A VERY GOOD ECONOMIC OUTLOOK

The U.S. economy is poised for the strongest growth in over 30 years as we enter the spring of 2021. Extraordinary stimulus packages have provided Americans with plenty of spending power, the labor market is red hot, the housing market is fierce, and both manufacturing and services are soaring.

All of this activity is supported by the arrival of warmer weather, and despite a recent rise in cases, the Covid situation continues to improve, with herd immunity likely to be reached before summer. In this report, we examine several factors that indicate a very good economic outlook into 2021.

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EULER HERMES

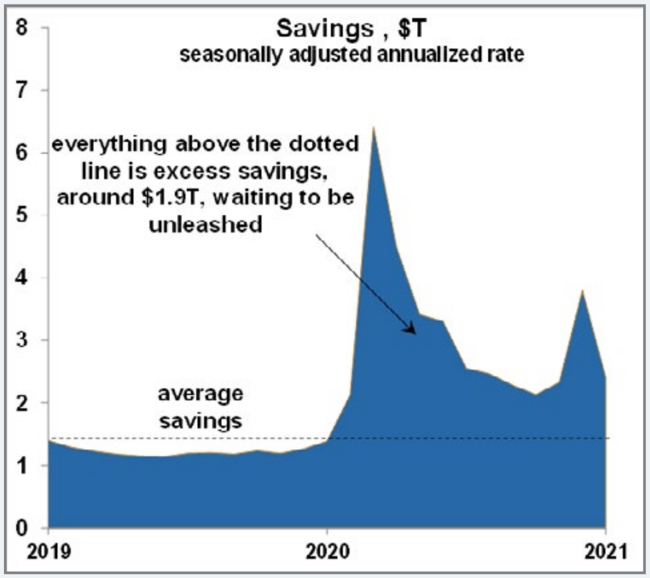
CONSUMERS ALREADY ON A SPREE

Almost 70% of all economic activity is driven by consumers, and as a group, consumers are flush with cash from the federal government's massive (perhaps overly massive) fiscal stimulus programs. The first round of stimulus came in April 2020 with the CARES Act, which sent $1,200 direct payments to individuals, totaling around $300B. The next round came in December 2020 with the Consolidated Appropriations Act (CAA), which sent $600 checks totaling $166B. And the most recent round of stimulus came in the American Rescue Plan (ARP), which is delivering $1,400 checks totaling about $400 billion.

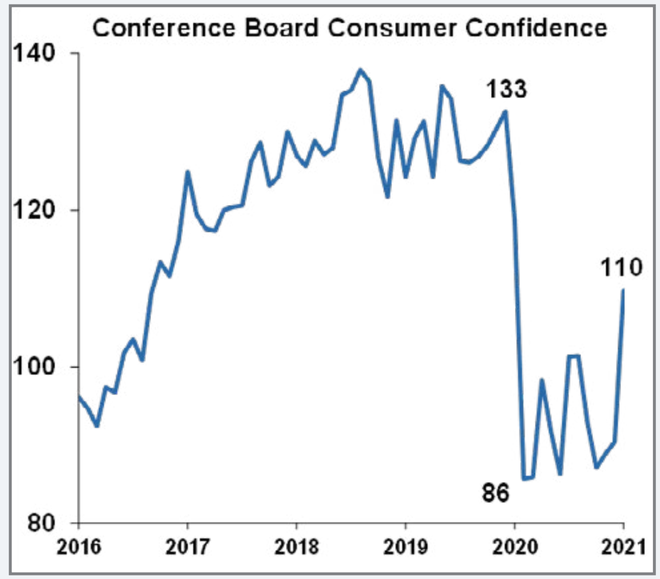
In addition to those direct payments, there have been huge extra unemployment benefits in place since April 2020. As a result, consumers have approximately $1.9T of excess savings, which are already being unleashed with vigor on the economy. That amount is equivalent to a gigantic 11% increase on top of what consumers might normally spend in a year and is a formidable 7% of Gross Domestic Product (GDP).

