



Rosenberg
Research

*Economic Research
for Informed Investing*

David A. Rosenberg
Information@rosenbergresearch.com

June 8, 2020
Economic Commentary

We are a global independent economic research and markets strategy firm, providing clients with unbiased insights and actionable investment guidance.

Breakfast with Dave

IN THIS ISSUE

MORNING MACRO/MARKET MUSINGS

- Once again, the current data are being ignored as markets move mostly on hope and faith

THE GREAT REPRESSION REVISITED

- There is no renewed hiring cycle that brings the unemployment rate back down without demand — demand is the key

TEN PROBLEMS WITH THE MAY JOBS NUMBER

- The irregularities in the data were incredible

THERE IS NO V IN THE NUMBERS (BUT THERE IS A U)

- Let's assess just how well the U.S. economy has been doing into the first month of the "re-opening"

HOW ABOUT AN F-SHAPED RECOVERY — AS IN FRUGALITY

- There is more of a permanent change in behavior following the sort of shock we have endured in the past several months

DON'T FIGHT THE FED!

- The logic of today's investing environment is: (i) valuations don't matter and, (ii) don't fight the Fed!



Rosenberg
Research

*Economic Research
for Informed Investing*

MORNING MACRO/MARKET MUSINGS

HIGHLIGHTS

- Investors enthused over more rounds of stimulus
- New York City begins its re-opening phase today!
- Investors ignore lousy Chinese trade and German production data
- The biggest source of upside pressure on stocks has been short-covering
- Investors seem far too early in celebrating – “re-opening” macro data still depressed
- Bond yields rose sharply last week but now hitting interesting resistance points
- We provide a list of laggards to buy if you to favor the V-shaped recovery view
- BBB-rated municipals look very attractive right now

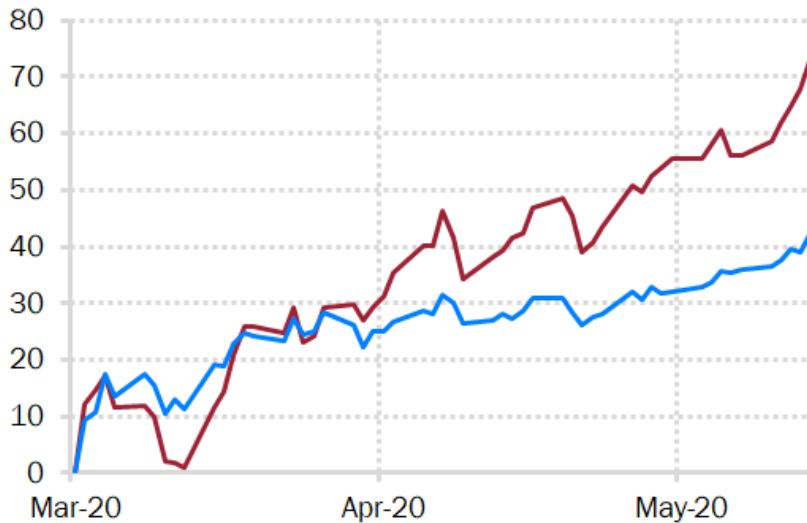
COMMENTARY

Global stock markets are mixed to kick off the week. While Asia-Pac extended its rally with a 0.7% gain, European markets were actually down 0.7% at 5 a.m., but are now close to being flat as the move towards reflationary-value stocks continues unabated. U.S. futures also were just slightly to the upside, but in the past few hours have been gaining momentum (excitement is building over New York City’s phase one re-opening which begins today). **There is tremendous confidence that Jay Powell will repeat at this week’s policy meeting that he will continue to underpin financial market pricing.** While it is hard to identify real buyers in the flow data, there is no selling of equities and that alone is extremely important. On top of that, we have a huge short squeeze going on – the most shorted stocks have collectively soared 65% from the March lows, and the CFTC data show that the four-year high net speculative short position on the CME is being squeezed (down 14% last week to 38,593 net S&P 500 short contracts to a three-week low – likely more to come).

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

CHART 1: Rally In Hated Stocks: Bears Give In As Market Trends Go Against Them
United States
 (red line; most short rolling; percent)
 (blue line; S&P 500; percent)



Source: Bloomberg, Rosenberg Research

Oil prices are bid with the weekend OPEC+ production cut (and with no drama) — Brent crude advanced 1.1% to \$42.77 per barrel. Iron ore spiked 4.8% even though the Chinese trade data were hardly stellar (exports -3.3% YoY in May — quite the swing from +3.5% in April — and imports tumbled 16.7%). Gold has rebounded 0.6% to \$1,695 per ounce after last Friday's shellacking — the softer tone to the DXY dollar index is helping out (down a further 10 pips, to 96.84, here in the early going). Both the Australian dollar (+0.5% to 70 cents; U.S.) and New Zealand kiwi (+0.5% to 65.37 cents; U.S.) are gaining against the greenback (New Zealand moved to end social distancing requirements after reporting zero active cases of COVID-19). Norway's krone, up 0.3% to 9.2836 kr, has benefitted from the oil price jump. Sterling also firmed 0.3% and touched the \$1.2730 level overnight before settling back to \$1.265.

Bond markets remain a bit jittery with the yield on the 10-year T-note up 1.3 basis points, to 0.91%, and now close to key price support levels at the 100-day moving average (a break here at 0.99% sets up a test of the 200-day at 1.37%). Globally, we see France now almost 7 basis points above zero and 10-year JGBs are 4 basis points out of negative terrain. Even German 10-year bunds are now within 30 basis points of following suit.

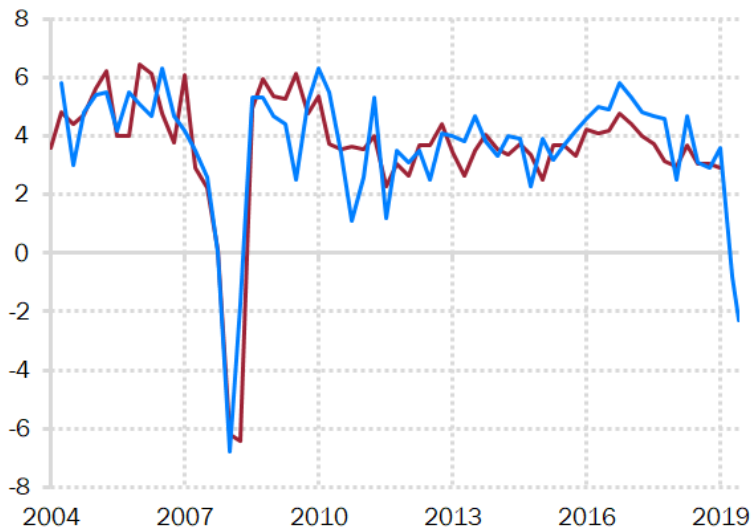
Once again, the current data are being ignored as markets move mostly on hope and faith. Here we have German industrial production plunging 17.9% in April after an 8.9% March slide — the YoY trend slipping to -25.3%. And no move in the German bund market at all. While the Bloomberg global GDP tracker is still flashing negative for May (a 2.3% annualized contraction in real economic activity), what the typical stock market participant sees is an improvement relative to the 4.8% slump in April. And the degree of stimulus announced out

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

of Japan, China, Korea, Europe and the U.S. in the past week alone topped \$5 trillion. So, the markets have adopted a view that policymakers will simply not stop pumping the system with cash. This remains a short-covering, hope-based, policy-led rally bereft of any solid fundamental underpinnings.

