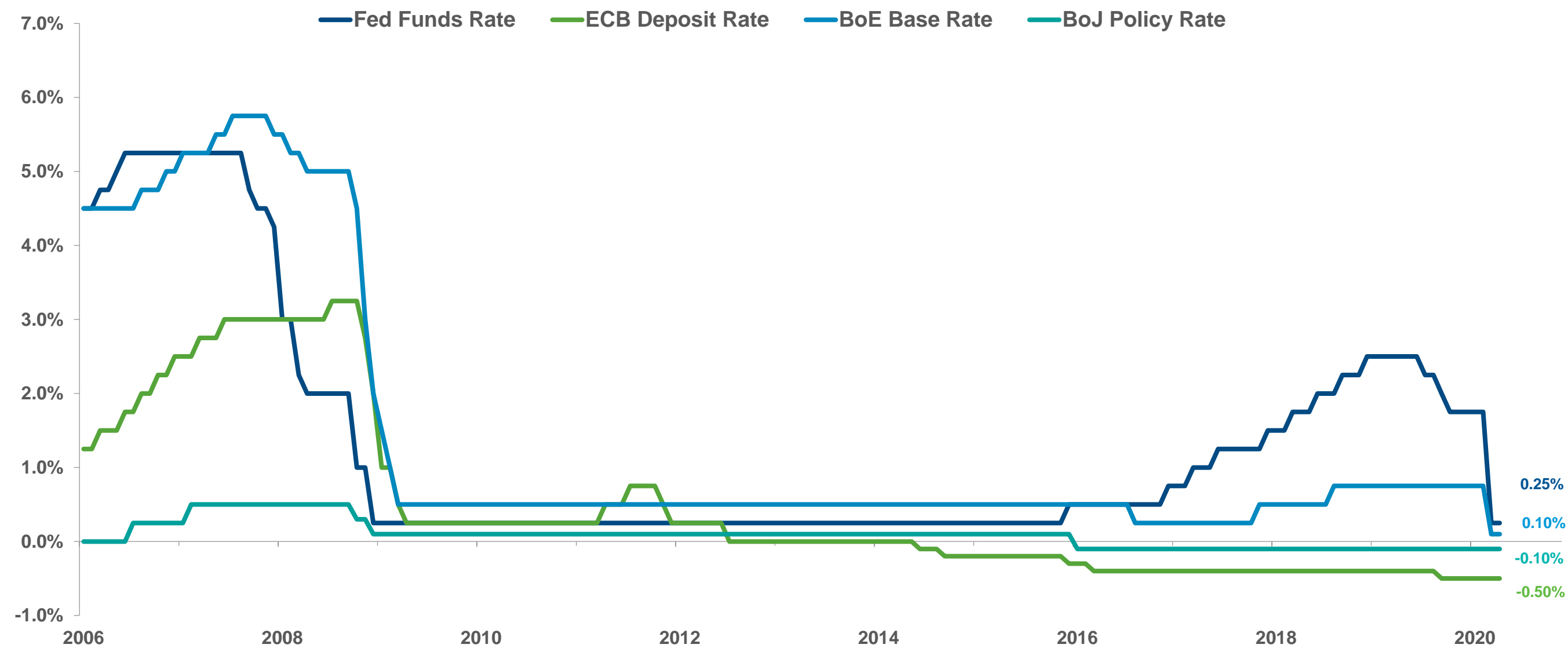
Covid 19 Policy Response- Go Big or Go Home

Policy Response – Firing the Big Guns



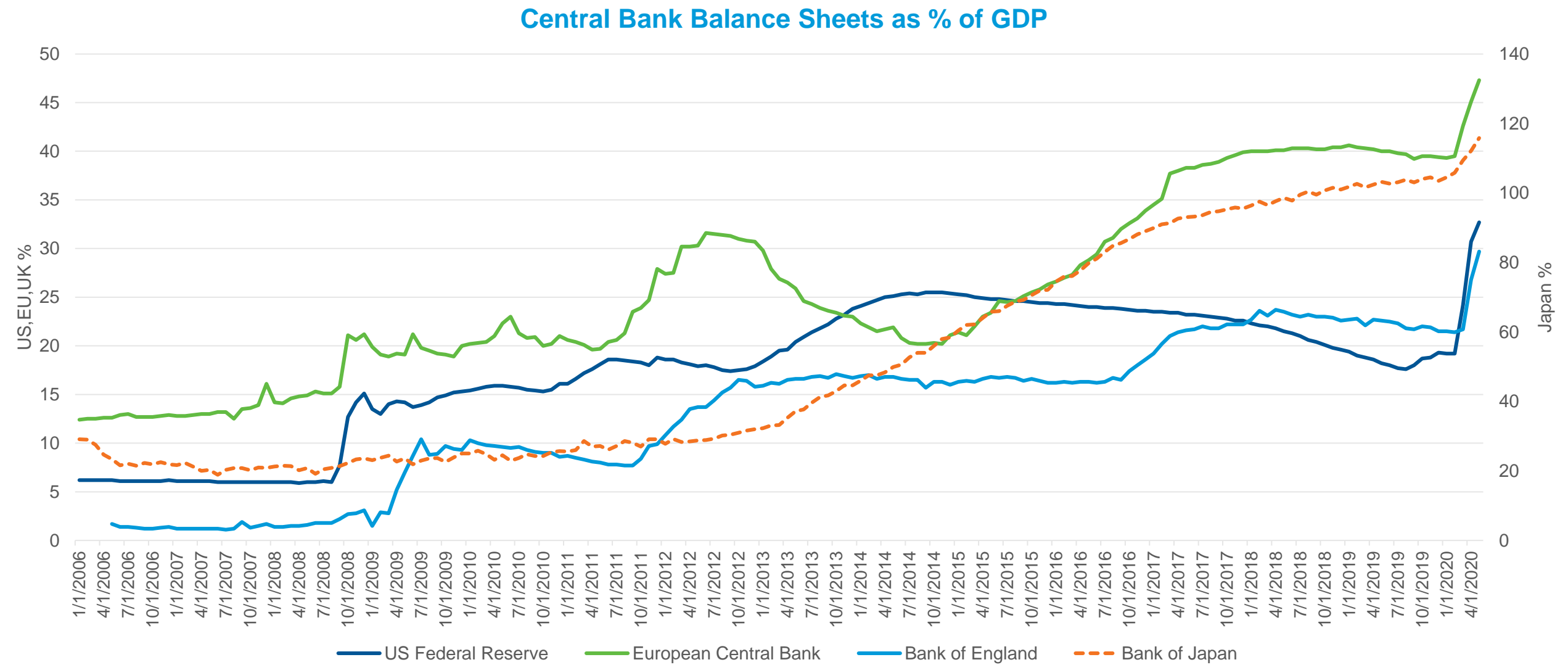
Photos of Mnuchin, Trump, Lagarde and Powell from Wikimedia Commons.

Policy Response – Monetary Policy – Interest Rates



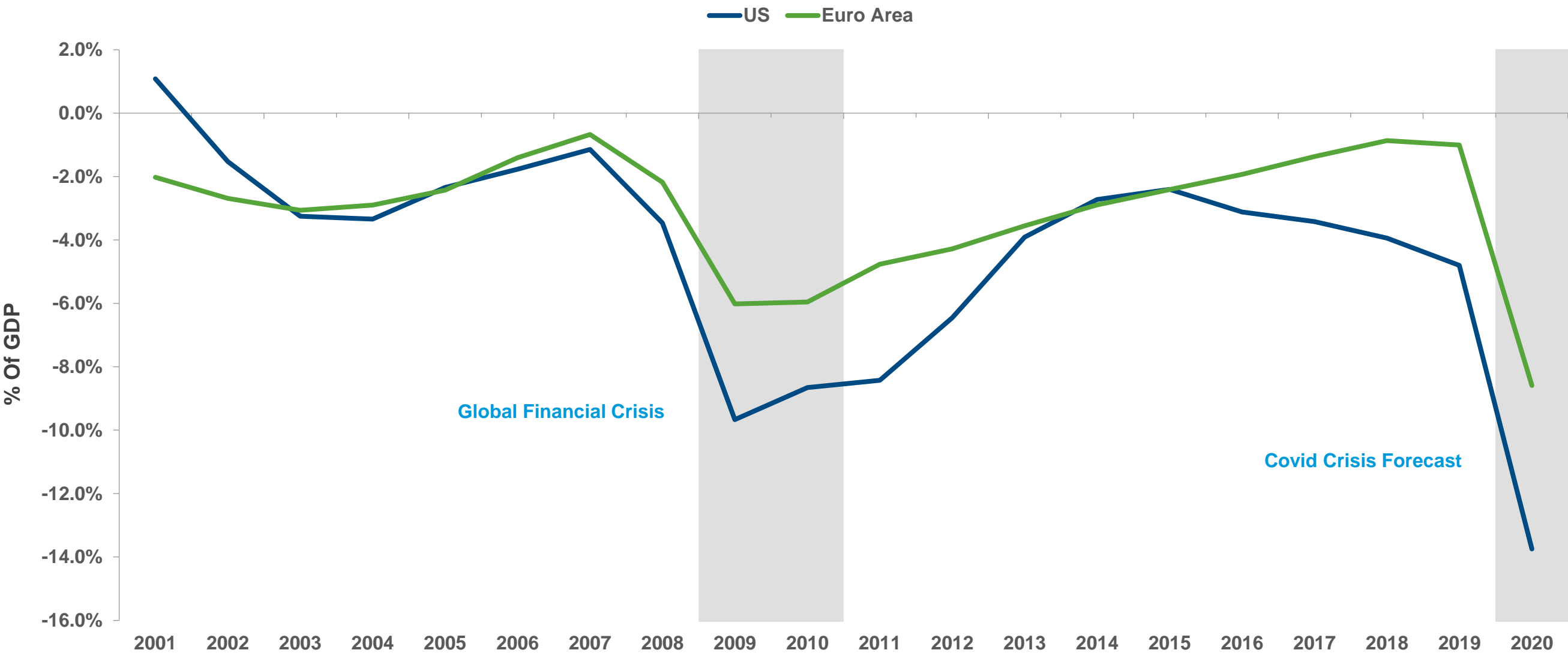
Source: Federal Reserve, European Central Bank, Bank of England, Bank of Japan, OANDA, NEAM

