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On the Radar

FAQS ON THE MARKETS AND ECONOMY

What does the new stimulus deal mean for the economy?

After months of failed negotiations, Congress has agreed on a new $900 billion relief deal to provide much needed financial lifelines for millions of Americans struggling with the economic fallout from the COVID pandemic.

The legislation will establish a temporary $300/week supplemental jobless benefit, $600 in direct payments to most Americans, and over $300 billion in assistance for small businesses, among a host of other measures.

Bipartisan compromise was finally reached by removing additional aid for state and local governments, a Democratic priority, from the final bill, as well as liability protections that shield businesses from COVID-related lawsuits Republicans had advocated for. Both issues will now have to be addressed in separate legislation.

The agreement comes at a crucial time for the economy. With the recovery losing momentum amidst rising virus cases and renewed restrictions in activity, and key previous relief measures set to expire, increased fiscal support should help to bridge the gap for consumers and businesses until vaccine distribution becomes widespread.

Bipartisan COVID-19 Emergency Relief Act of 2020

Funding	Amount
Extended Unemployment Programs, Additional $300/week	$120bn
$600 Direct Stimulus Checks	$166bn
Small Business Loans/Grants	$325bn
Education/Childcare	$92bn
Rental Assistance, Eviction Moratorium	$25bn
Nutrition/Agriculture Assistance	$26bn
Healthcare Providers/COVID-Related Programs (Testing, Tracing, Vaccine Distribution)	$70bn
Transportation	$45bn
Other	$30bn
Total	**$900bn**

Source: CNR Research

KEY QUESTIONS

What did we learn from the recent inflation report?

What changes did the Fed make to their economic outlook?

What is the outlook for state sector credit quality?

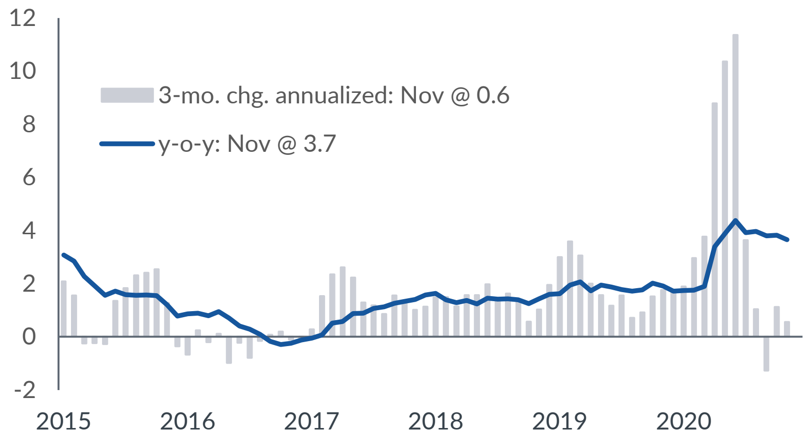
What did we learn from the recent inflation report?

CPI in November rose 0.2% m-o-m and stands 1.2% y-o-y. Pricing pressures from the supply/demand imbalance of the pandemic are dissipating. This is most notable in the food category. The three-month moving average–annual rate, currently stands at 0.6%, in June it was 11.4% (see chart). Car prices are also falling due to production catching up and offsetting the inventory shortages.

Some believe inflation will take off, just like they thought in the periods following the 2001 and 2009 recessions. But it didn't then and probably won't this time around – tame inflation has been the hallmark of this economy for the past 40 years.

That said, there will be some short-term pricing pressures in the spring as the pandemic-induced y-o-y declines drop off. Hopefully, a reopening of the economy will take place due to the vaccine. That may push inflation up toward 2.0% y-o-y. But it will be short-lived.

CPI — Food (%)



Source: Bureau of Labor Statistics as of November 2020.

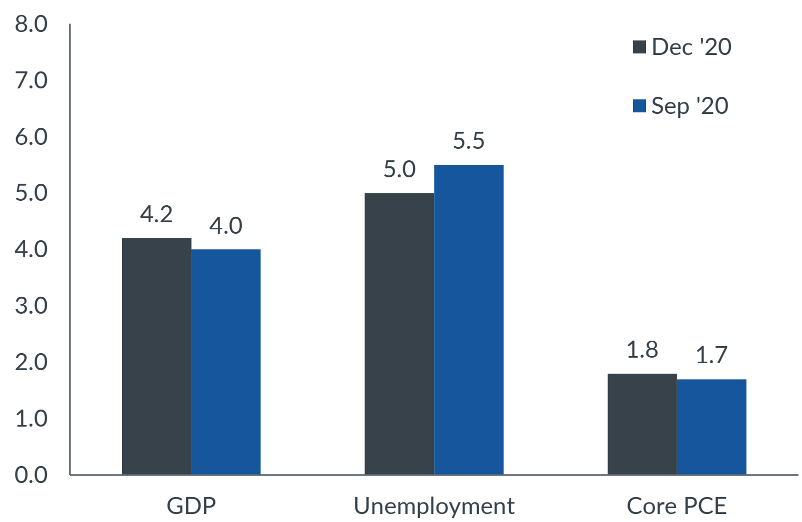
What changes did the Fed make to their economic outlook?

