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Post Election Outlook: It's Still About COVID

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COVID does not care who won the election or who will control the Senate, but it will be the single largest determinant of where the economy goes next. COVID cases, positivity rates and hospitalizations are all surging again, a fact lost in the turmoil surrounding the election. The current jump in infections is worse than the surge we saw in the Sunbelt during the summer.

The current surge is national as well as global in scope and is occurring before temperatures plummet across the country, which could exacerbate the spread of the disease. The pace of infections in the U.S. is now growing at an exponential rate and is starting to overtake that of the U.K., which has already initiated another round of lockdowns. (See Chart 1.)

Conditions could get markedly worse before they get better. Epidemiologists are predicting that infections will peak in late January, about the same time the next president will be sworn into office.

We are assuming president-elect Joe Biden will be sworn into office on January 20, despite challenges to the election results. The president-elect has already announced a new COVID task force to rein in the spread of the disease and better coordinate the country's response. It is unclear what he can accomplish before he is sworn in and even then, the challenges will be substantial. Skepticism over the basic need to wear a mask to contain the spread of an airborne disease is high, while trust in the safety of a vaccine is low.

Fleeting Gains in Third Quarter

Real GDP surged at a 33.1% annualized pace in the third quarter, the fastest pace in history. The bulk of those gains could be attributed to the initial bounce in activity we saw in May and June. The level of economic activity was so high in June that the average for the third quarter would be substantial even if growth stalled between June and September, which it did. The third quarter surge was not enough to get the economy out of the hole created by COVID. Growth was still down 3.5% from the peak hit in the fourth quarter of 2019; that is close to the 4% drop in economic activity we suffered during the 2008-09 recession.

A surge in COVID cases is expected to bring the economy to a near standstill in the fourth quarter. Spending on discretionary services will suffer another setback. Commercial real estate is contracting, while lockdowns abroad put a damper on exports. Celebrations for the holiday season will be delayed. We could find new meaning to Christmas in July.

A federal aid package will offset some of that weakness in the first quarter. We will not be able to fully reopen until a vaccine is distributed and administered. We still have a long way to restore the trust that was lost during the pandemic, but there is a glimmer of light at the end of what has become a very long pandemic tunnel.

The light at the end of this dark tunnel is a vaccine. Pfizer announced that clinical trials on its vaccine suggest that it could be more than 90% effective. That is a game changer, but the time it takes to ramp up production and distribution means we will have to wait to reap the benefits.

Most don't expect a vaccine to be widely available until well into 2021 and not all vaccines in clinical trials will be as effective. Pfizer has promised up to 50 million doses by year-end and over 1.5 billion next year globally, but two doses are required for immunity. That is still a small fraction of the world's population and we still don't know how long it will last. The jury is still out on whether the vaccine is as effective against the most mild and severe cases.

The vaccine requires a complex and well coordinated supply chain to retain its efficacy; it has to be kept at 94 degrees below zero. Pfizer plans to start shipping to hospitals and clinics that can accommodate the need for cold storage after it receives emergency authorization by the Food and Drug Administration in December. Hospitals overwhelmed by COVID patients in the interim could inadvertently slow the distribution of a vaccine. We simply may not have enough health care workers to care for patients and administer a vaccine.

Why can't we just isolate older people to avoid the worst outcomes and open the economy more fully? Because death is only the most dire consequence of contracting COVID. The disease triggers a whole host of long-term health problems for patients of all ages, including those with only mild symptoms. These span damage to major organs, blood clotting, fatigue and neurological problems. This is at the same time that the paid sick leave provided by the CARES Act has lapsed.

