Cornerstone
ASSET MANAGEMENT GROUP, LLC

5411 Commonwealth Ave | Western Springs, IL 60558 | 312-485-6847 | Kim.Suchy@csamg.com

Economic Indicators January 2021

By Kim W. Suchy

Like me, you are probably excited that 2020 is behind us. The eve of December 31st has usually been reserved for celebrating our accomplishments of the past year and welcoming the optimism of the New Year. This time, it seemed, it was an eve that could not pass quick enough. It was time for a new start and if there was a way to eliminate 2020 from the records (except for my eye exam results of course) we would all be better off.

The coronavirus pandemic (C19) has been a once-in-a-lifetime event that has transformed our society and the global economy almost overnight. This global pandemic has caused massive dislocations in business operations, government policies, travel, health care practices, international trade and human psychology. We have experienced a couple of serious global recessions over the past twenty years specifically the Great Recession of 2008-09 and the Dot-Com Bubble of 2001-02. These two recessions forced many changes in the way we do business but they were mostly changes in regulations and government oversight designed to slam the door on risky business practices and curtail future excesses. This time, it is different.

Many of the changes that have surfaced due to C19 have stemmed from the ingenuity of the private sector. Many of these changes are here to stay and likely strengthen as life returns to normal. While there are many, let's focus on three. Remote working, on-line dining and short-term vacation rentals (yes, vacations).

With regard to remote working, C19 created a surge in demand for technologies that enabled organizations to employ a decentralized workforce, and this trend will to continue. Technologies that facilitated team or firm-wide video conferences (i.e. Zoom and others) and electronic signatures of documents (i.e. Docusign).

To cite a great example, the WSJ reported that Nationwide Mutual Insurance Co. illustrates the shift to work from anywhere. Shortly after the pandemic hit, Nationwide had 98% of its 28,000 employees working from home. The initial impetus was safety, but chief executive Kirt Walker said it accelerated pre-existing plans to rely on virtual operations. Before the pandemic, roughly 15% of employees worked from home and the company now plans for half to eventually do so permanently.

As a result, Nationwide is closing 17 offices across the country and reducing its real estate needs by roughly 1.1 million square feet and saving about $100 million, which it says will be used to reduce policyholders' premiums. Further, this will enhance its earnings profile.

Nationwide is among the great majority of businesses conducting the same fast-forward transformation of producing more goods and services with fewer employees and fewer on-site location workplaces. I'm sure many of you were of the view that much of this work from anywhere world would give way to a return to the office, but now we are seeing more evidence that remote labor could be a permanent thing.

One caveat is that this new normal of work from anywhere has limited effect on manufacturing, healthcare, construction, landscaping, some retail, hospitality, travel, live entertainment, sports, home and auto repair, personal and pet care services, etc., but where this new normal has significant and long-lasting impact is in federal, state and local government operations, education at the collegiate level, real estate, law practice, financial services, media, publishing and extensive areas of high-tech, just to name the obvious target sectors. The savings and productivity enhancements have and will continue to be significant.

With respect to on-line dining, the National Restaurant Association, reports that roughly three million employees have lost their jobs, 100,000 establishments closed permanently, and the industry lost $240B in sales. While no a complete loss there has been a strong growth in online dining. Forced lockdowns in major cities have driven consumers to online delivery services and have created interesting opportunities.

Of course, the delivery services have prospered but perhaps the most intriguing is the explosive growth of ghost kitchen startups. These kitchens build and manage large commercial kitchens with no dining room where food from multiple restaurants is prepared simultaneously. Because they are designed exclusively for delivery, they are extremely efficient, which increases profitability for both the restaurant and the delivery service, and it decreases the time customers must wait to receive their meal. This may be a concept that is here to stay as many restauranteurs who have closed their dining facilities seek a "pandemic proof" model. Pandemic proof or not, I still find it tough to order my favorite porterhouse and have it delivered but most other cuisines are certainly in play.