Fed policymakers elevated their outlook for the economy. Growth will be a little stronger, unemployment will be lower, and inflation will be a tad higher (see chart). The upgraded expectations were probably due to the positive vaccine developments.

The Fed made no significant changes to monetary policy, which was consistent with our outlook. Although there are some specific risks to the economy in the short run due to the regional lockdowns, any monetary policy changes take time to impact the economy. So a stimulus move by the Fed now would affect the economy in the late spring, at the earliest, just as it will hopefully be opening up from positive results of mass distribution of the vaccine — it won't be needed then.

The Fed committed to continuing their asset purchase program ($120 billion per month) until they meet their employment and inflation goal. That is a more extended period than previously thought, and should keep downward pressure on interest rates.

FOMC Projections for 2021YE



Source: Federal Reserve Bank as of December 2020.

What is the outlook for state sector credit quality?

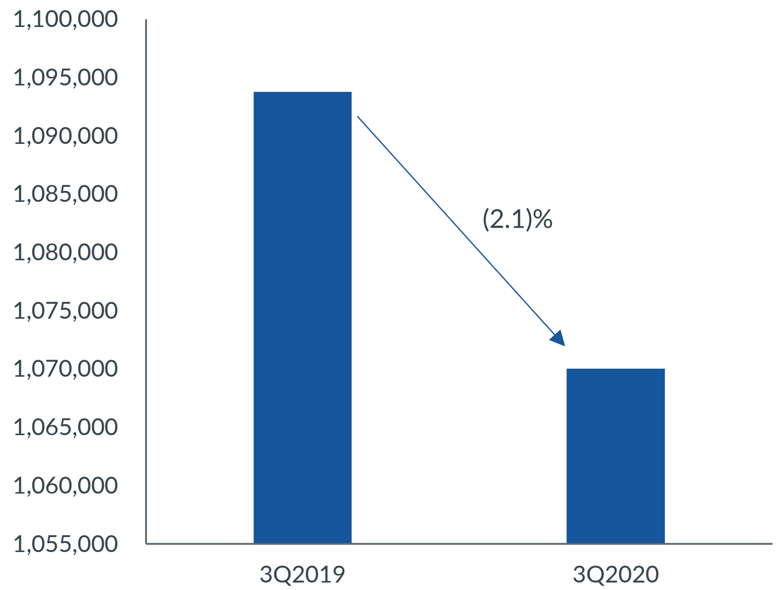
States should remain resilient and continue to respond to the public health crisis-induced budgetary challenges. Over the near-term, state finances will remain strained, yet most will manage their imbalances without any material diminution to credit quality.

Monetary and fiscal policy accommodations provided much needed economic support. The availability of payroll protection, economic impact payments, and enhanced unemployment benefits collectively provided broad relief to individuals and small businesses — the direct and indirect assistance to states helped to minimize the revenue dislocation. Job losses in lower-wage industries had less of an effect on most states' collections, with recovering financial markets and a strengthening housing sector adding significant benefit.

Available data indicates state revenue losses are less dire than initially predicted, although individual state performance varies widely. The U.S. Census reports rolling 12-month aggregate state tax collections through 3Q2020 fell roughly 2% YoY. Between April and September, the Urban Institute notes state collections fell approximately 5% from the previous year, suggestive of weak but manageable trends for most states. However, those states reliant on travel and tourism will experience a more protracted recovery.

Additional intervention should support the economy throughout the first half of 2021 despite high viral spread and hospitalizations now causing renewed restrictions. If vaccine distribution occurs as planned over the next several months, economic growth toward the back half of 2021 should allow for some stabilization in state metrics. Revenue recovery will likely extend beyond 2021, with certain states having to contend with somewhat larger budgetary shortfalls.

Rolling 12-Month Total State Tax Collections



Source: U.S. Census Bureau.

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Index Definitions

The Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care.