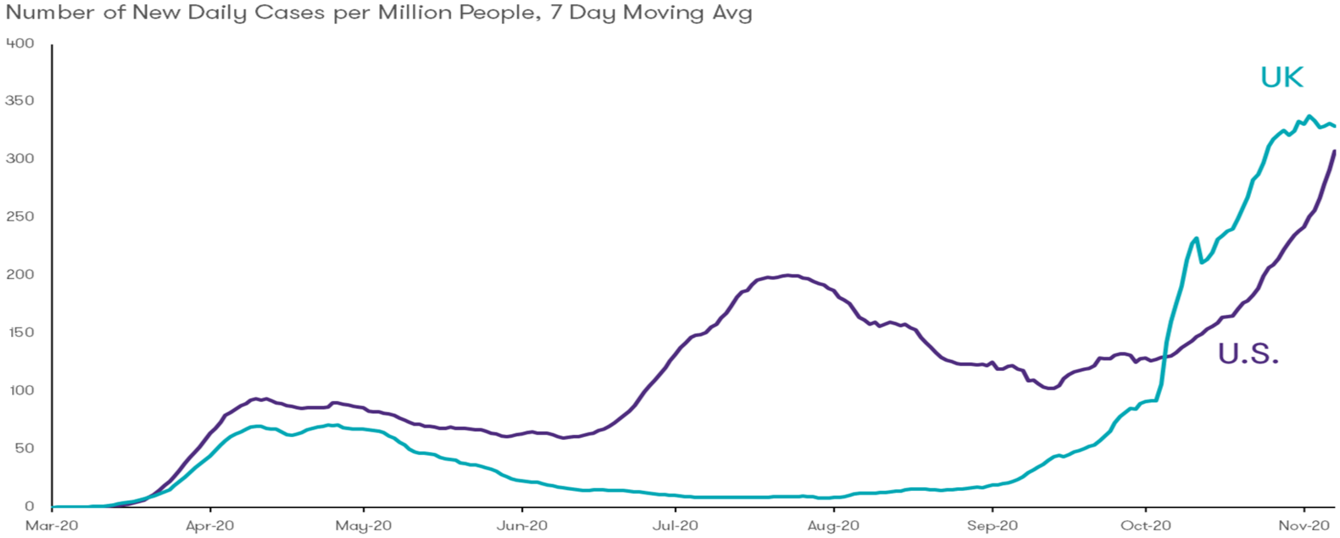
Hospitalization rates are high, which is overwhelming hospitals and undermining their ability to stay financially afloat. COVID is not a profit center; it is costly to treat and will accelerate consolidation in the health care sector. That will further curb access to quality health care and a vaccine, especially in rural areas where hospitals are few and far between.

The timing of the surge in cases couldn't be worse, given the lapse in aid tied to the CARES Act. Families who once were able to cover the basics of food and shelter are now running on fumes. The ranks of those who are slipping below the poverty line have soared. Layoffs once seen as temporary are now permanent. The number of people laid off for 27 weeks or longer jumped by more than one million in October.

Chart 1

Current Surge Could be Worst Yet

Number of New Daily Cases per Million People, 7 Day Moving Avg



Source: Johns Hopkins University, Europe CDC, Our World in Data, Worldometer

Unemployment is demoralizing. Once we cross the six-month mark, research shows it starts to take a more permanent toll on mental and physical health, family structure and the well-being of children. Reemployment is often at a lower-paying job than the one lost.

The resurgence in cases is in nearly every state. When consumers and firms usually ramp up for the holiday season, they will be pulling back. Celebrations will be scaled back or canceled. The hiring that accompanies those preparations won't occur and an economy that is recovering could stall out or worse.

High-frequency economic data has slowed. Credit-card usage has slipped; consumption of gasoline has fallen; and, initial unemployment insurance (UI) claims are still high. The number of people applying for UI extensions has jumped; those benefits will expire year-end. Consumer sentiment fell in October as job prospects and expectations about the future deteriorated.

This edition of ***Economic Currents*** takes a closer look at the outcome of the election and what that suggests about policy shifts going forward. COVID and the aid needed to fill the hole left by the pandemic will top the new president's agenda. We can't fully reopen and begin healing until people feel safe enough to congregate again. Waiting for a vaccine in the volumes needed to inoculate enough of us will feel like an eternity.