CHART 2: Worst Over: Global GDP Tracker Suggests Output Continued to Fall In May, Albeit At A Slower Pace
Global
(red line; global GDP change (PPP-weighted); percent)
(blue line; Bloomberg Economics global GDP tracker; percent)



Source: Bloomberg, Rosenberg Research

Regardless of my view, which is highly skeptical, let's assess what the message from the market actually is. Here is a review of the action of late, with the S&P 500 soaring more than 40% from the lows, and the reflationary pro-cyclical value plays taking over leadership after being totally decimated in that February-March meltdown (looks to me like nothing more than an extremely powerful short squeeze – I did see a reference to this in the Saturday Globe and Mail; something to the effect that there were a record \$275 billion of total short positions in U.S. equity futures at the end of May... cover, Mortimer!):

- The retailing stocks have surged 48% and are at a new high.
- The semiconductors have jumped 53%, and also are at new all-time highs.
- The truckers have gained 59% and are at new highs.
- Restaurants are up 52% from the lows and are 9% shy of a new high.
- Energy stocks have almost doubled (+86%), but are still 27% shy of the 2020 peaks.
- The airlines have bounced 54% and they remain 41% below their highs.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Economic Research
for Informed Investing

- Hotels/resorts/cruise line stocks are up 87% and remain 38% below their highs.
- Casinos have leapt 89% but still have 32% to go before hitting their highs.
- Auto stocks have spiked 85% from the lows – they are 19% below their nearby peaks.
- The rails have risen 61% and are only 3.5% from a new high.
- Old-economy machinery stocks are up 59% from the lows and are just 7% from the highs.
- The financials have advanced 48% – now 16% below the pre-COVID-19 highs.
- Homebuilders have skyrocketed 93% from the lows; now only 13% from the highs.
- The regional banks – how about up 64% from the trough and 22% below the peak.
- Office REITs, once left for dead, are up 36%, though remain 26% below their highs.
- Mall REITs, and this is rather incredible, have staged a 36% rally off the lows – still 26% shy of the highs.
- The small cap S&P 600 is now up a resounding 51% and now just 14% away from a new high.
- Within the bond market, the average yield in the high yield space has reversed 80% of the earlier backup, and is down to 6.1% after an amazing 500 basis point plunge from the highs.
- In the investment grade space, the reversal has been over 90% as the average yield is down to 2.4%.

So here is what the market, and the vigorous rotation beneath the headline, is telling us about the current belief system in the equity universe:

1. The recession is over and the recovery has begun.
2. This will be a V-shaped economic recovery.
3. A vaccine announcement is coming no later than the Fall.
4. The polls are fake and Trump will win the November election.
5. The worst fears over the pandemic were unjustified; the economy never should have been locked down; there will be no “second wave” and if there is, it will be contained but even if not, there will never be a national lockdown again.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

*Economic Research
for Informed Investing*

6. Friday's jobs data has reinforced this confidence that things are going to return to normal very soon.
7. Even with a recovery at hand, Fed Chairman Powell has pledged to continue to pump liquidity into the market (and the proof in the past three months is in the dramatic P/E multiple-led expansion) and that this is all equities and corporate bonds need; the fundamentals can stay on the back burner (as in, a 43% YoY plunge in Q2 corporate earnings).
8. The same is true of fiscal policy – even with the apparent “good feel” to Friday's jobs data, President Trump stated that he is willing to sign off on an additional fiscal stimulus package.
9. This is the dilemma for us “bears”. The system is swamped with money. We saw that in the April data when every dollar lost in wages and salaries was overwhelmed four-to-one by government stimulus checks. The weekend WSJ cited analysis showing that over half the ranks of the unemployed are making more money now than they were before the virus hit. Never before has the government spent \$3 trillion (at an annual rate) in the form of income transfers in a single month.
10. This is the crux of the matter. The market believes we are on the road to a durable recovery. And the market is doing the math and sees if we get this next round of fiscal and monetary stimulus, the total infusion will be \$10 trillion for the entire year. That offsets the likely loss of GDP for 2020 as a whole by roughly a five-to-one ratio. Obviously not all of that will get spent but investors are doing the math and seeing that the policy stimulus will outlast the worst point of this recession and any possible lingering aftershocks.

One of the major developments in the past two weeks was what didn't happen. First, we spent all of last year with the stock market on tenterhooks from the “Phase One” trade deal and its success catapulted the S&P 500 by at least 20% into the end of 2019. **So here we have a serious erosion of the U.S.-China relationship, which clearly will affect trade, and the market hasn't shrugged.** This was a surprise to me. Second, these riots and demonstrations are clearly unsettling, not even including the risks of creating another wave of infections, and the market just doesn't care. It has become commonplace for have strategists to tell people that such rounds of social unrest never cause much of a market ripple, and they even cite 1968 – even though, from a bird's eye view, that marked the end of a 14-year secular bull market and the onset of a 14-year secular bear market.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

Economic Research
for Informed Investing

But investors believe that the Fed and the federal government will simply not let that happen. The prevailing view is that the S&P 500 has become so important as an economic and policy yardstick that monetary and fiscal officials alike will do everything to put a floor under the market at the worst of times, and propel it as best they can at the best of times. To many investors right now, risk-on has become a free option. Your losses are limited and your gains all but guaranteed. This is not my view, as an aside, as much as a description of what the market currently believes.

In other words, the market thinks the re-opening of the economy is real and durable and will continue apace. The market believes a vaccine is coming very soon. The market believes there is tremendous pent-up demand. And the market has run the numbers and sees the surge in liquidity and stimulus having massively dominated the economic losses from the virus and the shutdown. And not just that, but the damage to the economy and earnings was temporary and that the stimulus, not only larger in scope, will be ongoing well into the future. From an election standpoint, the market sees Joe Biden as having no chance. Finally, while there was a time when 108,000 dead and 1.87 million coronavirus cases would have seemed unfathomable, but once again, market participants really are viewing numbers like these as “less scary than anyone thought three months ago” and oh, so passé. Indeed, I continue to also hear how “there’s no second wave!” when we are now up to a dozen states that are seeing the COVID-19 case count rise again. That includes Florida, which just began to re-open its theme parks. Nobody seems to care (outside of the people getting infected, that is).

Now, if you believe that narrative, it is clear what you have to do. You have to buy those cyclical value stocks that lagged furthest behind. After all, even with the rally off the lows, the average value stock is still down 26% for the year while the average growth stock is up close to 6%. Only once before (in the 1999 dotcom mania) has the performance gap been so wide over a five-month span. The fifty most expensive stocks are up 11% year-to-date while the fifty with the lowest valuations are still down 17% (and trade at a 13x P/E multiple). In fact, I saw in the weekend WSJ another factoid, which is that 73% of the broad Wilshire 5000 is still negative return-wise year to date.

So, if the retail stocks are back to a new high, and that is an accurate description of the consumer landscape, then sure the mall REITs have a lot of catching up to do. Hotels, casinos, energy, regional banks, and autos are still in bear market terrain from where they are relative to their highs – I mean, if retail is already back to the highs and restaurants closing in, and you are a believer in the V-shaped recovery, my suggestion is to extend your bullishness to those other areas that have still lagged so far behind in this value trade.

Of course, we have to also take a big picture view here. Yes, yes, the S&P 500 has soared 40% in short order. It did the same thing twice in the early 1930s. If memory serves me correctly, the Great Depression didn’t end until 1941 with the onset of WWII and the

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

secular bear market that began in the Fall of 1929, did not in fact end until 1954. And that included many a tradeable rally along the way. Then again – we didn't have central bankers using the stock market as a de facto third policy objective or a President using the stock market as the primary yardstick for success.

I continue to like Treasuries and gold as ballasts in the portfolio and the recent price pullbacks offer up some nice entry and re-entry points. These are insurance policies against things going possibly wrong with the newly-found ebullient forecast. Nothing goes in a straight line and we saw time and again this past decade how the instability of excess leverage can affect the market in a negative way – much of 2011, the spring of 2013, almost all of 2016 till the election, then the fourth quarter of 2018, were all periods of turbulence. **The bond-bullion barbell provides stability in the portfolio when we enter rough seas.** Maybe Powell, Mnuchin and Trump (add in Abe, Kuroda, Lagarde and now even Merkel to the mix) have managed to finally have the public sector take full control over asset valuations – this, of course, is the curse of the bears.