Policy Response – Monetary Policy - QE



Source: Federal Reserve, European Central Bank, NEAM

Policy Response – Fiscal Policy



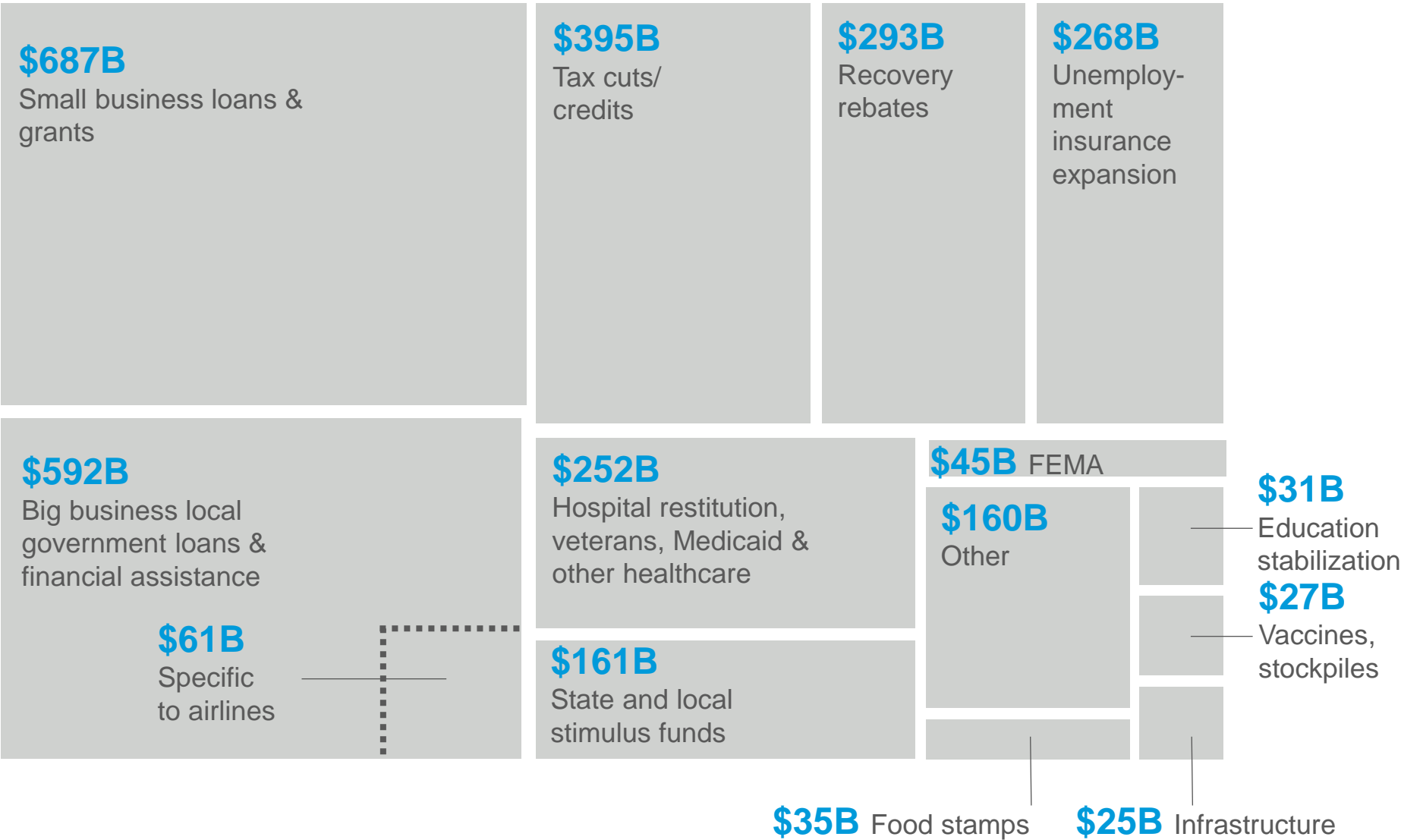
Source: Deutsche Bank, NEAM

U.S. Fiscal Response

Roughly \$3 Trillion (and Counting) in Rescue Funds



Where Nearly \$3 Trillion in Stimulus Funds Will Go



Sources: Congressional Budget Office, Committee for a Responsible Federal Budget

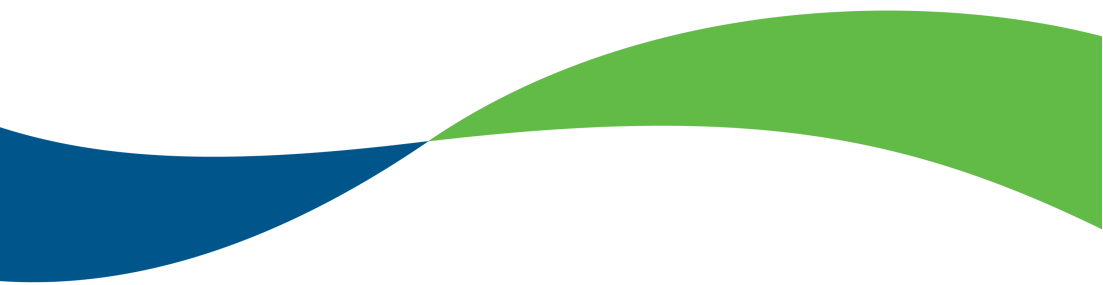
MASSIVE GLOBAL STIMULUS: U.S. 38% OF GDP, GLOBAL 21%.

| Global Monetary And Fiscal Stimulus To Fight COVID-19 Impact 2020 Feb to Apr (CSM) | | | | | | |
|---|----------------------------------|-------|----------------------|-------|---|-------|
| | Central Bank Liquidity Injection | | Govt Fiscal Stimulus | | Central Bank Liquidity Injection and Govt Fiscal Stimulus | |
| | \$ Tln | % GDP | \$ Tln | % GDP | \$ Tln | % GDP |
| U.S. | \$4.80 | 22.4% | \$3.30 | 15.4% | \$8.10 | 37.8% |
| Eurozone | \$1.10 | 8.3% | \$2.83 | 21.2% | \$3.93 | 29.5% |
| Japan | \$0.20 | 3.9% | \$0.99 | 19.2% | \$1.19 | 23.1% |
| U.K. | \$0.25 | 9.0% | \$0.14 | 5.1% | \$0.39 | 14.1% |
| China | \$1.44 | 10.0% | \$0.54 | 3.8% | \$1.98 | 13.8% |
| Others* | \$0.68 | | \$2.09 | | \$2.76 | |
| Global | \$8.46 | 9.8% | \$9.88 | 11.4% | \$18.35 | 21.2% |

Record Amount Of U.S. Monetary & Fiscal Stimulus.