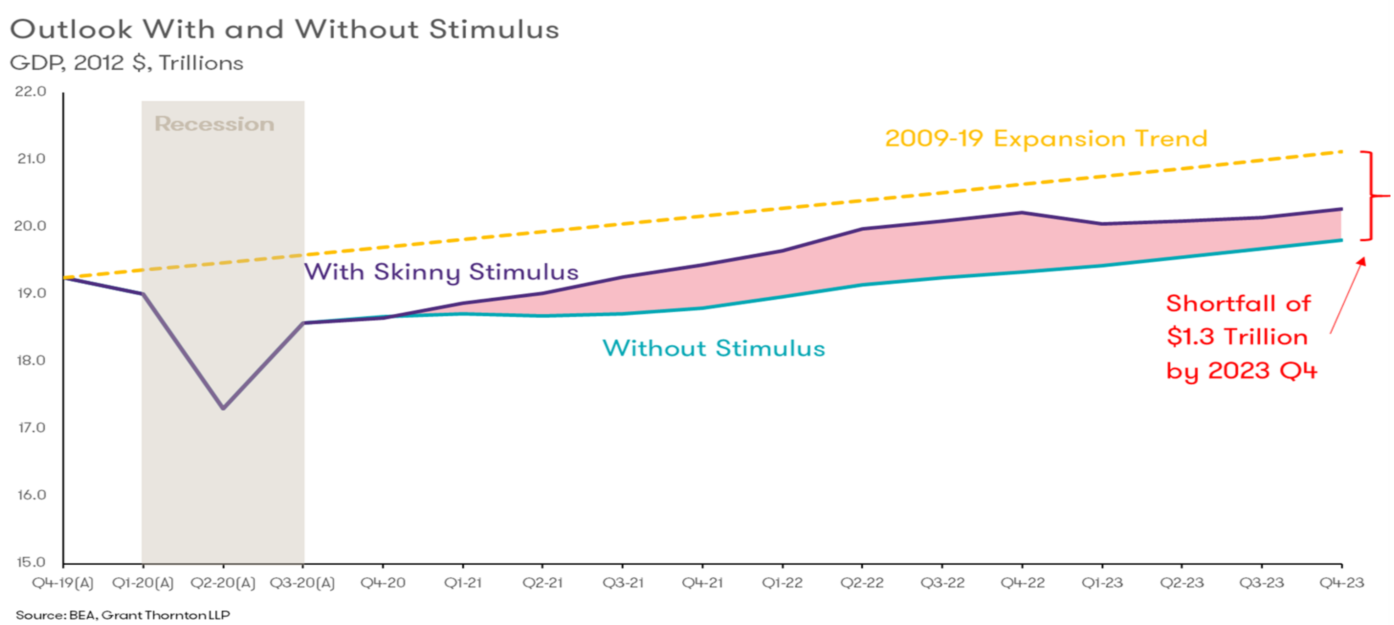
The remainder of the president-elect's agenda will depend heavily on the composition of the Senate, which is yet to be determined in runoff elections. The gridlock and partisan bickering that we saw leading up to the election is not expected to disappear even if the Democrats are able to win Senate runoffs in Georgia. Candidates who were able to replace incumbent Republicans are inherently more fiscally moderate than those who penned the agenda for the president-elect.

What's Likely and Doable

Chart 2 compares our postelection forecast with and without a new aid bill. We have put in a "skinny" $1 trillion package starting in the first quarter. That would get us back to our precrisis peak in economic activity in mid-2021. Employment would not reach its previous peak until late 2023. That is sooner than previous recessions. The receovery will depend on how much of the economy is left to reopen once a vaccine becomes widely available. The trajectory of growth could remain well below its precrisis trend for years to come without additional efforts to stimulate the economy.

Senate Majority Leader Mitch McConnell has said he'd be willing to pass a deal during the lame-duck session. McConnell is offering a much smaller deal than the package that Treasury Secretary Steve Mnuchin and Speaker Nancy Pelosi have been negotiating.

Chart 2



McConnell has some incentive to get a modest deal done, given the surge in cases and the boost that aid would provide incumbents in the Georgia races. I have given up holding my breath on the timing of a deal. The bulk of any new aid is not likely to show up in checking accounts until the first quarter of 2021, no matter how the data is cut.

Congress can't seem to get the votes to agree unless the stock market is tanking. This is despite the fact that the stock market is less reflective of the overall economy now than it was in the past. A vaccine can't come quick enough to feed hungry families .