The artificial has dominated the organic, and that is how in the span of just three months we have seen the forward P/E multiple soar from 13x to 23x – the highest since the tech bubble in 2000. Indeed, in three months we have gone to a valuation on the market that typically spells the end of a bull market as opposed to the onset of a new bull market. The response I get from colleagues who called the market correctly in these last few months (and they deserve a tip of the hat), is... “who cares?”. Or I hear “valuations only matter when they do.”

Okay – I've been around long enough to know when complacency has reached an extreme and we likely are there. So, I continue to resist TINA and FOMO and all the calls to “not fight the Fed”. I think the downside risks are real and not priced in at all, even if there is a general belief that public officials will put a floor under markets at all times. That is likely true – but we now are closer to the ceiling than the floor, and multiples on some future normalized and unaffected earnings projection look far too pricey for me. It is true that interest rates remain low, but they too are being manipulated by central banks and even if not, what they suggest is a future of a deflationary output gap that will crush profit margins and/or a lingering savings glut that will impede the very V-shaped economic recovery that the bulls seem to believe is dangling in front of their eyes at this moment.

Within the fixed income market, there is a glaring anomaly and opportunity right now. The muni bond market has rebounded far less than is the case for the market for corporate bonds. BBB-rated munis trade with an average yield (and nontaxable) of 3.5%. The BBB-rated muni market has only retraced 20% of the 200-basis point yield backup... and is trading at levels when the 10-year T-note was 2%-2.25%. They now trade at a 50-basis point premium to BBB corporates, whereas historically they trade at a 50-basis point discount. **This is a very rare occurrence and one that should be taken advantage of – all the more so when you consider the relative default risks.** In fact, the BBB-ranked munis trade at a huge 110-basis point

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

Economic Research
for Informed Investing

premium to A-rated comparable and nearly 200 basis points over AA-rated alternatives. That is a juicy spread and set to compress if (likely once) this next fiscal package comes to fruition.

Speaking of the Treasury market, while we may well face a future down the road of stagflation, it is outright deflation that is the clear and present danger. And so it is with great amusement to have watched the bond market community reprice the landscape to the extent it has – the 10-year TIPS breakeven has ballooned to 127 basis points from 50 basis points in mid-March. **Even if we get a V-shaped recovery, we are going to be stuck in a deflationary pricing situation for a very long time. When you have one in every five Americans either unemployed or underemployed, even after what was apparently a blockbuster jobs report, there simply is still too much idle capacity to be bidding up inflationary expectations at the moment. That's why Treasuries are a very good buy right now.** Growth may well come; inflation isn't for a long time. And yet it has been the inflationary component of nominal yields that has been the driving force in this latest Treasury market selloff. This faulty assumption will end up triggering a renewed move back to lower-yield activity, along with evidence that there is not going to be any follow-through from the Q3 re-opening-led economic rebound.

THE GREAT RECESSION REVISITED

The theme is “The Great Recession” and the tag line is “Business Will Not Be As Usual,” and a three-month rally that historians will look back on as basically a blip on a screen has not altered this big picture perspective. I remain of the view that the level of conviction I have in anyone's forecasts on the economy or the markets right now, including my own, is several standard deviations below the norm. I feel that I'm in pretty good company when you consider that more than a third of the companies who've reported their quarterly financial results so far have pulled their full-year guidance, which is something we haven't seen happen since the Lehman Brothers collapse in 2008.

As it stands, the second quarter hole in real GDP is getting bigger and bigger and across every country in the world. Looking at what is being built-in from all the data, it seems like we are in for an unprecedented 50% tailspin for second quarter real GDP – and remember that this follows a 5% decline in the first quarter, so for everyone who is saying they can't wait to get back to the pre-pandemic economy, be careful what you wish for. Like I said, the hole we have to dig out from is just getting bigger, and the economic math is daunting because to recoup a 50% plunge in GDP means it has to then surge 100% to make up for the deep loss. At the same time, we also need to consider that all these government programs are only bridge income-replacement support mechanisms. That's all they are for – to fix a leaky boat. Keep in mind that this is no FDR New Deal stimulus, when we built the Golden Gate Bridge, the Hoover Dam, the Lincoln Tunnel and Route 66 – this is not fiscal stimulus with any future multiplier impact or payback, it's simply government-assisted life support.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

Meanwhile, watching the stock market today is like watching a clown blowing up a balloon knowing the inevitable, though I have to say it is impressive to see the degree of confidence the equity market bulls have at the moment. **All I can say is that either the investment community sees the Fed going beyond high yield corporate bonds and actually coming in to buy stocks at some point, or investors have this view that what we are seeing is temporary; that the economy is going to bottom this quarter with the re-openings, and that even if things don't back to normal completely, they will by just enough to warrant the multiples being where they are.**

It's hard to handicap what the Fed is going to do, that much I will admit. I used to talk about them going into the junk bond market and bailing out the fallen angels, but in truth, I was saying it in jest. I won't for a second assume that the Fed doesn't have the stock market on its mind at all times, and Powell has proven to have been as much a back-stopper and market manipulator as Greenspan and Bernanke. I'll be the first to acknowledge that fighting the Fed is a futile game. **At the same time, however, what central banks everywhere have done is make it next to impossible to appropriately price risk and they have created tremendous moral hazard by bailing out poor managers of risk.** But the academics will tell you that this is what it takes to save the system... another financial sector bailout, the last one was about banks, and this one was about credit hedge funds.

It would be one thing if this was 2008 and 2009, when it finally took a ringfencing around, and a recapitalization of, the banking system to put in the lows.

It would be one thing if this was about mopping up the tech sector's excess capacity, which finally helped to establish the lows in the fall of 2002.

It would be one thing if all we had to do was wait for the RTC to absorb the commercial real estate mess created by the Savings and Loan crisis back in 1990 and 1991; or simply waiting for Paul Volcker to finally slay the inflation dragon in the late summer of 1982.

This current situation is all about when, and if, a treatment or vaccine come to the fore. But that could take months, it could take quarters, it could even take years.

It is definitely not all about re-opening the economy because what is going to matter most is demand. There is no renewed hiring cycle that brings the unemployment rate back down without demand. Demand is the key.

But, I can tell you that the stock market is behaving in a way that it seems to be expecting a vaccine to have successfully completed all its trial phases and be proven to have been safe and effective, and I am talking about this Fall. I say that because of the sort of value and cyclical stocks that have taken leadership, very recently mind you, and how the market is completely ignoring these heightened tensions between the U.S. and China and what is happening in Hong Kong. Let



Rosenberg
Research

Economic Research
for Informed Investing

alone the riots and demonstrations, which go beyond just police brutality but also speak to the extremes of income and wealth disparities, which I can tell you will emerge as the number one economic and political issue heading into the November elections south of the border. **Things that a year ago would have been sending the stock market into a tailspin are now being ignored, because it is all just about a vaccine.**

I think that there is also a lot of excitement in the marketplace around the re-openings that are now happening in most parts of the world and in all fifty states. And while the economic numbers, the high frequency weekly and daily trackings, are showing less negative readings, the economy is still struggling. It isn't just about re-opening the economy, because social distancing is going to impair capacity in practically every industry, including the consumer cyclical service sectors that have been rallying sharply lately, but what is going to matter most, again, is demand.