*incl ROW and AOE, BAE, WOE

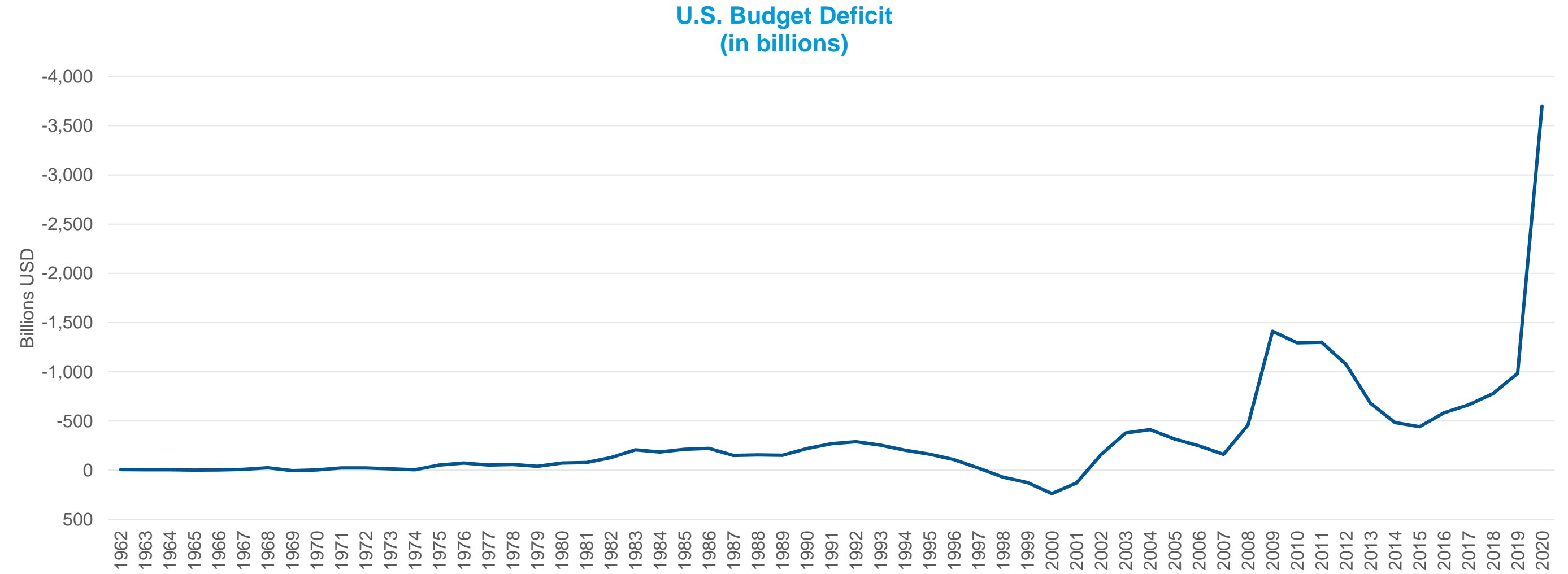
Source: CSM



Near Term Costs

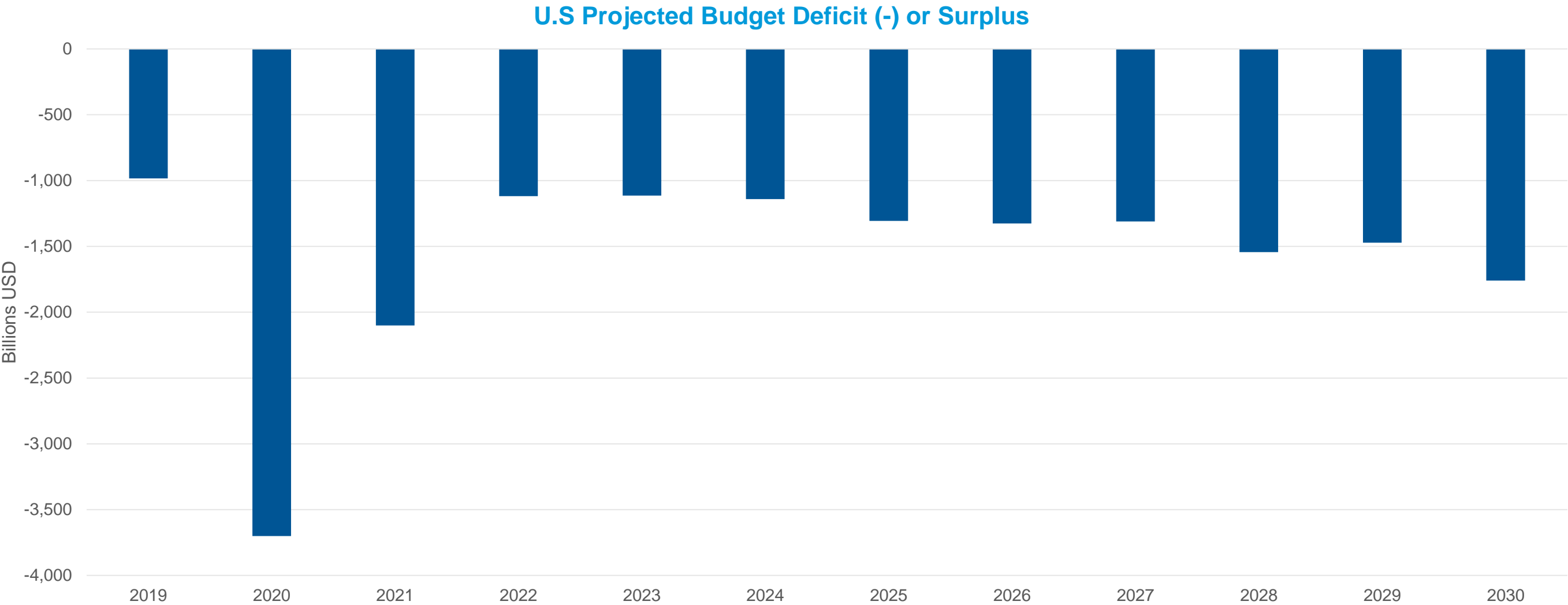
U.S Budget Deficit

Estimated at \$3.7 Trillion for 2020



Source: Congressional Budget Office, NEAM

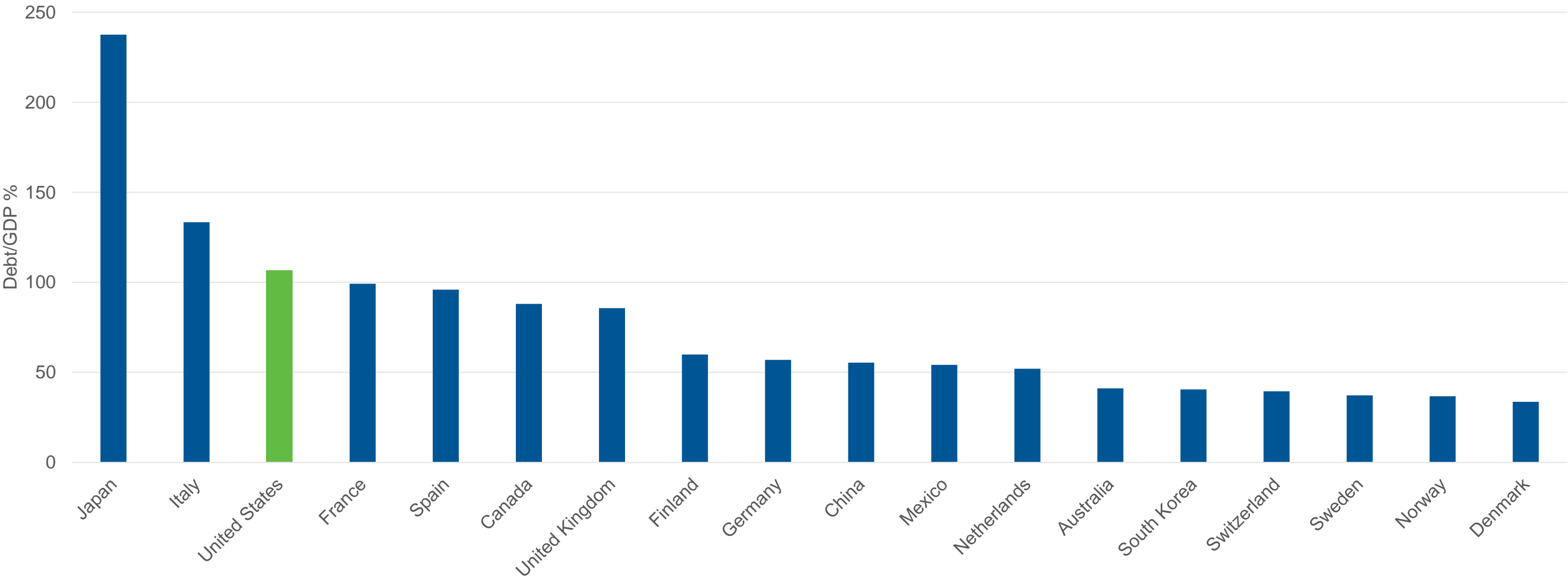
Budget Deficits as Far as the Eye Can See



Source: Congressional Budget Office, NEAM

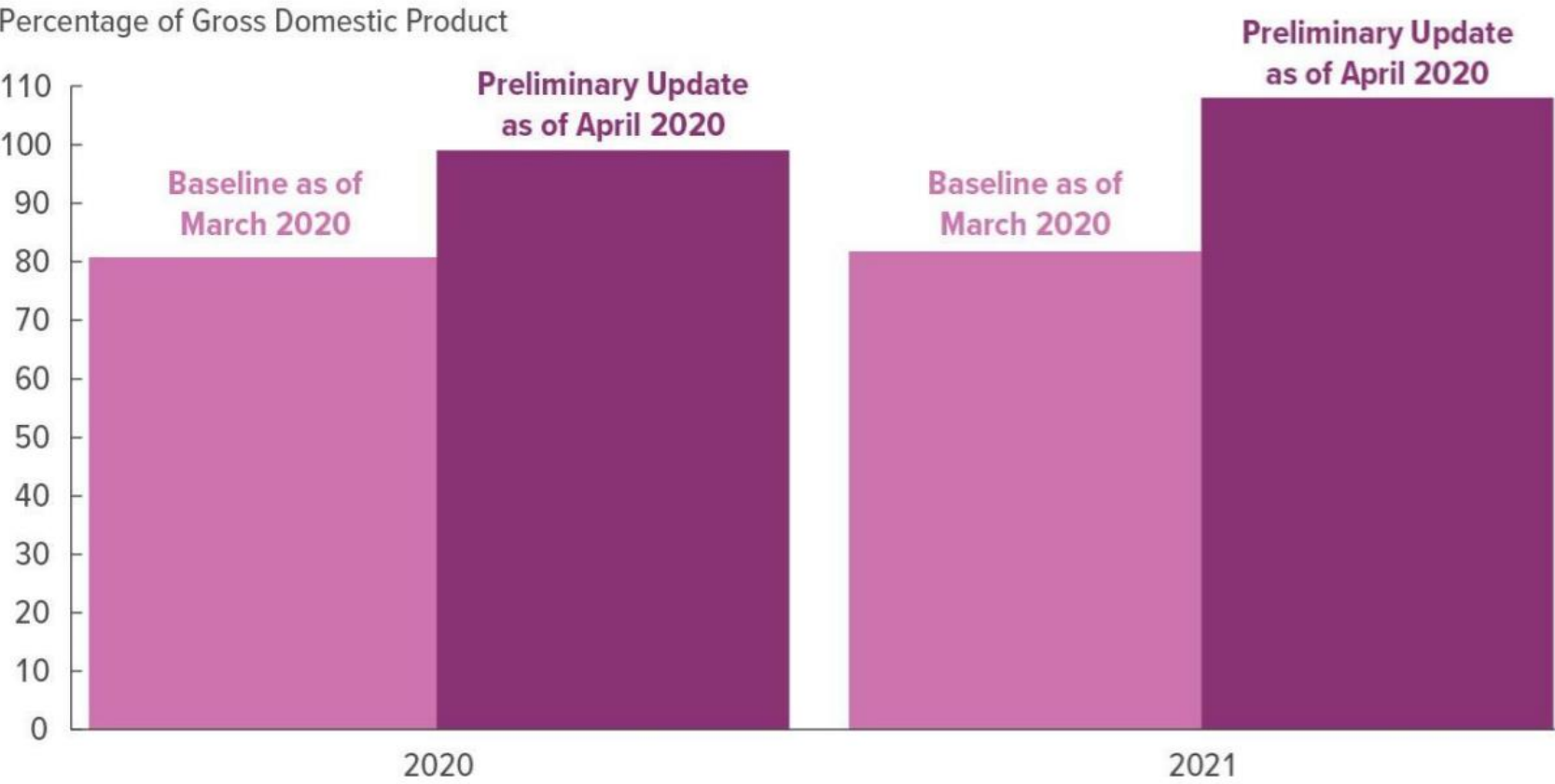
Debt vs GDP by Country

Total Sovereign Debt vs. GDP



Source: Worldpopulationreview.com

Federal Debt Held by the Public



CBO projects that federal debt held by the public would grow to 108 percent of GDP by the end of fiscal year 2021, up from 79 percent at the end of fiscal year 2019—again, if current laws generally did not change. That percentage in 2021 would be the highest in U.S. history.