One other area that has rapidly transformed is vacation rental property. Much like restaurants, travel and tourism have been hurt extremely hard by C19. The U.S. Travel Association, reports that travel and tourism has suffered $491B in cumulative losses in 2020. While many of us have not taken a vacation during this C19 period, one segment of the market that has held up reasonably well is vacation rentals. As consumers avoided hotels due to their transient flow, they gravitated to private rentals from vacation rental sites as whole families could rent a property for a week or two and work/school from anywhere. Certainly hotels will come back into vogue as we re-engage in travel but the vacation rental concept may be one that sticks until consumers are comfortable with the herd immunity of C19.

Here is to a better 2021. I wish all of you good health and success.

Here is your look at developments in the global marketplace.

Positive Developments:

- The recovery in the industrial sector continued in November. In addition, readings in prior months were revised higher, and when included with the headline 0.4% boosted November's gain to 0.8%. Industrial production has now made up 71% of the decline in activity seen during the height of C19 lockdowns back in March and April, but still has a way to go.

- New home construction is very robust as it has shrugged off recent increases in C19 cases that have negatively affected other sectors. While the biggest gains in came from multi-unit construction, single-family construction rose for the 7th mo. in a row, hitting the highest level since 2007. As I have stated before, as the pandemic continues there is a shift buyer of preferences away from dense cities and toward the more spacious suburbs. First Trust reports that single-family construction has now made more than a full V-shaped recovery and sits 14.7% above its February pre-pandemic high.

    - New building permits rose 6.2% in November at a 1.6M a/r. Compared to a year ago, permits for single-family units are up 22.2% while permits for multi-family homes are down 13.7%.

- As expected, the Fed did not change rates at its December meeting. In fact Fed Chair Powell noted The Fed has no plans to move rates in 2021, 2022, or 2023! With regard to Fed forecasts, GDP and inflation projections were revised higher, while the unemployment rate forecasts moved lower, all signaling a stronger economic recovery than the Fed believed possible earlier this year. In fact, back in June, the Fed forecast the US economy would see a decline of 6.5% in real GDP in 2020, now they are targeting a decline of 2.4%. The year-end unemployment rate was projected at 9.3% back in June, but is now seen at (the current level of) 6.7% And future year outlooks have brightened, both for economic growth and unemployment, which is now forecast to fall to 5.0% in 2021 and move below 4.0% in 2023.

- A very encouraging development rests with the rapid growth in new business applications. So far this year, there have been more than 500K applications to the IRS for employer identification numbers associated with planned wages. Even with the big slowdown following the onset of C19, that's 6% higher than the recent average. This is a big boost in the vote of confidence in the future by America's entrepreneurs that should provide a sound foundation for a strong economy in the years ahead.

- Real GDP growth for 3Q was revised up to a 33.4% annualized pace versus the 33.1% reported last month. Corporate profits were also revised higher. In essence, the economy surged in Q3 and will likely continue its upward climb in Q4. Looking ahead to Q1 2021,

the pace of growth will depend on the path of C19, the pace of vaccination delivery AND acceptance, and the restrictions on business activity being imposed by state and local governments.

- The Census Bureau reported that durable orders rose 0.9%, beating expectations of a 0.6% increase. Vehicle orders rose 2.4%, electrical equipment orders rose 0.8% and machinery was up 0.9%. Fabricated metals orders fell 0.8%, but they rose 2.3% and 2.9%, respectively in September and October. Overall, this was a very positive report!