There is now upside risk to the outlook for the second half of 2021 due to the prospects for a vaccine. That is still a long time for an economy that is struggling to reopen without the aid necessary to fill the holes left by COVID. Any missteps in the process would set us back further but it is very welcome news.

The president-elect has already announced a new COVID task force. The goal is to coordinate efforts in the U.S. and abroad, learn best practices and effectively distribute tests, PPE, therapeutics and a vaccine. Therapeutics could play a key role in minimizing the need for hospitalization, but they are still in short supply.

He has also pledged to rejoin the World Health Organization. Pandemics are by definition global in scope. Much like the terrorist attacks of 9/11, this requires global cooperation and a sharing of intelligence to prevent another outbreak.

That said, we only have one president at a time; the current president has yet to concede. The White House has frozen funds for the transition team, which could slow the process. The COVID task force will restart daily briefings, but not until January. That is an eternity when COVID case counts are rising at an exponential rate.

Fewer Tax Hikes and Spending Increases

Senate Democrats are more fiscally conservative than those who wrote the platform. Even if the Senate tips in favor of Democrats winning the two seats in Georgia, the new president is not expected to have enough votes for aggressive tax hikes or spending plans.

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Beyond COVID, the president-elect is expected to devote much of his time to repairing frayed relationships with our allies. He has pledged to rejoin the Paris climate accord.

He is expected to reverse a flurry of executive orders issued by the current president. These include an end to curbs on immigrants including foreign students, H-1B visa holders and Muslims from certain countries. The immigration curbs represented a body blow to university budgets, which rely on foreign students to boost revenues and subsidize tuition for U.S. students. The curbs on H-1B visas, including restrictions on the ability of married partners to work, have inhibited recruitment for technology firms.

Bottom Line

COVID still determines the course of the economy. The current surge in cases is much more worrisome than the one we saw in the Sunbelt over the summer; it is expected to be more disruptive to economic activity. The fact that the cushion provided by the CARES Act has lapsed adds insult to injury.

The longer we wait, the more the wounds triggered by COVID will fester and leave permanent scars. A vaccine with a 90% or better rate of efficacy is great news but can't stem the current surge in cases. Therapeutics that stem hospitalizations are coming on line but will take time to ramp up. We have the benefit of science and technology that our forefathers didn't during the 1918 flu pandemic. We need to leverage those advantages.

Buy a small turkey. Tell your family you love them enough not to risk their lives. Know they love you as much from afar as near. Delay celebrations and demand our elected officials do more for those suffering through no fault of their own. Masks are disposable; people are not.