Source: Congressional Budget Office

The background features two large, overlapping, wavy shapes. The shape on the left is dark blue and tapers towards the center. The shape on the right is green and starts from the center, extending to the right edge. They meet at a point in the middle of the slide.

**Will Enormous Policy
Response Cause
Inflation?**

Answer...It Depends on What Kind of Inflation

- General Price Inflation (CPI)
 - Short to intermediate term – **NO**
 - Longer Term (3 years +) – **Possible** , more likely with “structural” changes
- Financial Asset Inflation
 - Short to intermediate term – **Absolutely**
 - Longer Term (3 years +) - **Absolutely**

Year Over Year Change in Consumer Price Index

- Average 1930-Current 3.1%
- 1960-1994 4.8%
- 1995-2008 2.7%
- 2009-2020 1.6%
- Fed Target 2.0% sustained

Source: Bureau of Labor Statistics

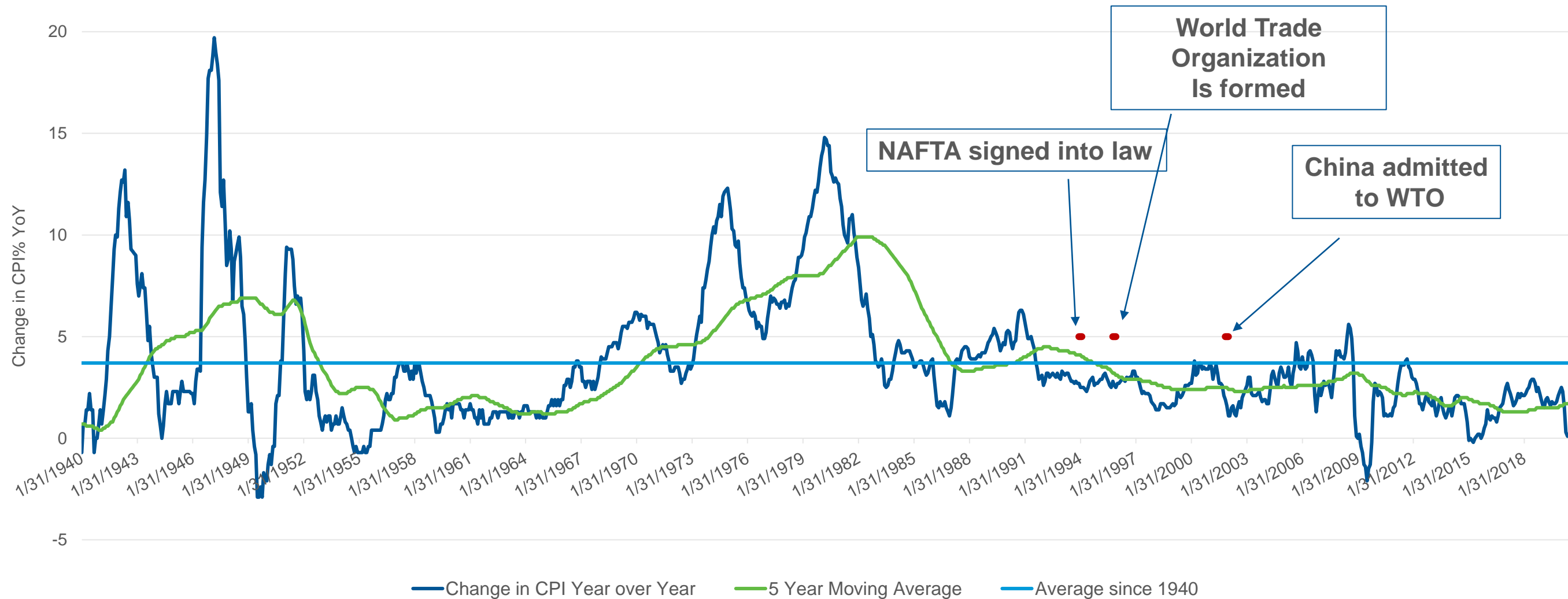
- Demographics
 - Aging populations consume less
- High Debt Levels
 - Higher Debt levels “crowd out” other beneficial spending
- Globalization
 - For the last 25 years, globalization of supply chains and labor has driven down costs
- Income/Wealth Disparities
 - Each dollar of income and wealth has a lower economic “multiplier” as one moves up the income spectrum



Globalization Has Exerted Downward Pressure On Consumer Prices



Price Inflation as Measured by CPI



Source: Bureau of Labor Statistics; NEAM

The Pandemic Will Likely Disrupt the Status Quo



Mind the Gap....

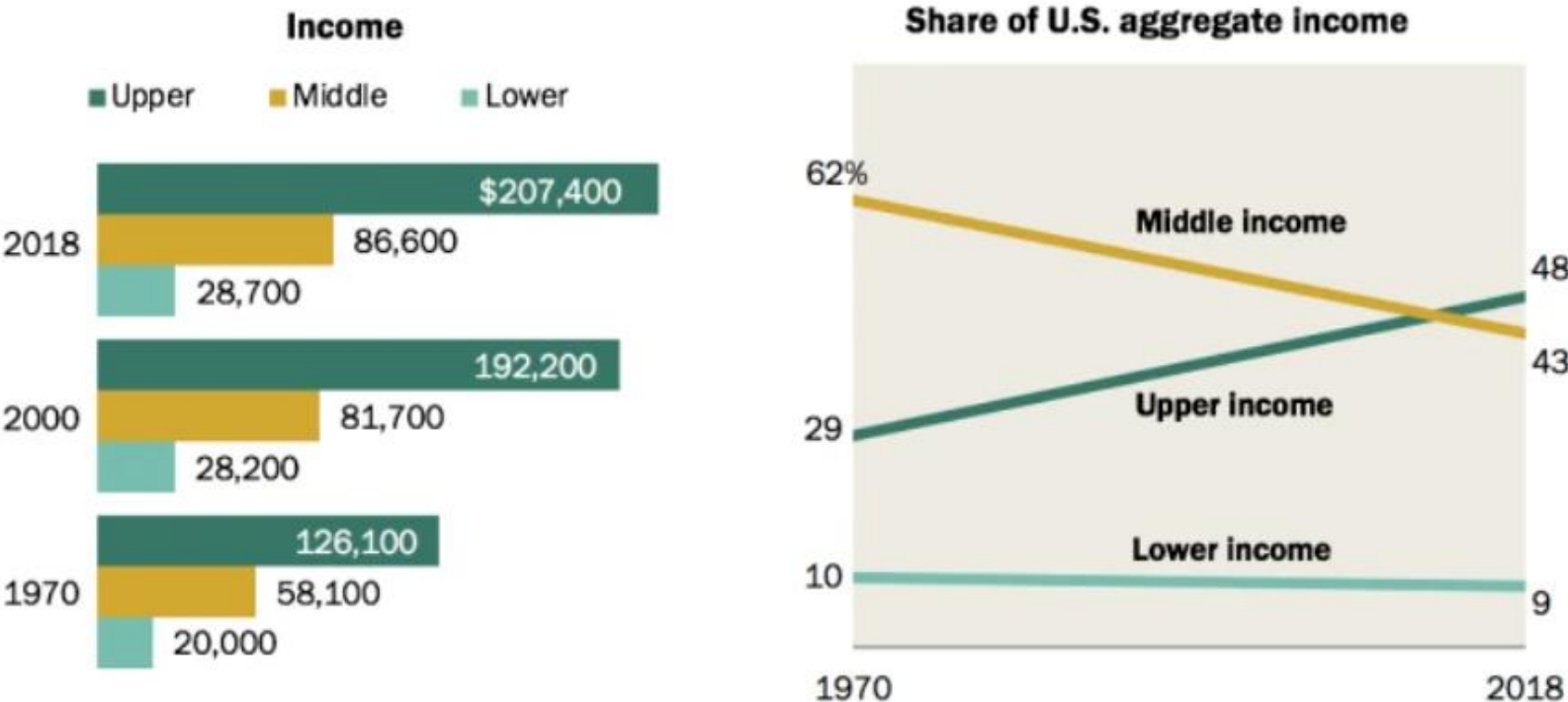
Income and Wealth Metrics are Disinflationary



Wider Income Gaps Hurt Consumption and End Demand

The gaps in income between upper-income and middle- and lower-income households are rising, and the share held by middle-income households is falling

Median household income, in 2018 dollars, and share of U.S. aggregate household income, by income tier