The daily mobility trackers look exciting to the bulls. And all the pictures in the media show lineups. But the reality is that restaurants with 25%-50% capacity will go bust, even after they rationalize on space expenses. Not just that, but a Cowen survey of 2,500 U.S. households in May found that three-quarters plan to dine out less frequently as before or avoid restaurants altogether. Data from OpenTable show that its booking gauge has improved since the lockdowns ended, and yet reservations are still down 80% from where they were a year ago – well, that receives very little mention. Occupancy rates in the hotel industry are the grand total of 32.4% – yes, up from the lows of 21%, but half the pre-COVID-19 level of 61.8%. RevPAR (or revenue per available room) is still down 74% from a year ago even with the modest improvement in the past week or two. Sequential improvement only takes you so far – the key will be for every such industry to shift into profitability. **In any event, it's all about what passes for “good news” today.**

The Chicago Fed conducted a survey and found that three-quarters of firms say the U.S. economy needs at least a year to fully recover from the pandemic. There were 670 respondents in the poll and half told the Chicago Fed that the recovery will take between one and two years to develop. The other half was split between a recovery in less than a year or one that would take more than two years. The report stated that:

“Many of the small businesses we heard from – especially those in the entertainment, tourism, recreation, restaurant, and retail sectors – are in danger of financial distress... Many businesses are facing very difficult challenges that are unlikely to go away quickly.”

You tally up these sectors and before the crisis, they supported 32 million jobs, or about a third of the private sector workforce, and it looks to me as though half of them are not going back to their old jobs.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

And I'm not sure many people understand that amusement parks, airlines, restaurants and hoteliers cannot stay in business at 50% capacity (or even 75% in the case of restaurants). I think people have to understand that for cyclically-sensitive consumer-oriented sectors like restaurants, they spend 30% on labor, 30% on rent and 30% on food — they have a 10% margin. Good luck with partial re-opening and social distancing.

Let's look at some of the other survey data. A Bankrate survey found that 55% of Americans still think it's too early to re-open the economy; 43% say they will be spending less than they were pre-COVID-19. Only one-third said they will feel comfortable visiting any establishment within the first month of re-opening in a classic "you first!" message. As it stands, the U.S. Chamber of Commerce said that 25% of small businesses have already shut down. The AARP reports that 53% of American households have no "emergency savings" — so I don't think they're heading on a cyclical spending spree any time soon, even if they could. A Washington Post/University of Maryland poll shows that only 56% of consumers across the nation intend to shop at the supermarket, which I suppose is a continuous bullish data point for delivery services, but that's about it. Just 33% say they are comfortable entering a retail store. And a mere 22% say they are willing to dine in a sit-in restaurant.

A YouGov/CBS poll finds that 71% of Americans have zero intention of heading out to a restaurant or bar despite all these other feelings of being forlorn and claustrophobic, and 85% say they wouldn't get on an airplane even if they could.

All these polls say basically the same thing — it will not be "business as usual," as the bulls will try and convince you, and the best we can hope for is a partial recovery. I mean, at best. What we have on our hands is a vertical down economic decline with job losses an order of magnitude higher than anything we have witnessed since the Great Depression. **So, even as the stock market is telling you it has it all figured out, I can assure you that what we face at this very moment is a very uncertain economic future. And unfortunately, most of the longer-term risks are to the downside.**

We are in a depression - not a recession, but a depression. And I think the dynamics of a depression are different than they are in a recession because depressions invoke a secular change in behavior. Classic business cycle recessions are forgotten about within a year after they end. At a minimum, depressions entail a prolonged period of weak economic growth and widespread excess capacity and deflationary pressure and a wave of bankruptcies. **Asset markets, as I see them, still don't reflect the economic depression but do reflect a V-shaped or even a U-shaped recovery which, I think you can tell, I believe is nothing more than pure fantasy. The best-case outcome is an L-shaped or backward-J shaped recovery.** And to repeat, that's the best case. That's what I would call a slow "jobless recovery" made possible by continued and constant support from gaping fiscal deficits and central bank liquidity.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

Fundamentally, as I said at the outset, this economic crisis will continue until we control the spread of the virus – in whatever form that happens. That’s the bottom line. And as this insolvency phase heats up, I expect a re-testing of the lows in the stock market. And so, as I hope for a post-lockdown bounce that ends the deepest part of this recession, the best case from there is a painfully slow, grind-it-out recovery. Again, to repeat, when you’re drawing that probability curve of all possible outcomes, that is the best case.

With that in mind, I want to bring your attention to a San Francisco Fed report that was published in March, a report well worth a look titled, *Longer-run Economic Consequences of Pandemics*. In a nutshell, the economists studied the medium to long-term effects of major pandemics – fifteen in total dating back to the 14th century. **The major finding – a secular shift towards greater precautionary savings.** At the same time, investment demand also tends to decline. As such, the impact of the great historical pandemics of the last millennium has been to exert lasting downward impact on the natural (“neutral”) rate of interest – in fact, 150 basis points lower, typically, than if the pandemic had not occurred. **This is why we can’t rule out negative interest rates, which by the way, are being discussed in the U.K., and especially when you consider that the starting point this cycle on bond yields was already a fraction of one percent.** So, all of a sudden, today’s 1.6% yield on the long bond could end up looking like a bargain, as it did at 2.4% at the turn of the year. Because of the importance of convexity at these very low yield levels, the total return in the long bond so far this year is +23%; and yet when everyone crows about how the Nasdaq is up 8% for the year, nobody seems to mention what the total return in long-dated Treasuries have been. **In fact, the total return in the 30-year Treasury the past year is 28% against 13% for the S&P 500, so it is true that bonds have more fun. We’ll keep that our little secret.**

Let me read to you the conclusion of that San Fran Fed report:

“Following a pandemic, the natural rate of interest declines for decades thereafter, reaching its nadir about 20 years later. At about four decades later, the natural rate returns to the level it would be expected to have had the pandemic not taken place... history shows that real neutral rates can be depressed for 5 to 10 years.”

If that isn’t an advertisement for physical gold, I don’t know what is.

All that said, I do think from an economic standpoint, we are right in the eye of the storm and there will be an economic recovery – I’m not saying that won’t happen – but the recovery will be muted and frustratingly slow, and it could take at least three years before all the economic damage from the virus and the lockdowns are recouped, whether it’s output, income or employment we are talking about.

The current surge in the deficit is not about shovels in the ground with some hope of future multiplier effects on the economy – it is simply

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

a transfer from some future taxpayer to today's household and business who are out of work and for some reason had no cash, savings, or liquidity to get through even a few months of shutdown for public health purposes. That says a lot right there. So, who paid for the fiscal largesse in the 1930s? Guess who? Corporate income tax rates from 1929 to 1939 rose from 11% to 19%. Capital gains tax rates rose from 12.5% to 22.5%. And top personal income tax rates went from 24% to 63%.

Think about this too. FDR never ran a deficit greater than 7.5% of GDP during the Great Depression (we are going to 20% this year), and by 1938, five years after the New Deal was unveiled, the government was back in balance. The government debt-to-GDP ratio peaked that year (prior to WWII) at 43%, and the CBO just told us the federal government debt ratio is going to 101%. Taxes back then were not a dirty five-letter word, complaining about having your taxes raised in the 1930s was like wearing a red dress to a funeral, because there was a concept that the upper classes understood called "shared sacrifice", and there was productivity and revenue payback from that "stimulus" as opposed to today's "cash transfer."

Then we have to consider, when we get to the other side, the massive government debt we will have built up and how that, along with even more bloated central bank balance sheets, get dealt with. Will the debts get monetized or not? Again, it is interesting to see the Bank of England openly heading in that direction.

Will tax policy have to change as it did to defray the cost of fighting the Great Depression? What the world looks like when the crisis ends is truly anyone's guess but I will say with 100% clarity that it is going to look lot different than it did before. Not just the question over government policy, but at the individual level, months of isolation and distancing, and fear of a return of the pandemic are going to fundamentally alter lifestyles. There will be a profound influence not just on the way we live, but how we conduct ourselves in our personal and commercial lives.