And now in addition to having the ability to spend, consumers are also regaining the willingness to spend as shown by The Conference Board's Consumer Confidence Index (see below). The Index soared in March to 110, recovering half of the plunge from the pandemic, and landing well above the long-term average of 95.

The Ability to Spend



The Willingness to Spend

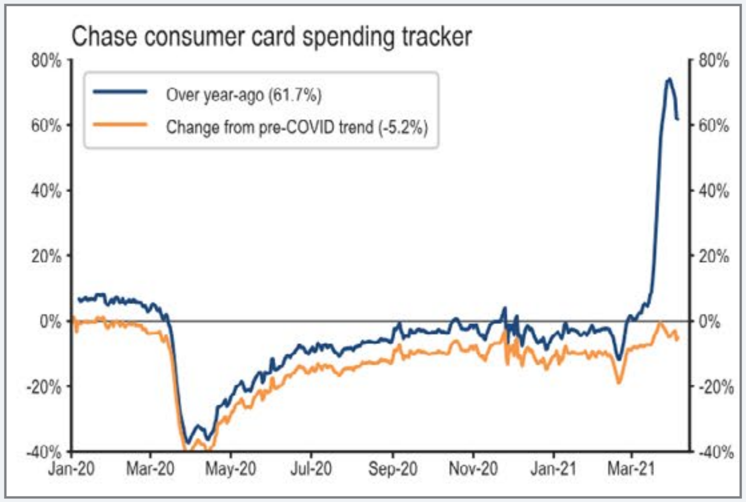


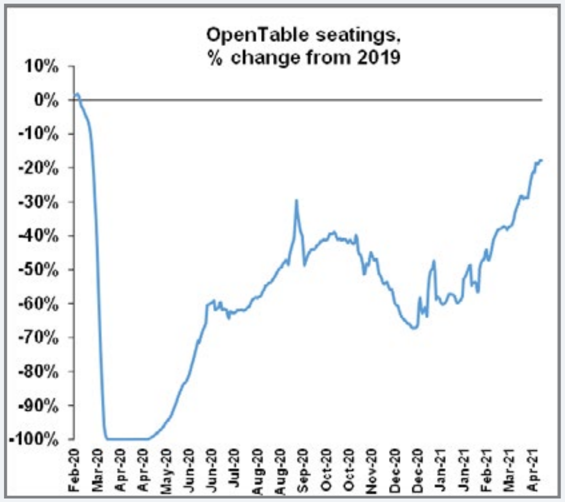
source: Census, The Conference Board, Allianz Research

CONSUMERS ALREADY ON A SPREE (CONT.)

As a result, consumers are already gleefully spending after a horrible year of Covid:

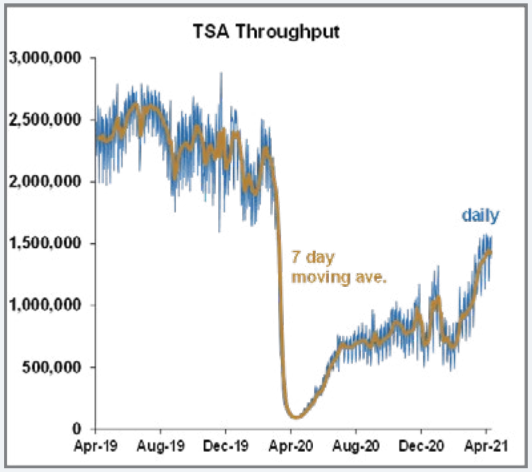
- The J.P. Morgan/Chase consumer credit card tracker fell almost 40% year/year when the pandemic struck. But just in the last month that number leapt from 0% y/y to a 60% y/y increase.
- Dinner reservations on Open Table fell virtually 100% when nationwide shutdowns occurred in March 2020. They then recovered slowly to being down approximately 60% at the beginning of 2021. Since then however, reservations have improved rapidly to being down only 18% and are on a steep ascent.