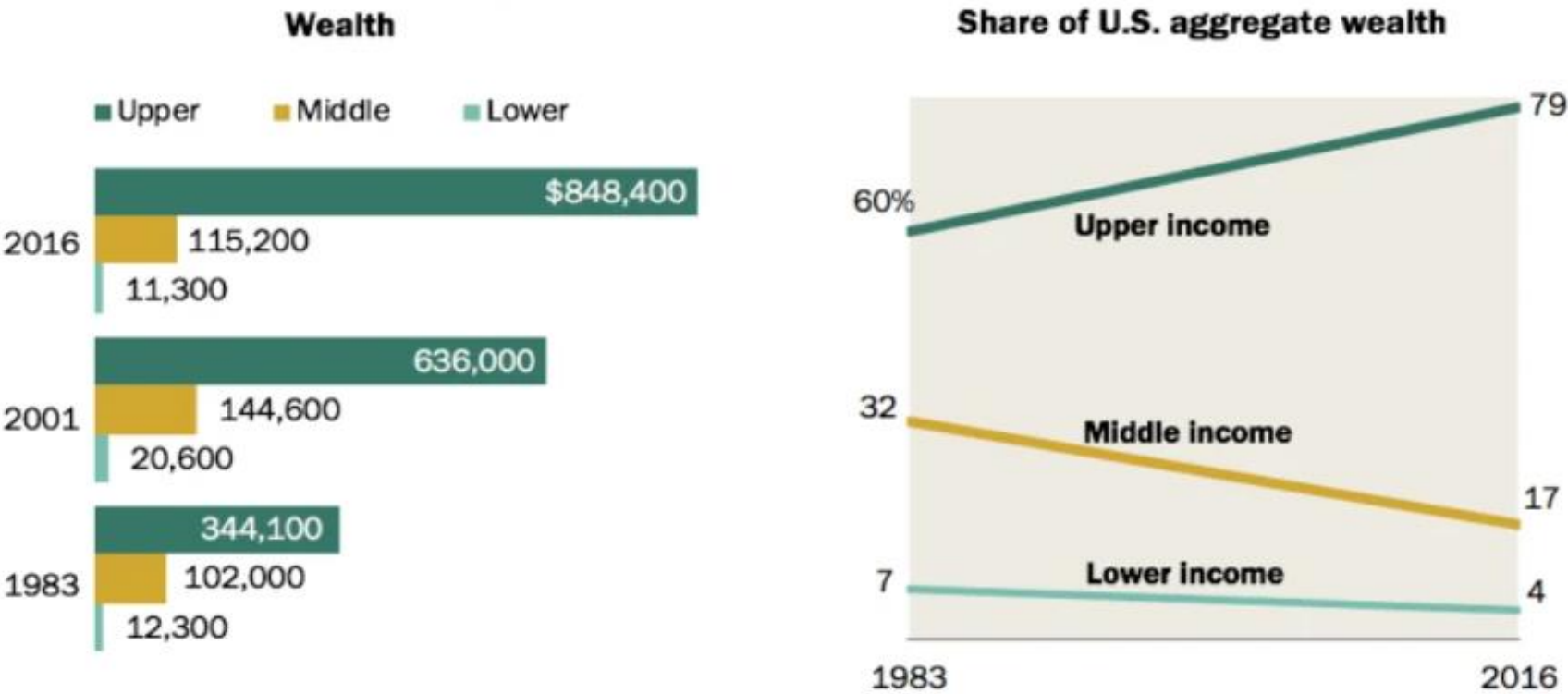
Note: Households are assigned to income tiers based on their size-adjusted income. Incomes are scaled to reflect a three-person household. Revisions to the Current Population Survey affect the comparison of income data from 2014 onwards. See Methodology for details.
Source: Pew Research Center analysis of the Current Population Survey, Annual Social and Economic Supplements (IPUMS).
"Most Americans Say There Is Too Much Economic Inequality in the U.S., but Fewer Than Half Call It a Top Priority"

Source: Pew Research Foundation

Wealth Metrics Tell an Even More Extreme Story

The gaps in wealth between upper-income and middle- and lower-income families are rising, and the share held by middle-income families is falling

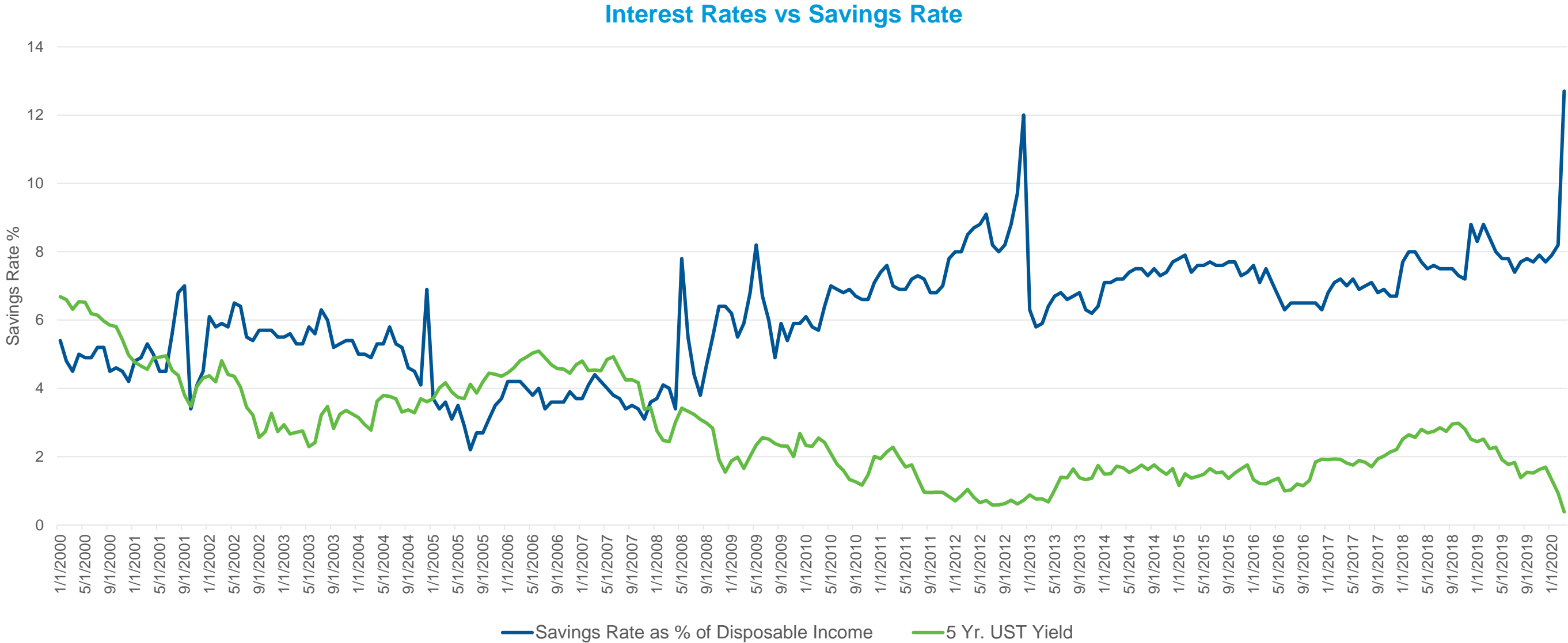
Median family wealth, in 2018 dollars, and share of U.S. aggregate family wealth, by income tier



Note: Families are assigned to income tiers based on their size-adjusted income.
Source: Pew Research Center analysis of the Survey of Consumer Finances.
“Most Americans Say There Is Too Much Economic Inequality in the U.S., but Fewer Than Half Call It a Top Priority”