For example, working from home is certainly going to be a more dominant force, with obvious negative implications for commercial real estate but positive implications for internet infrastructure, computer hardware and video conferencing. There is going to be a sharp reduction in travel to work, travel in general, and this means fewer cars on the road. There is nothing here that is very good for the auto sector, not just office REITs. **But there are some bullish themes that emerge, too, as we go into an era of elevated personal savings rates where people are going to focus on what they need, not what they want.** It was very interesting, behaviorally-speaking, to see what consumers have spent their money on in the past few months of lockdown besides canned food, toilet paper and booze – things like garden supplies, bread makers, jigsaw puzzles, anything related to e-commerce, cloud services and wiring up your home to become your new office.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

*Economic Research
for Informed Investing*

Delivery services have now become an essential, so here is a budding bull market right there for Amazon and any business model that copies it. I should tack on grocery chains with online services coming out of this as a winner. **So, the shifting behavior that is already taking place tells me to focus on consumer staples and on other areas of the market, health care and even big tech, that have become essentials. Microsoft has become a utility. One could argue that Amazon has become a utility. One could also argue that Google has become a utility. And it's apparent to me that you want to have exposure to health care because this clearly is an under-invested area and will, without a shadow of a doubt, become less regulated in the future.**

There are other ways to hedge and diversify such as REITs, which have stable income, including multifamily REITs and industrial REITs benefiting from the Amazon effect. Low interest rates make their stable yield more attractive and the cap rates will remain lower for longer. **So, I may not be bullish on the market, but you can certainly create your own index that fits the theme I'm describing.**

An investment theme that also deserves close consideration that could combine all the attributes of safe income, value and defensive growth, is the Dividend Aristocrats index. This is a perfectly appropriate strategy for the investment world I see unfolding, one where dividends become scarcer and where the reliable payout growth becomes more important than the yield – my advice here is to focus on the stability of the dividend, not the yield.

Which brings me to one of my key investment ideas for the current state of the world: Gold, as in physical gold, is a very good hedge against the instability that the extremes of deflation and inflation bring. If there is deflation, interest rates will remain low or go negative, making the opportunity cost of holding gold nil. If there is inflation, gold will do well as a store of value. Lastly, all this central bank alchemy has led to ever increasingly unstable markets and gold will do well against this backdrop.

It can't possibly be lost on anyone that what we had was a health crisis morph into an economic crisis, which then somehow managed to morph into a financial crisis that was ten times worse than anything we saw in the Global Financial Crisis and forced the Fed to probe the outer limits of monetary intervention to the point where it had to backstop CMBS, investment grade bonds, the muni market and high yield debt and expand its balance sheet more in three months than it did cumulatively in a six-year period from December 2007 to November 2013.

We simply refuse to stop these cycles of redressing debt crises by adding more debt, which merely compounds the adverse effects from the recession that is inevitable, and yet at the peak of the cycle nobody ever seems too prepared for one. And even in the household sector, while there was no bubble this time in mortgages, there was clearly a huge bubble in autos, credit cards and student debt. This is why it's going to be a depression, because what comes next is a

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

Economic Research
for Informed Investing

secular change in attitudes towards credit and towards savings. I mean, seriously, that over half of American households didn't have enough cash on hand to even get through three months of a job loss is quite remarkable when you consider we went into this mess with a 50-year low 3.5% unemployment rate.

Not to mention the corporate sector where, for some reason, the word "liquidity" became a dirty nine-letter word this past cycle. Now every business has working capital they have to cover with a fraction of last year's cash flow. And this got me thinking about how the future will be one of treating "savings" as sacrosanct and that Friday's number represented a real secular shift with that 33% personal savings rate for May, something we haven't seen since the Great Depression. **By itself, this is deflationary on the demand front, but we also have a future of a sclerotic or inelastic aggregate supply curve that will ensure a future of weak productivity, more regulation, and cost-push inflation.**

So, I think a strong case can be made if you have a three-year-to-five-year view that stagflation is going to emerge as a new secular theme coming out of this crisis once demand conditions stabilize. Think of a future with massive public deficits, debts, and government intervention and regulation. And a world of reduced globalization and more localized supply chains, an end to just-in-time inventories, and what the future holds for taxation.

So, globalization slows, or stalls here, as does the cost-saving strategy of just-in-time inventories, because we have seen in real time the importance of having stockpiles on hand. And the implications of everything I just mentioned means that for every unit of production, the global corporate cost curve goes up in a secular fashion; and since for a while we will still be operating with a deflationary output gap for an extended period of time, this in turn means more compressed profit margins; and this, at a time when share buybacks will be **slowed in favor of retention of cash on business balance sheets.** **Maybe Fed liquidity will continue to prop up the markets, but the fundamental picture I see is very weak outside of the specific investable themes I've put in front of you.**

And the laundry list of outcomes I just cited all comes at the cost of a higher corporate cost structure, compressed margins, which again leaves me wondering why so many people who focus on normalized earnings think there's no impairment to that curve. Not to mention how China's relations with the rest of the world will undergo a major transformation. And not just China, but one can expect the already rising tide of nationalism, populism and isolationism to gain more momentum globally. **From a really big picture standpoint, we come out of this with a world that is going to be smaller. A world that is more nationalistic, much more protectionist than before, and was a trend that was already in motion from the trade conflicts that started about a year-and-a-half ago.** There will be more regulation and government intervention, and global supply chains becoming more localized, especially in vital areas of national interest like medical supplies, food supplies, and even semiconductors.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

And I should probably add socialism to the mix, knowing what history has to say on what happens when the economy enters a crisis with unprecedented income and wealth disparities and where the ones responsible for the “financial plumbing” get bailed out ahead of the “little guy”, and it was the little guy, or gal, that had his and her thumbprints all over the past few detonating jobs reports.

At the risk of sounding like an economics 101 professor, what I am describing here in the future, maybe just a case of looking at the forest past the trees, is a sclerotic or inelastic aggregate supply curve that will ensure a future of cost-push inflation even with lingering weakness in aggregate demand, but that is probably at least three years away. But that is what stagflation is — higher inflation even with weak economic growth. So, I think at some point we will be dusting off the 1970s investment playbook. Either way, physical gold comes out a winner, and is my highest conviction call, if for any other reason than it is a currency that is no government’s liability, and its production growth runs at a pretty reliable, and constant, 1% annual rate, whereas the production of money right now is running at 30%. I kid you not, that has already taken out the 20% growth peaks in the 1970s and 80s when we were watching Happy Days, playing Trivial Pursuit, and listening to disco music.

As for the stock market, and I apologize if I insulted anyone with my clown reference earlier, because maybe this pattern we are seeing is just a repeat of what we have seen in the past. Let’s dust off Bob Farrell’s market rules to remember and go straight to #8:

“Bear markets have three stages — sharp down, reflexive rebound and a drawn-out fundamental downtrend.”

Every bear market looks the same and this one is no different. We had the severe leg down as everyone thought this was going to be a repeat of the Black Death. Now for the past three months we have been in the throes of massive policy stimulus and certainly a tradeable rally, but every bear market rally is very tradeable and they can last several months. Never mind the five-month 48% bear market rally from November 1929 to April 1930, we saw this same thing in 2002 and again in 2008. **Trade it, but know when to fade it because the third stage of Bob Farrell’s Rule #8 is coming as sure as night follows day. A little history can sometimes go a long way.**

In any event, everyone knows I think the stock market (financial assets in general) have become a casino with no more true price discovery or risk assessment; because Jay Powell is the dealer handing out chips for free. What’s been created is totally one-sided, “heads you win, tails we bail you out” psychology. **But nothing the Fed does can distract me from assessing true intrinsic value — the Fed may have your back, but it can’t stop anyone from figuring out what the risks and rewards really are.** From my lens, high yield is not high yield when the HYG ETF yields 5% to 6%, given the default wave that’s coming. I mean — May was a horrible month for credit downgrades. As I have said many times before, it is not called high spread; it is called high yield. You need more yield to take on quasi equity risk.

