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UPDATED U.S. ECONOMIC OUTLOOK:

Delayed Stimulus Ramifications on Economic Recovery Expectations

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By Andrew Duguay, Chief Economist

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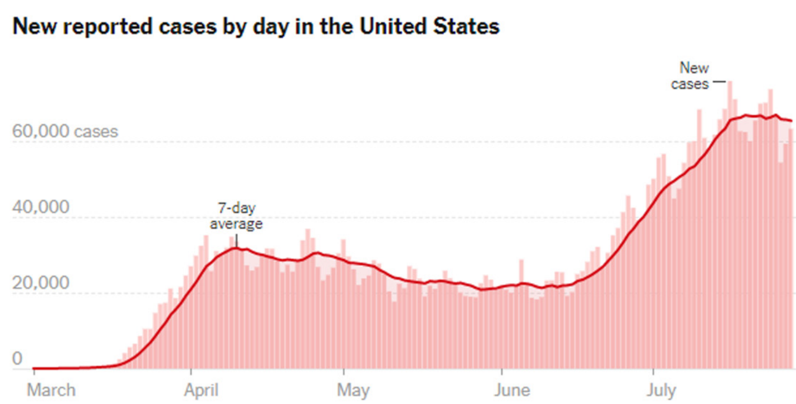
It's most likely a low probability that benefits and stimulus will expire without any extension or revision. However, a couple of different options are getting weighed in Congress. This report discusses how they fit into the overall economic picture for the second half of the year as we look towards the future.

Recovery starts when the U.S. can control the pandemic. The pandemic is the essential cause of this global economic crisis. If we can't get over the pandemic, we can't get one foot forward into the economic recovery in earnest.

We can do certain things as an economy from federal fiscal policy to remediate specific ailments that the economy is facing in the near term. But a long-term, sustainable recovery is not possible without a safe and healthy economic environment from which to do business.

When it comes to the number of COVID-19 cases, it's been largely negative news for the United States. Unlike many other countries controlling the pandemic, U.S. cases have been on the rise, which is not news to anyone. However, looking at a seven-day moving average smooths out some of that daily volatility.

As of July 29th



New York Times

The U.S. may have reached the second plateau, but it's much higher than the first plateau back in April when thought perhaps the worst was over. But here we are again, looking forward to cases declining and thinking about how to reopen safely while hopefully not reopening too soon.

Lessons may have been learned the hard way in some areas about reopening. It appears that you can face more economic pain by trying to be too aggressive with those actions than not, and this backdrop impacts the outlook.

It's hard to forecast the likely scenario for economic recovery regardless of stimulus if the pandemic crisis does not subside. This isn't just a U.S. phenomenon. Cases are rising in India, Brazil, and other emerging markets, impacting economic growth in those areas. While we're focusing mainly on the U.S. economy, it's not necessarily a U.S. isolated issue.

Next Steps in Recovery

As for how to mediate the next steps, Congress is negotiating another stimulus package. Part of this will extend the $600 a week federal unemployment top-up, which the U.S. economy has grown to rely on quite heavily. This additional unemployment is becoming a significant part of the U.S. economic engine when it comes to people's spending, paying their mortgage, or making ends meet.

The stakes are high. About 15% of total wages are relying on this additional unemployment. U.S. jobless claims are at 25 million+ people, a large number for comparison's sake, and we remain at over a million new jobless claims every month. This scenario continues to play out several months after the pandemic forced the economic shutdown.

At the peak of the Great Recession in 2008/2009, jobless claims never surpassed 675,000 in a given week. Comparatively, at the end of July 2020, jobless claims were at about 1.4 million for the last week. The timing of expiring unemployment benefits could not be worse. The newest jobless claims were the first increase since the peak after the initial shutdown of the economy in April.

The impact of the fading of the stimulus on the unemployment benefits is of deep concern. In response, reactions from both the Republicans and the Democrats seem to be a range of options. Both are proposing between $1 and $3 trillion for the next stimulus package.

Looking at the previous Great Recession, the American Recovery and Reinvestment Act stimulus package didn't even reach a trillion dollars. The top-up we're talking about now, the extended stimulus package, will be over a trillion dollars on top of the nearly 2 trillion that was passed a few months ago with the CARES Act. These are unprecedented aggressive levels of stimulus in this recession, bringing comfort for those who have lost their jobs.

Extending Benefits for Extenuating Circumstances

Regardless of the package that gets passed, the context of the federal response will be by historic standards much more aggressive than anything we've seen in history. Why does this matter for the near term?

Some have criticized previous stimulus actions because they are concerned about increasing federal government debt. They think consumers are fearful for their safety and, as such, save the money rather than spend it to stimulate the economy. In times of crisis, people do what seems logical, and they keep it for a rainy day.