Source: Pew Research Foundation

As Interest Rates Plummet, Savings Rates Rise



Source: Bloomberg; NEAM

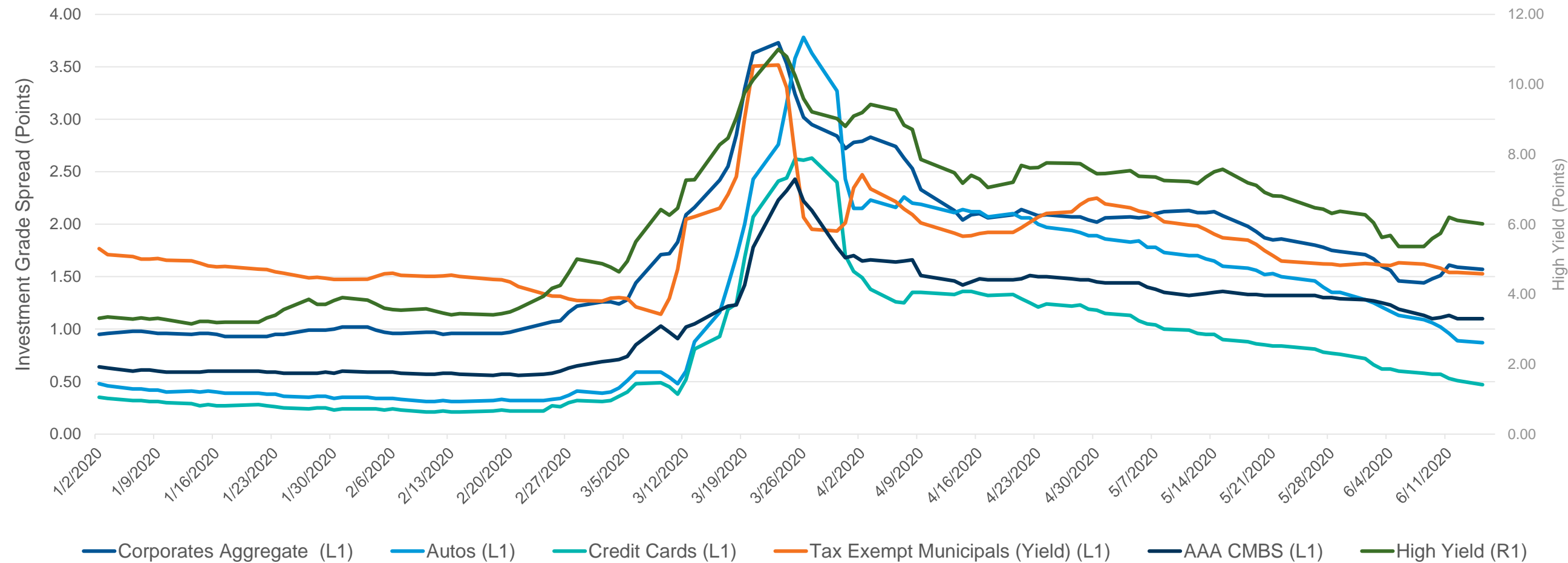


Covid 19 Rescue - Capital Markets Impact

U.S. Fixed Income Credit Spreads



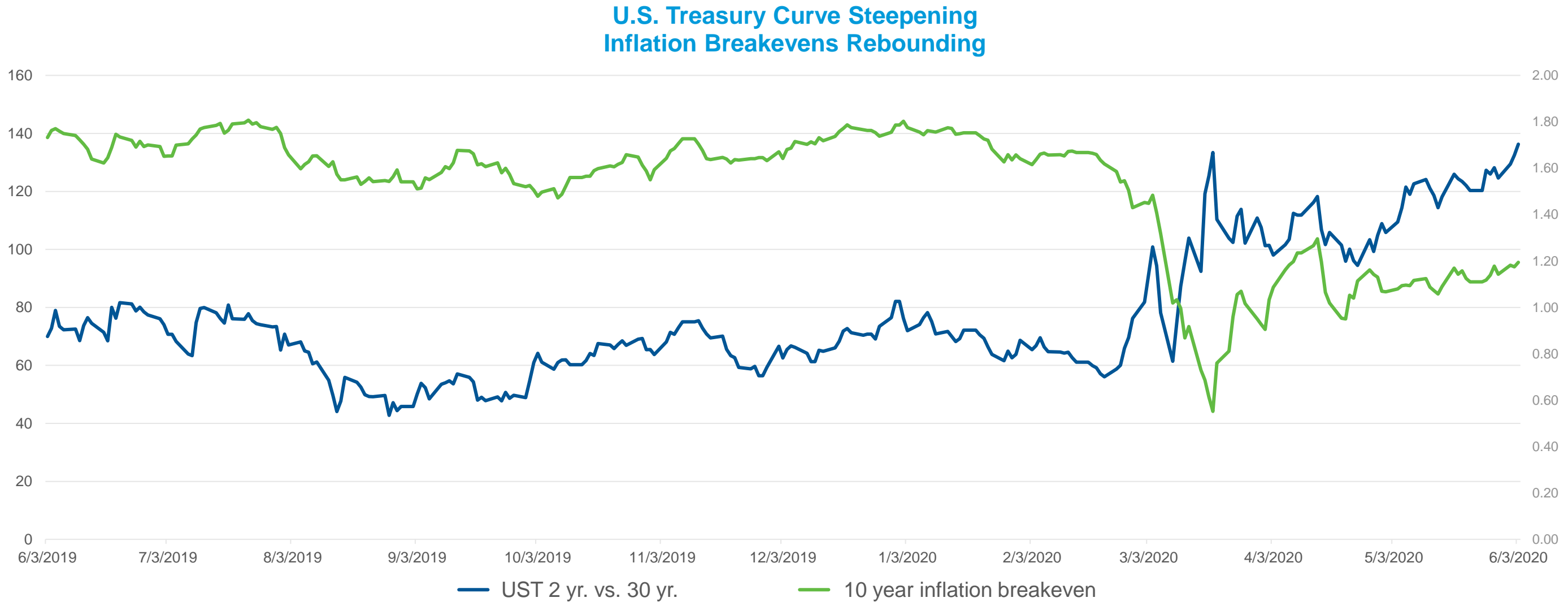
U.S. Fixed Income Spreads
YTD 2020



Source: Bloomberg Barclays Indices; NEAM

Long Rates are Rising, Curve is Steepening

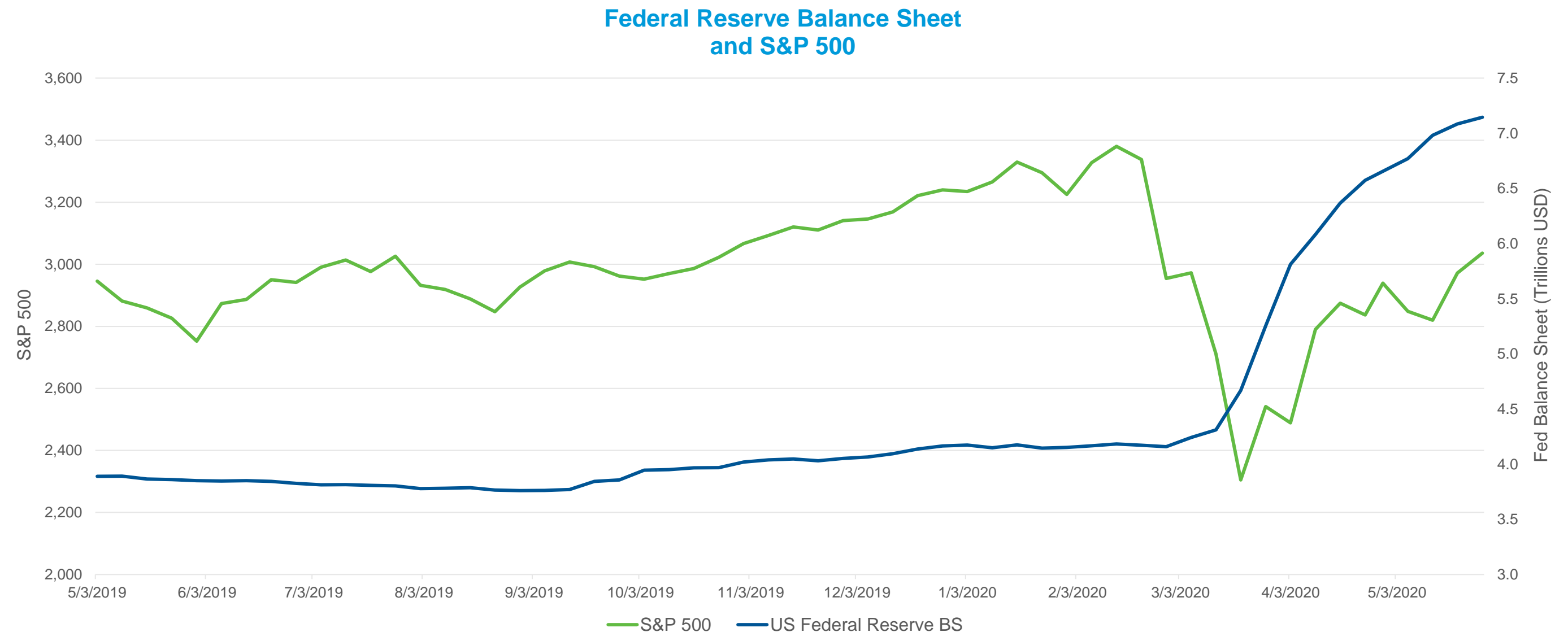
Inflation Breakevens Back Above 1%



Source: Bloomberg; NEAM

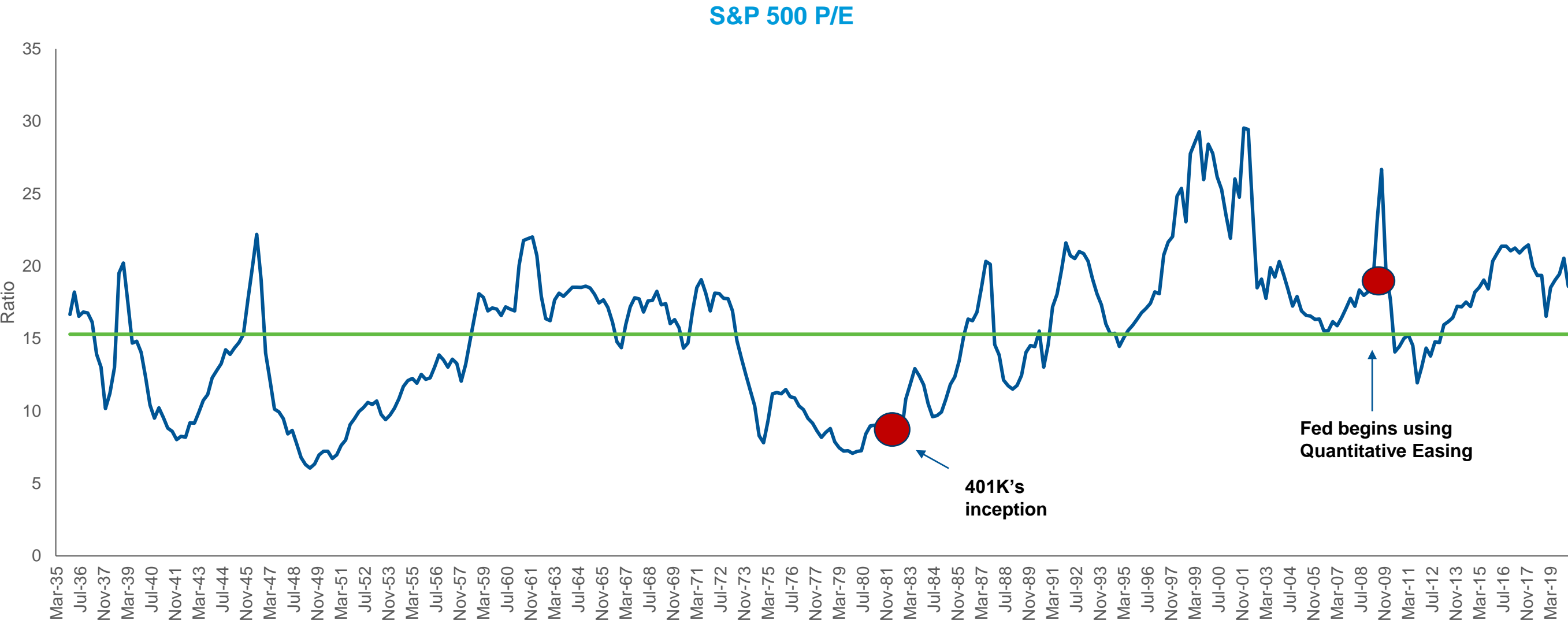
Fed Balance Sheet Has Exploded

Stock Investors Riding the Wave, But Will The Rally Be Durable?