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Economic Research
for Informed Investing

Relative value becomes meaningless when the Fed is buying everything but equities. High yield has averaged 9% over the past three decades and 13% in recessions; investment grade has averaged 5% in the past and about 6.5% in recessions. Bottom line is that you have to have a hurdle rate for investments, and they have been totally distorted.

At a minimum, investment grade should be 5-6% between yield and capital appreciation and spread compression potential. High yield should be at least 8% since it's quasi equity. But "rates are zero", so investment grade is at 2%, most of high yield is at 5% (under generous assumptions) and I truly find that amazing. **Relative value against a broken price discovery system become the crutches upon which the weak rely on to justify absurd behavior. But the Fed is making it hard to own risk assets right now with any degree of moral, intellectual, or economic based grounding.** High yield is totally mispriced. Just remember, it is called high yield, not high spread – to lend to a single B you need 8%, not a 600-basis-point spread on zero rate Treasuries. Actually, when you think about it, spreads in a zero rate Fed induced rally become less relevant.

You need to price risk absolute and absolute yields are stupidly low right now, so I say let the stupid buy it. So, people say, "if I am buying expensive high yield, why not just then buy equities with more upside?" and they do it; which has been the story in the equity market for the past two months. Then they say, "if I am buying equities, why not just buy the COVID-19 names and get even more upside?" Ahhh, the value cyclical trade is back, right! So, they buy cruise ships, retail, banks and energy. But why not go to the 40 million newly unemployed and ask them if they're going on a cruise ship or airplane any time soon and see what they say?

One last thing. Let me just say that in these riots we've been seeing, many, not most but many, are coming in from outside these cities and are not local civil rights groups. These are far left groups, meaning these groups are using George Floyd's death to protest and attack on their far-left agenda. And to anyone that knows anything about history and sociology, a disproportionate number of African Americans have been impacted, sick and killed from COVID-19. More African Americans were likely laid off and furloughed as a result. Aided and abetted by the Fed, the wealth gap just keeps getting bigger and bigger. And so, here we have the makings of a backlash – probably going to be Occupy Wall Street on steroids.

Expect President Trump to ratchet up the fear factor with middle-class and upper middle-class rhetoric during election cycle around the "masses". And then expect Joe Biden to provide an extremely progressive left-leaning type of platform. We'll see what happens in November and it's too early to be handicapping anything, but Trump's approval rating is way down in the past two months to 42%. Biden is leading in some of the key battleground states which is incredible, and I see in the betting markets that the Senate is now a toss-up to flip Democrat. We'll see by Labor Day when there is no vaccine, no V-shaped recovery and polls suggesting a Democratic sweep just how

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

Economic Research
for Informed Investing

bullish Mr. Market is at that juncture. Something tells me Powell won't be taking any part of the summer off.

Everyone is comparing the current situation to 1968 and maybe that isn't a bad thing to do except for the fact that the music was a lot better back then. And when you go back to learn from history, go back to 1968 and you'll see that we were at a real inflection point from a financial, political, economic and social perspective. From a risk standpoint, it marked the end of a 14-year bull market and the onset of a 14-year secular bear market. The latter coinciding with escalating geopolitical tensions, beggar-thy-neighbor currency policies, Fed-induced inflationary strategies, massive fiscal deficits, reregulation, heavy government intervention in the economy, and an acceleration in labor power which impinged on profit margins for years to come.

In other words, stagflation, the bitter enemy of financial assets, but a friend to real tangible assets, like precious metals, and I would throw real estate into that mix too, maybe not office or retail, but residential and industrial for sure.

TEN PROBLEMS WITH THAT MAY JOBS NUMBER

1. The initial jobless claims data show the total number of people receiving benefits at 30 million. Yet the Household survey only shows a total number of unemployed at 21 million. **That's 9 million collecting benefits but not showing up in the official "unemployment" count – how is that possible?** Every month going back to when the records began, the level of unemployment has always exceeded the level of claims – and usually by a factor of two (because normally, not everyone who is unemployed is necessarily still eligible for support). Go figure. Does make one wonder about conspiracy theories.
2. **The irregularities in the data were incredible.** Even by the BLS's own admission, there were 4.8 million people who reported that they weren't unemployed when they actually were unemployed. That means the unemployment rate was 16.3% in May, the same level it was in December 1939. For the history buffs and depression-deniers out there.
3. **The number of permanent job losses jumped 295k in May and by more than one million in the past three months – we haven't seen that since the 2008/09 Great Recession.**
4. The Household survey only received a response rate of 67% – the sample size normally is 82%. That makes the report even more spurious. The Payroll survey also

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

- was plagued by a lower-than-normal response rate in May.
5. It's interesting that the Dow transports have been soaring lately in the stock market and yet the group let go 53k workers last month.
 6. There were net downward revisions of 882k in the March-April period — there was a time when that alone would have made the front-page news.
 7. In reality, only one-tenth of the 20 million-plus carnage of the prior two months was recouped in May.
 8. There were 10.887 million people working part-time for “economic reasons” in May, up from 10.663 million in April. It has to be understood that these are numbers that are at least double what typifies a normal economy (remember what that looked like?)
 9. The BLS had the temerity to assume that 227k jobs were created by the net creation of new businesses (the “birth-death” model). Give me a break.
 10. When you look at the aggregate hours worked index, barring a productivity miracle, it looks as though real GDP contracted at a 46% annual rate in Q2.

THERE IS NO V IN NUMBERS (BUT THERE IS A U)

Now that we've established the lack of veracity in the Friday jobs data, let's assess just how well the U.S. economy has been doing into the first month of the “re-opening”:

- OpenTable reservations (June 6th): -74% YoY
- Dallas Fed mobility/engagement index (May 29th): -59% YoY
- Steel production (May 30th): -36% YoY
- Coal production (May 30th): -34% YoY
- Railway carloadings (May 30th): -18% YoY
- NY Fed's weekly economic index (May 30th): -10% YoY
- Lumber production (May 23rd): -10% YoY
- Electrical output (May 30th): -7% YoY

I should add that the modified NY Fed recession model is now up to 46% odds of another recession. This was where it was on January 10th, just ahead of this past recession that nobody seemed to see coming. On March 23rd, the recession odds stood below 30% so even as the stock and credit markets have ripped, more on policy stimulus than on true earnings and balance sheet fundamentals, recession risks have been on the rise right in front of our eyes — and more than double the historical norm of 20%. This means a 22x forward multiple

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.

Rosenberg
ResearchEconomic Research
for Informed Investing

and 6% coupon on high yield corporate bonds offer investors poor protection against a growth relapse.

And here is what the home-based COVID-19 impact is telling us where things are in terms of employment and business openings against the pre-pandemic benchmarks:

- Beauty salons: employment -51%; business openings -49%
- Leisure/hospitality: employment -37%; business openings -35%.
- Restaurants: employment -36%; business openings -26%.
- Transports: employment -26%; business openings -28%
- Retail: employment -21%; business openings -23%

The economy has a massive hole to climb out of. Unprecedented. And risk assets are way overpriced for the macroeconomic climate we are in and are likely to be in for some time yet.

HOW ABOUT AN F-SHAPED RECOVERY – AS IN FRUGALITY?

