May 11, 2020

OBSERVATIONS

- Covid-19: With more than 100 candidate vaccines in motion, 3 are gaining attention based on announcements last week: Moderna granted clearance by FDA to begin phase 2 trials, Pfizer vaccine begins phase 1 trials, and the University of Oxford's vaccine is also in early human clinical trials.
- The U.S. Treasury will borrow nearly $3tn this quarter – a record – due to stimulus related to COVID-19 and changes in timing related to tax receipts.
- $187bn (average loan size of $73.5k) of the $310bn Payroll Protection Program (PPP) has been lent since the program's reopening on 27-April. The average Loan size seen in the first round of the PPP was $206k.[1]
- Mortgage rates for 30-year conventional homes hit a record low 3.4%. New purchase mortgage applications reported 6-May were 7% higher from the prior week, though down -19% from one year ago. Refinance activity (70% of overall mortgage applications) were reported up +210% from a year ago.[2]
- The U.S. services sector contracts for the first time since December 2009. The ISM non-manufacturing index dropped to 41.8 in April vs. 52.5 in March[3].
- Retail pain: J.Crew, Neiman Marcus, and Stage Stores file for Chapter 11 bankruptcy protection. J.C. Penny could file as early as this week.
- Official unemployment figures put the unemployment rate at 14.7% in April with 20.5 million jobs lost in the month alone—this was the highest unemployment rate and largest month-over-month job loss since monthly data began being published in 1948.[3]
- 83.7% of the 20.5 million jobs lost in April came from the services sector, while the goods and government sectors accounted for 11.5% and 4.8% of jobs lost. Leisure and hospitality alone accounted for 7.7 million of the 20.5 million jobs lost.[4]

EXPECTATIONS

- Oil has recovered back above $24/bbl[3] – levels last seen in mid-April. Signs of production cuts curtailing supply, and easing storage fears along with the gradual reopening of economies has helped spur oil's gains. Uncertainty related to demand remains and the market continues to be oversupplied.
- With the S&P 500's recent gains, the P/E (NTM) has pushed to 20.4X, the highest level since April 2002. Thus far, 86% of S&P 500 companies have reported Q1 earnings, with a blended earnings growth rate of -13.6% YoY[5]. As earnings season winds down (21 S&P 500 companies report this week), macro data likely to take center stage.
- In a sign that investors are highly scrutinizing debt deals, United Airlines postponed a planned $2.25bn debt raise as investors demanded sweetened terms. The airline plans to use proceeds to pay off a 1-Yr $2bn loan taken from banks on 9-March.

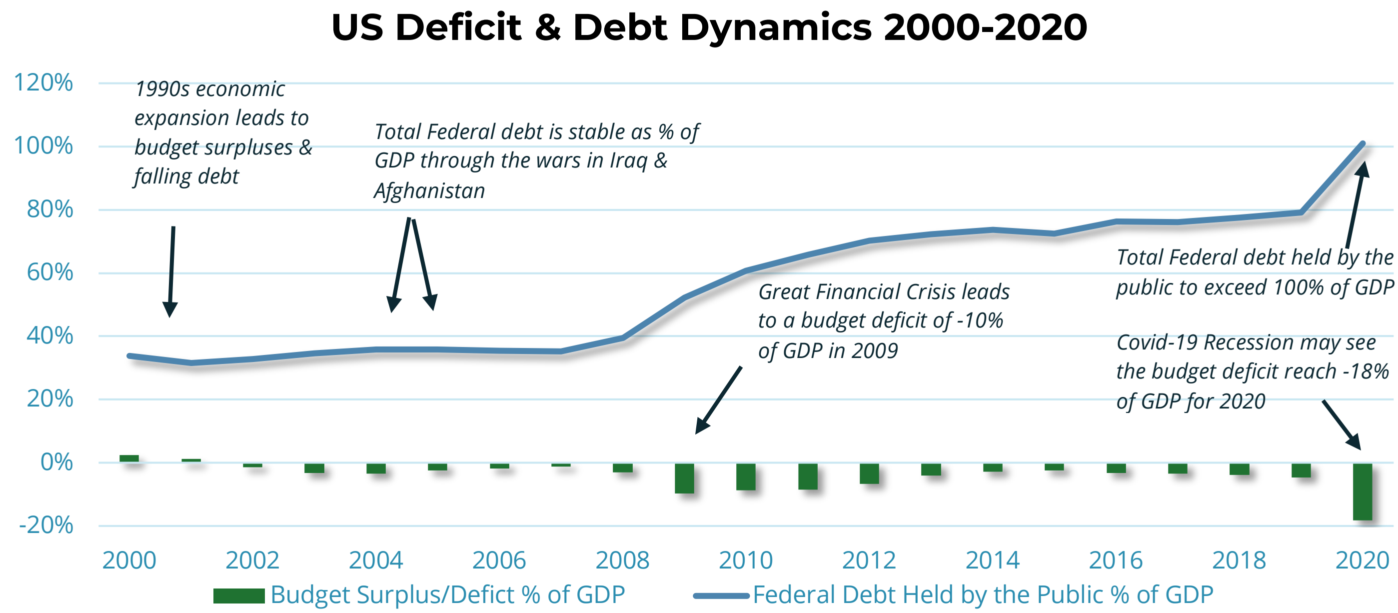
ONE MORE THOUGHT

With the imminent start of the Federal Reserve's Main Street Lending Program (MSLP) we thought to spend a moment reviewing the program(s) as we understand them. The MSLP is comprised of three facilities: (1) Main Street New Loan Facility (MSNLF), (2) Main Street Priority Loan Facility (MSPLF), and (3) Main Street Expanded Loan Facility (MSELF), all of which target 4-year loans at LIBOR+3% and include a 1 year deferral on repayment. Eligible lenders

[1] U.S. Small Business Administration, as of 3-May
[2] Mortgage Bankers Association, as of 6-May
[3] Bloomberg LP
[4] U.S. Bureau of Labor Statistics, Employment Situation Summary, 8-May
[5] Factset Earnings Insight, as of 8-May. NTM = Next Twelve Months

(i.e. banks) originate the loans with the Fed's respective facility purchasing between 85% and 95% of the value of those loans – provided they meet the criteria of the respective facility.[6] These programs are designed to encourage U.S. banks to continue to lend to small and medium sized businesses by minimizing the risk these banks take in issuing these loans given the Fed will purchase the bulk of these loans once issued. So long as the small/medium sized business was viewed by the bank as being in "good financial standing" before the pandemic, it would be eligible for these programs. The programs should ensure that small and medium sized business are not crowded out of bank lending by larger firms that may be viewed as less risky by the banking system.

CHART OF THE WEEK



Source: Congressional Budget Office (CBO), Clearstead

The $3.6tn in cumulative emergency spending approved over the past 6 weeks exceeds the total stimulus spent over a 5-year period during, and following, the 2008-2009 financial crisis.[7]

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[6] *Federal Reserve MSLP Term Sheets updated 30-April*
[7] *Committee for a Responsible Federal Budget, WSJ*