Source: U.S. Federal Reserve; Standard & Poors; NEAM

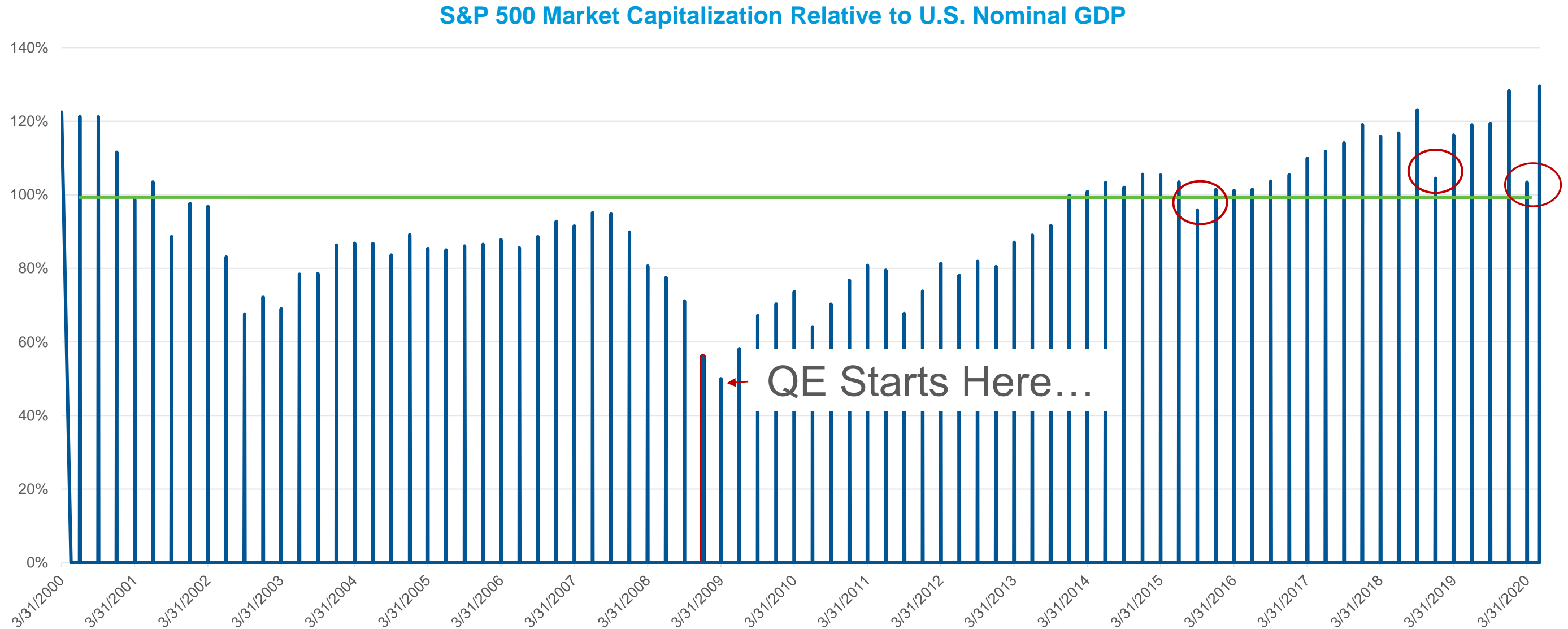
S&P 500 Price to Earnings



Source: Haver Analytics; NEAM

Bottom Fishing No Longer Allowed

Signed, the Fed



Source: Bureau of Economic Analysis; Bloomberg; NEAM

QE Infinity – There’s No Way Out



Total Central Bank Assets
as a Percentage of Equity Market Capitalization

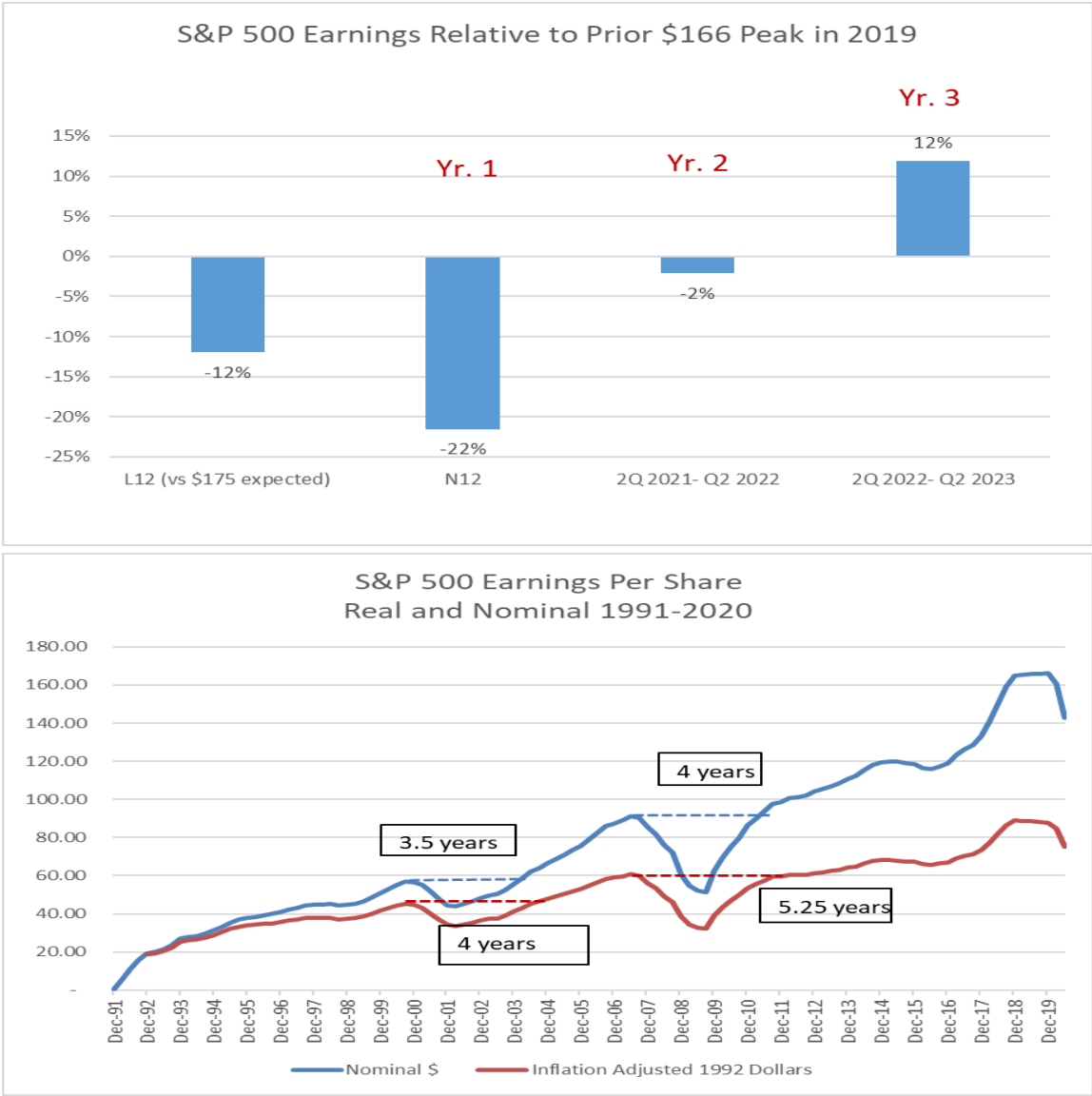
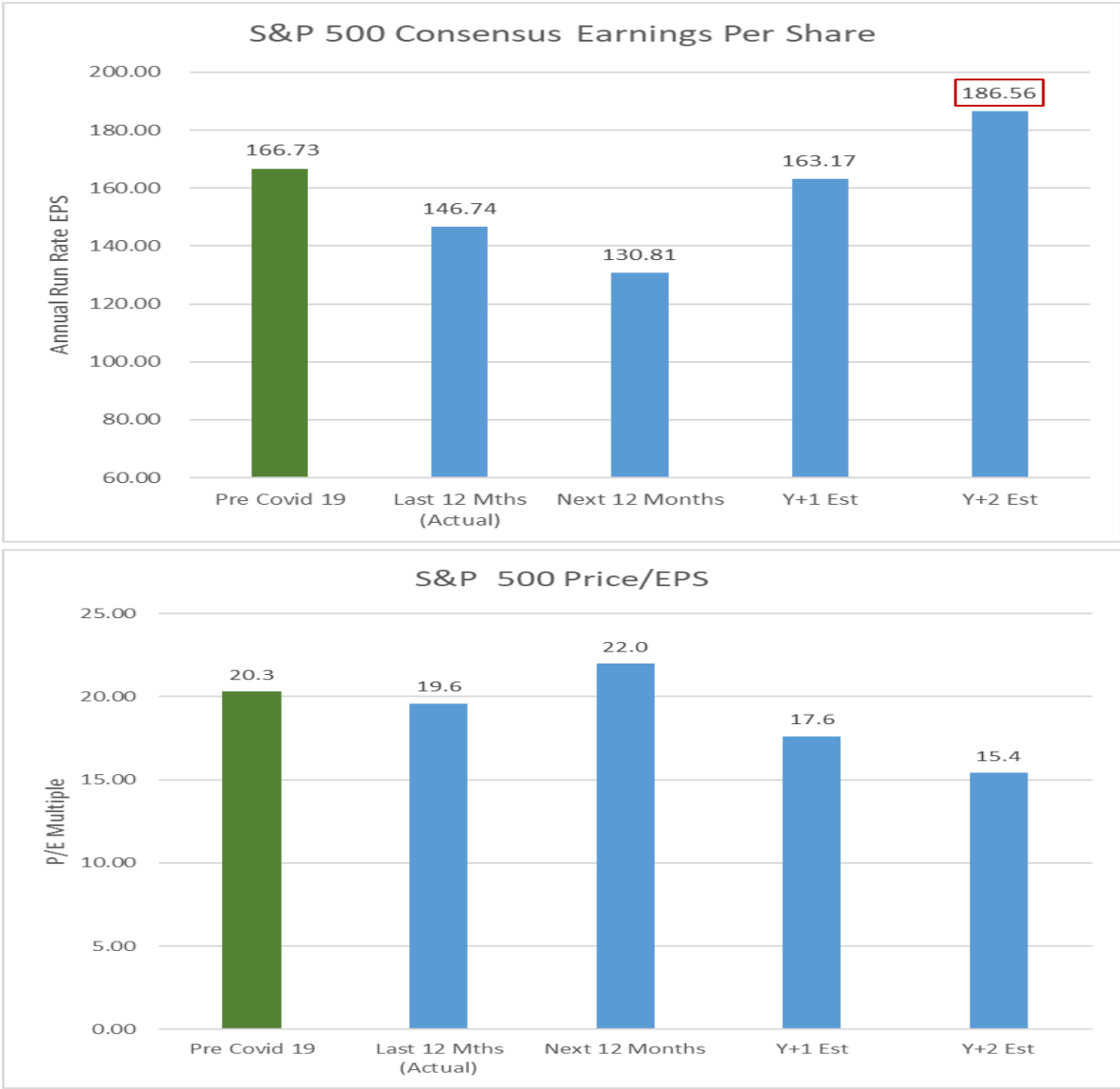