We have long said that what makes a depression different than a plain-vanilla recession is that, with the former, attitudes towards debt, savings and balance sheets undergo a secular shift, whereas with the latter, nobody even remembers the downturn a year after it ends. **There is more of a permanent change in behavior following the sort of shock we have endured in the past several months.**

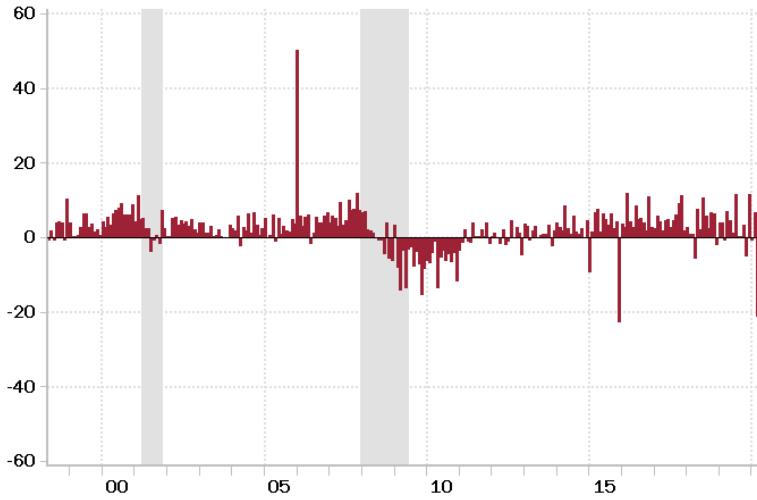
Well, we saw this first-hand both in March and April – early signs of a change in attitudes towards caution and debt paydown. U.S. consumer credit contracted \$68.8 billion in April and that followed a \$6.8 billion decline in March for the second steepest decline on record. Fully \$58.3 billion, or 84%, of that credit contraction last month was in credit card balances – and that came on the heels of a \$21.5 billion net paydown of balances the month before. In fact, the caution was setting in before the pandemic, as consumer credit outstanding has now declined in three of the past four months – between January and April, the contraction has been unprecedented: at a -24% annual rate.



Rosenberg Research

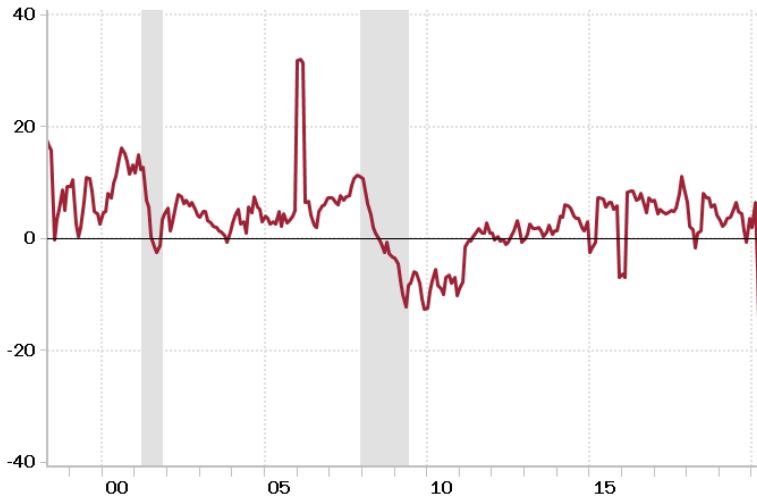
Economic Research for Informed Investing

CHART 3: Revolving Consumer Credit Outstanding United States
(month-over-month change; \$ billions)



Shaded regions represent periods of U.S. recession
Source: Haver Analytics, Rosenberg Research

CHART 4: Revolving Consumer Credit Outstanding United States
(3-month annualized percent change; \$ billions)



Shaded regions represent periods of U.S. recession
Source: Haver Analytics, Rosenberg Research

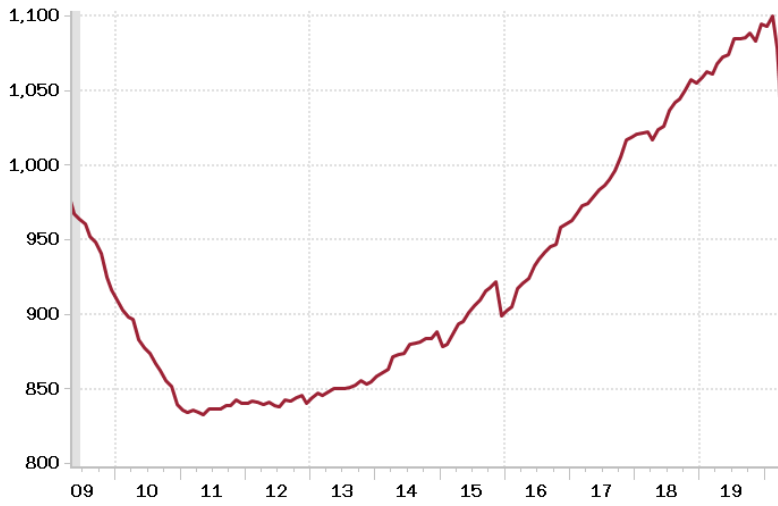
This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg Research

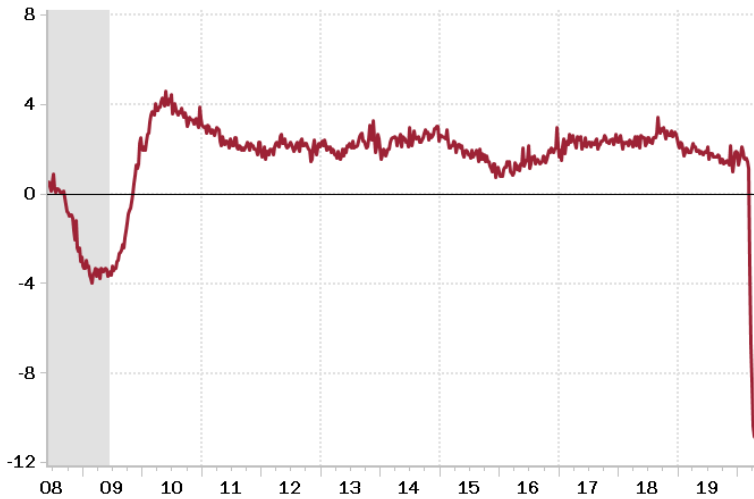
Economic Research for Informed Investing

CHART 5: Revolving Consumer Credit Outstanding
United States
(\$ billions)



Shaded region represents period of U.S. recession
Source: Haver Analytics, Rosenberg Research

CHART 6: Weekly Economic Index (Lewis, Mertens & Stock)
United States
(index; scaled to year-over-year GDP growth)



Shaded region represents period of U.S. recession
Source: Haver Analytics, Rosenberg Research

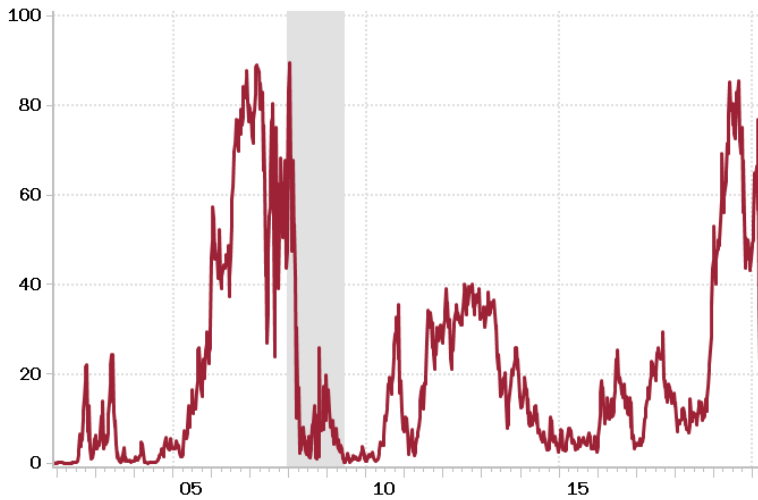
This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Rosenberg
Research

Economic Research
for Informed Investing

CHART 7: Probability of U.S. Recession 12 Months Ahead as Predicted by Near-Term Treasury Spread
United States
(percent)



Shaded region represents period of U.S. recession
Source: Haver Analytics, Rosenberg Research

DON'T FIGHT THE FED!