- Modestly higher inflation coupled with a weakening Dollar, the potential return of post-pandemic aggregate demand and a return to investor risk-on appetite, will be beneficial to asset classes like commodities and emerging markets (EM). There has already been rise in oil and metals prices since C19 onset lows. Many EM currencies tend to have a strong correlation with commodities and a boost in commodity prices can provide reasonable expectations for growth in many commodity driven economies like Latin America and Africa. EM's are also inversely correlated with the Dollar as much of their debt is Dollar denominated so as loans are paid back, they are paid back in cheaper Dollars which will enhance credit profiles of the borrowers. Further, as commodity prices rise their currencies strengthen, and purchasing power accelerates facilitating a growth in demand. *I could keep going but I'll end my econ 101 lesson here.*

Neutral Developments:

- Commodity prices tend to have an inverse relationship with the Dollar. A strengthening U.S. dollar will put downward pressure on commodity prices, while helps boost prices. Persistent low levels of inflation globally has contributed to the lackluster performance of commodities over the past decade or so but the decline in the relative value of the U.S. dollar over the past few months has provided a nice tailwind for commodities (gold and silver have certainly had a boost).
- Stock buyback activity for Q3 shows buyback activity increasing to $101.B from $89B in Q2. Buybacks remain far below the Q4 2018 peak of $223B. For Q4 2020, buybacks are expected to continue to rebound as more issues venture in to cover employee options; expenditures likely to remain top heavy.
    - The top 20 issues in the SP500 dominated buybacks accounting for 77% of all buybacks. Apple, Berkshire Hathaway, Intel, Google and Microsoft were the top firms buying back their stock.
- After 5 straight mos. of gains, *existing* home sales took a breather in November. Existing home sales declined 2.5% in November to a 6.7M a/r. Sales are up 25.8% vs. a year ago. The median price of an existing home fell to $311K in November and is up 14.6% versus a year ago. Average prices are up 11.3% vs one year ago. Low interest rates and strong demand during the flight from cities, has given rise to higher prices.

- *New* home sales fell dramatically as sales fell 11% AND several previous months were revised down as well, making November's drop the 4th decline in a row. Even with the recent declines, new home sales are still 8.7% above the January pre-C19 high and are on pace to log the best annual sales pace since 2006 according to the Census Bureau.

- Initial claims for unemployment insurance fell from 885k to 803k last week, quite possibly because — as the WSJ noted this morning — an increasing number of states are cracking down on fraud. Nevertheless, despite the drop, the average level of claims in the first three weeks of December is 111k higher than the average in November. Normally, a 100k increase in claims is enough to justify worrying about a recession.
- Now for your Econ 101 lesson for this month, what is the Misery Index? The first misery index was created by Economist Arthur Okun, who served as an advisor to President Lyndon B. Johnson. Okun's misery index used the simple sum of the nation's annual inflation rate and unemployment rate to provide Johnson with an easily understood snapshot of the economy's health. The Index, regained its popularity earlier this year as another yardstick to assess the C19 impact. In March, pre C19, the Index read 5.94. In the early onset of C19 shutdowns, the Index was 15.1. Today, the most recent measure is 7.8. While many of us can find plenty of other misery-like variables to add to this index, it is at least important to note that Okun's Index has improved dramatically.

Negative Developments:

- Fears over a new strain of the coronavirus that causes C19 (as discovered in December in the U.K.), may continue to fester. The U.K.'s health minister Matt Hancock warned that the new strain, said to be highly infectious, was "out of control" as the government terminated the planned relaxation of the rules over the holiday period. Prime Minister Boris Johnson said the strain could be 70% more transmittable…*while this number is disturbing, let's wait on verification as to strain and rate of transmission. In the meantime, news and rumors could inject more volatility into the markets.*

- Microsoft reported that a major hack took place over the past few months. Hackers gained access to 18,000 government agencies and companies. From there they planted "back doors" into the networks of some 40 companies, government agencies and think tanks that allowed them to come and go, steal data and — though it apparently has not happened yet — alter data or conduct destructive attacks.