Source: U.S. Federal Reserve; European Central Bank; BoJ; Bloomberg; NEAM

Are Equity Markets Too Optimistic?

History Implies the Answer is Probably “Yes” BUT if a PE of 20X is the New 15X, then the Answer Might be NO





Source: Bloomberg; S&P; NEAM

The background features two large, flowing, wavy shapes. A dark blue shape enters from the left side, curving upwards and to the right. A green shape enters from the top right, curving downwards and to the left. The two shapes meet in the center of the frame, creating a point of intersection.

What's Next?

Defaults and Bankruptcies Are Rising

J.CREW

Hertz

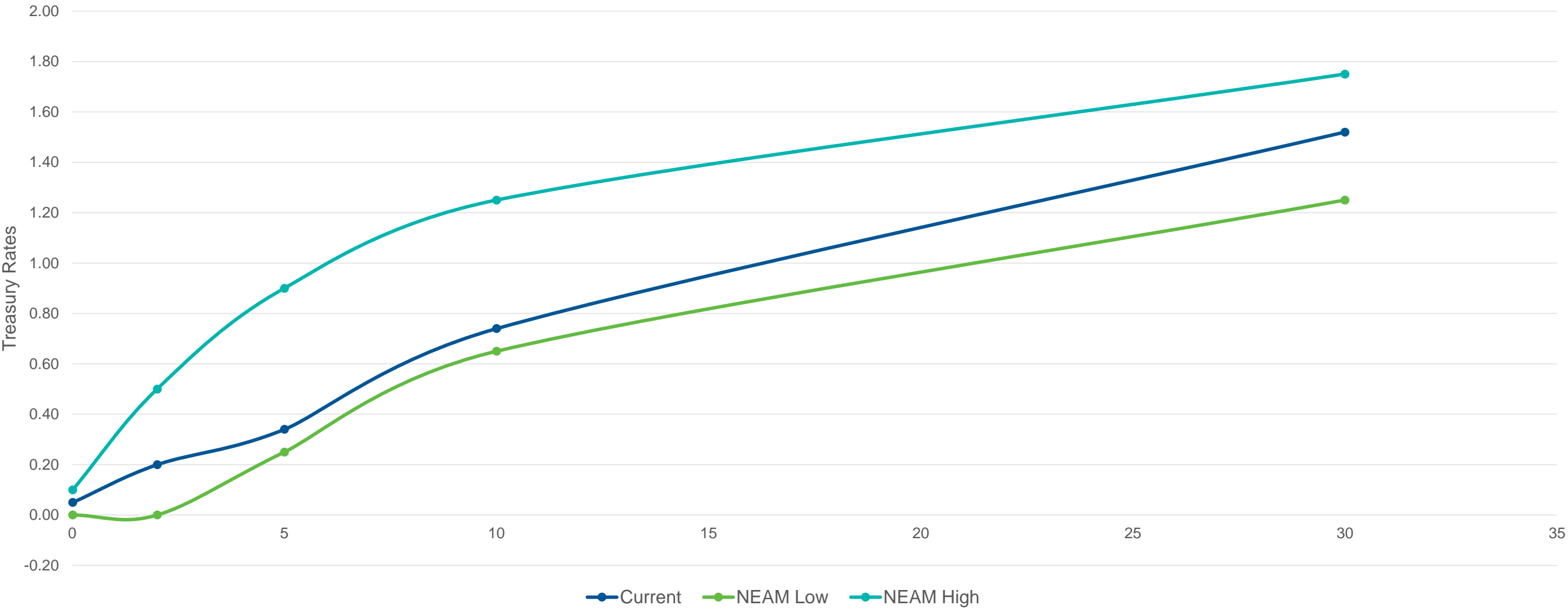
JCPenney

- Bankruptcies
- Restructurings
- Mergers
- Spin offs
- Roll ups
- Divestitures

Interest Rates Will Remain Exceptionally Low



U.S. Treasury Rate Forecast Year End 2020



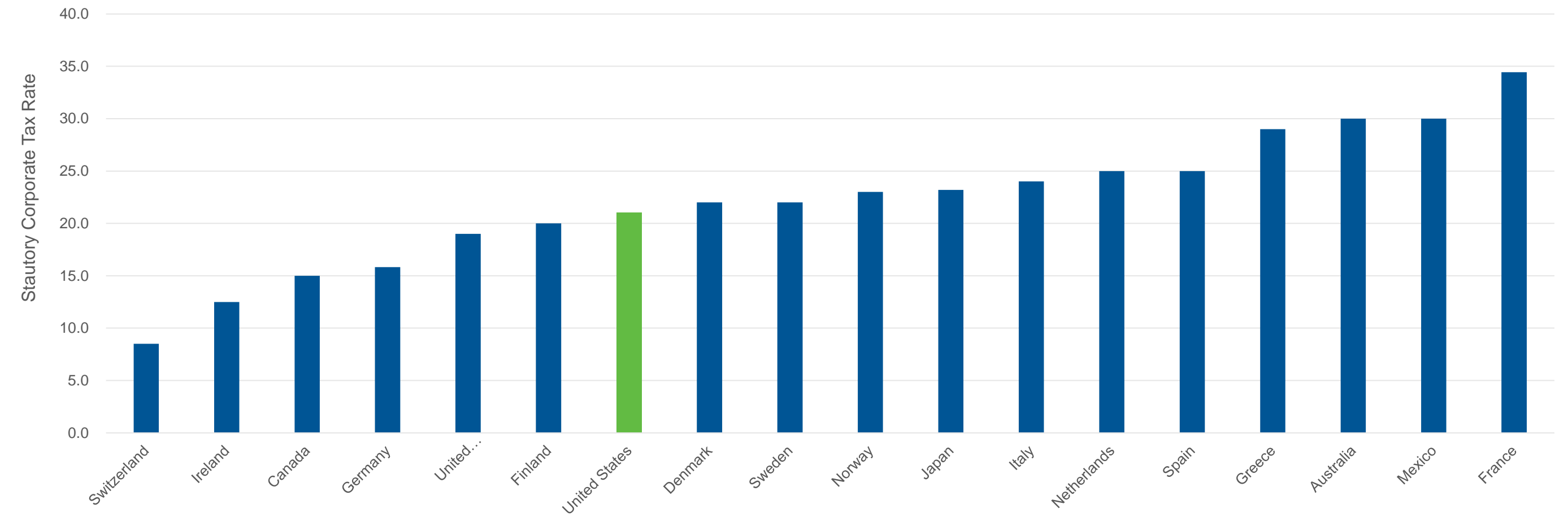
Source: Bloomberg, NEAM

Tax Rates Likely to Rise in the Future

Budget Deficits Will Need to Be Paid for Eventually



Statutory Corporate Tax Rates
Select OECD Countries



Source: Organization for Economic Cooperation and Development (OECD)

Longer Term Considerations for Investors

- Potential for Higher Savings Rates vis a vis Consumption
- Larger Fiscal Deficits/ Sovereign Debt Levels
 - Weaker U.S. Dollar could spark inflation in the longer term
- Higher Tax Rates
 - Corporations have been massive beneficiaries of Fed's credit programs
- Supply Chain Re-ordering / Peak Globalization
- “Not-So-Free Markets” Featuring Low Interest Rates and Tight Credit Spreads
 - Central bankers with their thumbs on the scale
- Changes in Consumer and Company Behavior

The background features two large, smooth, wavy shapes. A blue shape enters from the left side, curving upwards and to the right. A green shape enters from the right side, curving upwards and to the left. They meet in the center, creating a symmetrical, wave-like pattern.

Thank You