So, I was talking over the phone to a long-time Merrill colleague who turned into a highly successful hedge fund manager — successful enough to retire before hitting sixty years young.

Here's how the conversation went:

Dave: “The S&P 500 is back to where it was last October when real GDP growth was 2%. Now it's going to be -50% this quarter on top of -5% last quarter.”

Friend: “Who cares? Don't fight the Fed.”

Dave: “You don't find it strange that the unemployment rate then was 3.5% and today it is 13.3%? And the stock market is the same level now as it was then?”

Friend: “The Fed's balance sheet was \$4 trillion then and over \$7 trillion now. Don't fight the Fed. “

Dave: “The industry-wide CAPU rate, the root of corporate pricing power, is 65% today compared with 77% last October. How can the market dismiss this massive deflationary gap?”

Friend: “The market isn't fighting the Fed. You are.”

Dave: “Okay, let's go to earnings. Last October, the consensus was projecting \$180 of operating EPS for 2020. Now that's down to \$128. For 2021, last October, the consensus was \$196 and now it's \$164.”

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



Economic Research
for Informed Investing

Friend: “The market doesn’t care. It sees those 2020 and 2021 losses as being recouped quickly with a V-shaped durable recovery. Besides, multiples deserve to be where they are because of the Fed. Don’t fight the Fed.”

So, there you have it. It’s that simple. Don’t do any homework. Don’t do any fundamental analysis. Don’t bother to even learn how to invest. Don’t waste your time enrolling in the CFA program. Just don’t fight the Fed.

I will say this much. **When the S&P 500 was sitting at today’s level last October, the forward P/E multiple was 17.3x. Today, it is 22.5x. That means that investors are paying 30% more for the earnings stream in a backdrop that surely is more uncertain than it was then. Alas, I forgot the logic of today’s investing environment – (i) valuations don’t matter and, once again, (ii) don’t fight the Fed!**



Rosenberg
Research

*Economic Research
for Informed Investing*

HOW TO INVEST IN THE POST-CRISIS “HOMEBODY” ECONOMY

For those with long investment horizons, I can tell you almost without a shadow of a doubt where the future demand growth is going to be. What the crisis has accentuated is this trend towards “cottage industries”, where working at, and being closer to, home is going to be a major investment theme (not to mention in high demand during this period when we have already become “homebodies”):

- Home-office technologies (cloud)
- Video streaming (home entertainment)
- Online retailers
- Health care services (bio tech and pharma)
- Utilities/residential REITs (fat yields and money-good)
- Semiconductors
- Delivery services
- Windmills, battery storage, solar panels on rooftops
- Hygiene producers
- 3D printing manufacturers
- Robotic technologies
- Telecommunications (with deep financial strength)
- Treasuries/municipals/A- and BBB- (high) rated corporate bonds
- Gold/precious metals
- Food supplies
- Consumer staples

This report is prepared for the exclusive use of the individual Rosenberg Research and Associates Inc. subscriber to whom it was delivered. Sharing, redistributing, retransmitting or disclosing this report in whole or in part, or in any form or manner, without the express written consent of Rosenberg Research and Associates Inc. is a violation of our Terms of Use and will be prosecuted to the fullest extent permitted by law.



MEET THE TEAM

ECONOMICS

David Rosenberg
Chief Economist & Strategist

Andrew Hencic
Senior Economist

Marius Jongstra
Economist

Ellen Cooper
Economist

Julia Wendling
Junior Economist

OPERATIONS

Enrique Flores
Chief Marketing Officer

Marcel Aulls
Vice President, Sales

Dana Habib
Office Manager

For questions or enquiries please contact us at information@rosenbergresearch.com



IMPORTANT DISCLOSURES

This report comments on the economy and capital markets. The opinions are those of the author as of the date of the report and are subject to change without notice. Rosenberg Research & Associates Inc. (Rosenberg Research) will not necessarily update the report in the event facts or opinions change.

This report is for discussion purposes only.

Although Rosenberg Research may provide commentary relating to investment approaches and opportunities to buy or sell securities, you should not construe such commentary as legal, tax, investment, financial or other advice. Nothing contained in any Rosenberg Research report or any other content on our web site constitutes a solicitation, recommendation, endorsement, or offer to buy or sell any securities or other financial instruments. Consult your own advisors if you require such advice.

This report should not be regarded by recipients as a substitute for the exercise of their own judgement and readers are encouraged to seek independent, third party research on any companies discussed or impacted by this report.

This report is not a research report under applicable U.S. rules and regulations.

Rosenberg Research does not guarantee the accuracy of any information in this report. This report may contain links to third-party websites. These links are provided as a convenience only. By providing these links, Rosenberg Research is not expressly or impliedly endorsing or approving these other sites, nor warranting or guaranteeing the content of the materials on such sites or the services or products that may be offered on such sites.

Rosenberg Research reports are distributed simultaneously to internal and client websites and other portals by email and are not publicly available.

TERMS AND CONDITIONS OF USE

Your receipts and use of this report are governed by the Terms and Conditions of Use which may be viewed at [www.rosenbergresearch.com]

THIS ROSENBERG RESEARCH REPORT IS NOT PUBLICLY AVAILABLE. UNAUTHORIZED USE OR DISCLOSURE IS PROHIBITED.

This report is prepared for the exclusive use of Rosenberg Research clients, subscribers to this report and other individuals who Rosenberg Research has determined should receive this report. This report may not be redistributed, retransmitted or disclosed, in whole or in

part, or in any form or manner, without the express written consent of Rosenberg Research.

ANY USE OF THIS REPORT IS AT YOUR OWN RISK AND LIABILITY. NEITHER ROSENBERG RESEARCH, NOR ANY DIRECTOR, OFFICER, EMPLOYEE OR AGENT OF ROSENBERG RESEARCH, ACCEPTS ANY LIABILITY WHATSOEVER FOR ANY DIRECT, INDIRECT, CONSEQUENTIAL, MORAL, INCIDENTAL, COLLATERAL OR SPECIAL DAMAGES OR LOSSES OF ANY KIND, INCLUDING, WITHOUT LIMITATION, THOSE DAMAGES ARISING FROM ANY DECISION MADE OR ACTION TAKEN BY YOU IN RELIANCE ON THE CONTENT OF THIS REPORT, OR THOSE DAMAGES RESULTING FROM LOSS OF USE, DATA OR PROFITS, WHETHER FROM THE USE OF OR INABILITY TO USE ANY CONTENT OR SOFTWARE OBTAINED FROM THIRD PARTIES REQUIRED TO OBTAIN ACCESS TO THE CONTENT, OR ANY OTHER CAUSE, EVEN IF ROSENBERG RESEARCH IS ADVISED OF THE POSSIBILITY OF SUCH DAMAGES OR LOSSES AND EVEN IF CAUSED BY ANY ACT, OMISSION OR NEGLIGENCE OF ROSENBERG RESEARCH OR ITS DIRECTORS, OFFICERS, EMPLOYEES OR AGENTS AND EVEN IF ANY OF THEM HAS BEEN APPRISED OF THE LIKELIHOOD OF SUCH DAMAGES OCCURRING.

If you have received this report in error, or no longer wish to receive this report, you may ask to have your contact information removed from our distribution list by emailing [subscriptions@rosenbergresearch.com].