Economic forecast — November 2020

	2020	2021	2022	2020:1 (A)	2020:2 (A)	2020:3 (E)	2020:4	2021:1	2021:2	2021:3	2021:4	2022:1
National Outlook												
Chain-Weight GDP[1]	-3.7	4.2	4.4	-5.0	-31.4	33.1	1.4	4.9	3.1	5.3	3.7	4.4
Personal Consumption	-4.1	3.1	6.1	-6.9	-33.2	40.7	-0.1	1.0	2.0	3.8	5.1	10.0
Business Fixed Investment	-5.0	3.4	6.1	-6.7	-27.2	20.3	0.7	4.4	3.9	6.2	5.6	5.4
Residential Investment	5.0	3.5	-3.8	18.9	-35.5	59.3	23.1	-2.2	-8.7	-6.7	-3.6	-4.8
Inventory Investment	-82	69	130	-81	-287	-1	40	50	65	74	86	116
Net Exports (bil $ '12)	-903	-1113	-1199	-788	-775	-1011	-1038	-1058	-1113	-1129	-1151	-1169
Exports	-13.8	3.8	9.9	-9.4	-64.4	59.7	5.5	6.7	0.1	11.4	12.6	11.5
Imports	-10.5	9.5	9.2	-15.0	-54.1	91.1	7.2	7.2	6.9	9.6	11.1	9.9
Government Expenditures	1.4	8.8	-1.9	1.3	2.5	-4.5	0.8	22.6	12.7	11.6	-1.1	-14.4
Federal	4.3	0.7	-1.1	1.6	16.4	-6.2	-1.4	2.0	1.2	0.8	-0.5	-3.3
State and Local	-0.6	13.8	-2.3	1.1	-5.3	-3.3	2.1	37.1	19.8	18.0	-1.4	-20.0
Final Sales	-3.1	3.4	4.1	-3.6	-28.1	25.5	0.6	4.7	2.9	5.1	3.5	3.8
Inflation												
GDP Deflator	1.2	1.8	1.8	1.4	-1.7	3.8	2.0	1.7	1.7	1.7	2.0	1.6
CPI	1.3	2.0	2.5	1.2	-3.5	5.1	2.6	1.1	2.3	2.3	2.6	2.7
Core CPI	1.8	2.1	2.1	2.1	-1.6	4.4	2.9	1.5	1.9	1.6	2.2	2.2
Special Indicators												
Corporate Profits[2]	-18.3	6.9	9.2	-6.7	-19.3	19.3	-18.3	-11.5	2.6	-26.1	6.9	14.7
Disposable Personal Income	5.4	-0.9	0.5	2.6	46.6	-16.3	-13.4	32.3	-26.0	1.4	1.2	3.5
Housing Starts (mil.)	1.38	1.36	1.30	1.48	1.08	1.43	1.51	1.39	1.38	1.35	1.32	1.29
Civilian Unemployment Rate	8.2	6.4	5.8	3.8	13.0	8.8	7.2	6.8	6.4	6.2	6.2	6.0
Total Nonfarm Payrolls (thous.)[3]	-7966	5435	711	-1257	-15406	6778	1919	2056	1150	1494	735	873
Vehicle Sales												
Automobile Sales (mil.)	3.5	4.1	4.2	4.0	2.6	3.6	3.7	3.9	4.0	4.1	4.3	4.2
Domestic	2.5	2.8	2.7	2.9	1.8	2.6	2.7	2.8	2.8	2.8	2.8	2.8
Imports	1.0	1.3	1.5	1.1	0.8	1.0	1.0	1.1	1.2	1.3	1.5	1.4
Lt. Trucks (mil.)	10.5	12.6	13.0	11.2	6.8	11.7	12.3	12.4	12.5	12.7	12.8	12.9
Domestic	8.6	9.8	10.1	8.9	6.7	9.2	9.7	9.7	9.7	9.9	10.0	10.1
Imports	2.4	2.8	2.9	2.3	2.1	2.5	2.6	2.7	2.8	2.8	2.8	2.8
Combined Auto/Lt.Truck	14.0	16.7	17.2	15.1	9.4	15.3	16.0	16.3	16.5	16.8	17.1	17.1
Heavy Truck Sales	0.4	0.5	0.5	0.4	0.3	0.4	0.4	0.4	0.4	0.5	0.5	0.5
Total Vehicles (mil.)	14.3	17.1	17.6	15.5	9.7	15.7	16.4	16.7	16.9	17.3	17.6	17.6
Interest Rate/Yields												
Federal Funds	0.4	0.1	0.1	1.2	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
10-Year Treasury Note	0.9	1.0	1.2	1.4	0.7	0.7	0.8	0.9	1.0	1.0	1.1	1.1
Corporate Bond BAA	3.6	3.6	3.8	3.9	3.9	3.3	3.2	3.7	3.6	3.5	3.6	3.6
Exchange Rates												
Dollar/Euro	1.13	1.18	1.19	1.10	1.10	1.15	1.18	1.18	1.18	1.18	1.19	1.19
Yen/Dollar	107.2	106.0	105.5	108.8	107.6	106.3	106.0	106.0	106.0	106.0	106.0	105.9

1. 1 in 2019, GDP was $19.1 trillion in chain-weighted 2012 dollars.
2. Corporate profits before tax with inventory valuation and capital consumption adjustments, quarterly data represents four-quarter percent change.
3. Total nonfarm payrolls, quarterly data represents the difference in the average from the previous period. Annual data represents 4Q to 4Q change.

Quarterly data are seasonally adjusted at an annual rate. Unless otherwise specified, $ figures reflect adjustment for inflation. Total may not add up due to rounding.