Unfortunately, this doesn't necessarily boost spending, retail sales, or help the economy in any tangible, immediate way. However, with this extra $600 a week in unemployment benefits, we see that people who have lost jobs are spending it.

The benefits are covering ongoing expenses such as rent and groceries. The $600 a week has been more than a replacement for over 50% of those unemployed, increasing their wages versus just covering part of the salaries they were earning on average before they lost their job. In many cases, the unemployed actually have more money to spend and are in a better financial situation than before their job loss.

Studies show that those who have received higher unemployment benefits are increasing their spending. This helps offset consumers continuing to work, who have spent more conservatively, and who have increased their savings rates in fear of a crisis.

JPMorgan Chase did a case study of two different control environments. They compared the newly unemployed who are changing spending overtime to those who have not lost their jobs since COVID happened. It showed that those who are recently unemployed and therefore getting the new generous unemployment benefits had increased their spending by about 10%. Meanwhile, those who have had no employment change have become more conservative, as expected during a recession, and decreased their spending by 10%.

This is an interesting and perhaps, worrying trend. Not only are individuals placed in a financially precarious position by not extending extra unemployment benefits, but the economy as a whole will experience negative ramifications related to total retail spending. The result could be adverse effects on many jobs, many businesses, and many industries.

Impact of Unemployment Benefits

From an economics standpoint, there are two significant ways in which the extension or expiration of additional unemployment benefits impacts recovery.

One, if consumers no longer have this money, economic crisis numbers will increase. The economy will be in a more challenging spot in terms of GDP growth, and the like, for the second half of the year.

Two, benefits will most likely continue in one shape or another. You might see an adjustment towards income. Many European countries have successfully come through this crisis with similar policies tied to some percentage of pre-COVID income. That's a reasonable response as well, rather than a flat number.

The U.S. policy settled on a flat number for the first round of stimulus for logistic reasons to get the unemployment benefits out quickly. Economically it may not have made complete sense because some people ended up receiving more than what they were earning when working, creating some disincentives.

Assuming a new stimulus package passes, how will the second half of the year look? It's still a slog. There are many uphill battles to face in the U.S. and around the world.

Historically, it takes four to five times as long to get jobs back then jobs were lost in any crisis. Whether it's due to a pandemic, financial crisis, or a stock market bubble burst, new jobs tend to take longer to create than old jobs tend to get lost. We need to be thinking about this even though we saw sharp declines in April, followed by rapid increases in May, June, and July.

While these economic indicators might look like a V-shape recovery, it's more likely to be choppy and W-shaped, filled with micro-recessions and micro-recoveries.

Looking to the Future

Many companies are looking towards the second half of 2020 and 2021, thinking about their annual operating plans. This is the time of year when planning becomes intensely real. There has been no more challenging of a year to create yearly operating plans than 2020 because of all this uncertainty.

Businesses should think about their annual operating plans in terms of coming up with fact-based, data-driven scenarios, considering how they can adapt those scenarios as new information comes available. Creating a plan today for the next year or 18 months is called agile planning or continuous planning.

Plans built now are almost guaranteed to be wrong in some way because there are so many unknowns. Part of proper planning means to adapt and change your plan continually, taking into account new datasets that are rapid release, coming out on daily or weekly frequency. Making use of this data provides the intelligence companies need to adapt plans and nudge them in one direction or another. It will allow a continuous planning process so that companies aren't locking in numbers and then finding a few months later that the target needs to move, but the business can't move along with it.

Agile planning involves scenario planning, which includes creating an economic baseline that considers some high and low scenarios about what's reasonably going to happen and have the company march towards that. This type of planning will be an essential part of the annual operating plan over the next year. Many businesses right now are starting to think about how to formulate 2021 strategies. An essential aspect of planning is adapting those plans and pivot accordingly as new information is coming out daily.

Economic Scenario Planning in a COVID-19 World

Planning and forecasting based on historical performance is no longer valid in today's economic climate. As you look ahead beyond the immediate crisis and consider your business plans, having visibility to external economic factors and considering how your company will fare in the "new normal" economy is paramount. This is what we call Intelligent Forecasting.

Prevedere helps companies answer, "what's next?", using global data and AI technology. Whether it is a black swan event like the COVID-19 pandemic, less severe shocks like falling oil prices, or the regular contraction-expansion business cycles, Prevedere provides executives with insights on global forces impacting their business.

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About Andrew Duguay

Mr. Duguay is a Chief Economist for Prevedere, a predictive analytics company that helps provides business leaders a real-time insight into their company's future performance. Prior to his role at Prevedere, Andrew was a Senior Economist at ITR Economics. Andrew's commentary and expertise have been featured in NPR, Reuters, and other publications. Andrew has an MBA and a degree in Economics. He has received a Certificate in Professional Forecasting from the Institute for Business Forecasting and Certificates in Economic Measurement, Applied Econometrics, and Time-Series Analysis and Forecasting from the National Association for Business Economics.

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