- Initial claims for unemployment insurance fell from 885K to 803K last week, quite possibly because — as the WSJ reported on 12/23 — an increasing number of states are cracking down on fraud. WSJ states that Illinois blocked 341K fraudulent claims and Michigan is investigating 190K. As fraud is rooted out, claims are revised. Louisiana alone revised claims down 30K in 2 weeks in November after a review. Nevertheless

shutdowns in certain C19 hotbed cities have been the primary driver for significant claims. Despite the drop, the average level of claims in the first 3 weeks of December is 111K higher than the average in November. Normally, a 100K increase in claims is enough to justify worrying about a recession…..*This time it is different the "R" word will be back-burnered as many economists see the unemployment situation as temporary*.

- The Census Bureau reports that the share of American renters concerned that they will miss their next month's rent has been rising. This is a distressing development, given the expiration of the federal eviction ban this winter. For mortgage borrowers, the foreclosure moratoriums and the boost in home prices has made the situation less dire. There are currently 2.8M loans in forbearance plans with more than 500K due to expire at year-end.

- The Bureau of Economic Analysis reported that personal income declined 1.1% and personal consumption fell 0.4% in November Personal income is up 3.8% yoy, while spending has declined 1.3%. Disposable personal income (income after taxes) declined 1.2% in November, but is up 4.3% from a year ago. Consumer prices were basically unchanged in November and are up 1.1% yoy. After adjusting for inflation, "real" consumption declined 0.4% in November, and is down 2.4% from a year ago. Leading to the slide in income and spending was a combination of stimulus roll-offs and a slowdown in consumer purchases due to a return of business shutdowns and restrictions. New York and California were key headwinds in the shutdown/restriction factor.

- The Conference Board reported that its Consumer Confidence index declined to 88.6 in December, down from 92.9 in November, the 2nd straight monthly decline, bringing consumer confidence to its lowest level since summer as more C19 restrictions have deflated consumer optimism, particularly in states where business shutdowns and enhanced restrictions are taking place. Many will be glad when 2020 is over (including me). With progress being made on the C19 front, a new mess surfaced via a cyberattack on the U.S. government agencies. Details remain murky at the time of this writing but certainly expect lots of finger pointing and cold war-like behaviors as we move into 2021.
- The U.S. trade deficit in goods climbed 5.5% in November to a new record high, reflecting weaker U.S. exports tied to C19. The trade gap in goods increased to $84.8B in November from a revised $80.4B in October, according to the Census Bureau.

Over the past month, despite issues surrounding our elections and the degree of penetration of C19 vaccinations the markets were higher across the board. Moving forward, the headwinds of herd immunity and getting people back to work continue. Last month, energy, financials and technology were the strongest performing sectors in the SP500 while utilities, real estate, industrials and consumer staples were laggards.

U.S. Index	Last Month (% return)	YTD (%)
S&P500	2.6	16.4
Dow	2.6	7.4
NASDAQ Comp	4.3	43.6
Russell 2000	7.6	18.4

On the international front, both European and Asian markets logged positive returns. Gold bullion was higher last month and posted a 20.2% return in 2020 holding its spot as one of the best performing asset classes of the year.

International Index	Last Month (% return)	YTD (%)
Euro Stoxx 50	0.8	-5.1
Hang Seng	2.5	-3.4
Germany	2.5	4.4
Nikkei	2.5	16.0
FTSE-U.K.	1.2	-14.3
China Shanghai Comp.	0.6	13.9
Gold	3.7	20.2

While bond yields remain near record lows the 10-year yield is trading at .92% which is 8 bps higher than at the close of November. The 2-year Treasury closed yielding .12%, which is slightly lower than where the 2-yearsclosed last month. The curve has widened a bit given that the 10/2 spread is at 80bps or 12bps higher than last month. The slight widening is typically good for financial (banks) as banks borrow at the 2-year and lend at the 10-year. A wider spread enhances their profit margin.

As always, if I can be of additional guidance, please feel free to call me at 312.485.6847.

Best regards,

Kim W. Suchy
CEO Cornerstone Asset Management Group

Email: Kim.Suchy@csamg.com
Website: www.csamg.com
LinkedIn: https://bit.ly/30Gr3XF