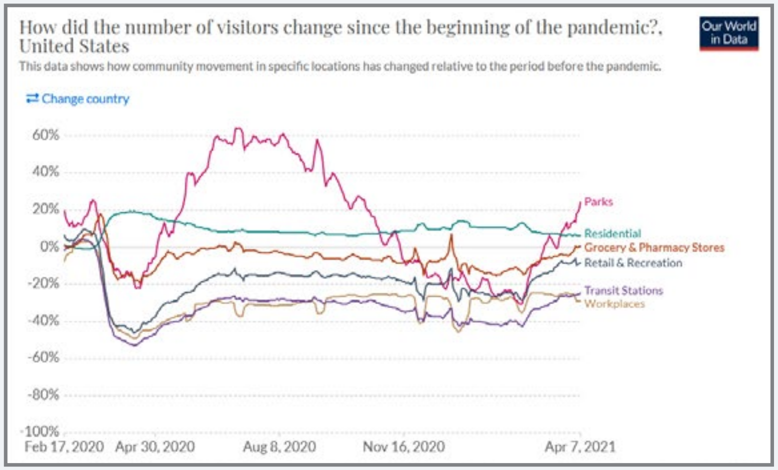




source: JP Morgan/Chase, OpenTable, Allianz Research

- As measured by TSA checkpoints in January and February of 2020, around 2.2 million passengers traveled by air every day. By April of 2020 that number had plummeted to around 100,000. There was a gradual recovery to around 750,000 by January of this year, but since then, it has doubled to about 1.5 million over the past three months and is quickly increasing.
- Mobility indexes, which measure when people visit certain venues and are correlated with economic activity, have risen sharply in the past few weeks. In some cases, they are now at pre-pandemic levels.

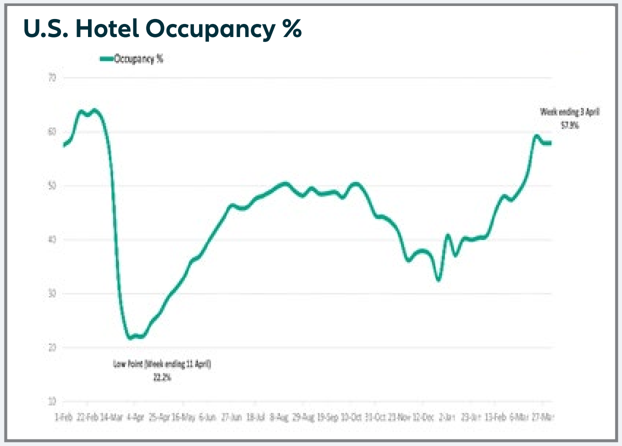


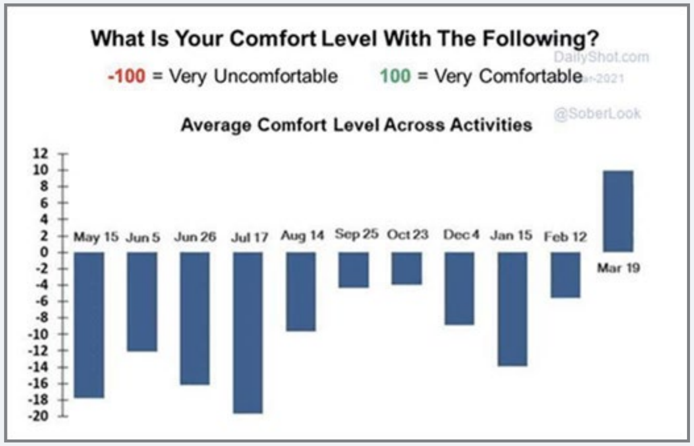


source: TSA, ourworldindata.com, Google, Allianz Research

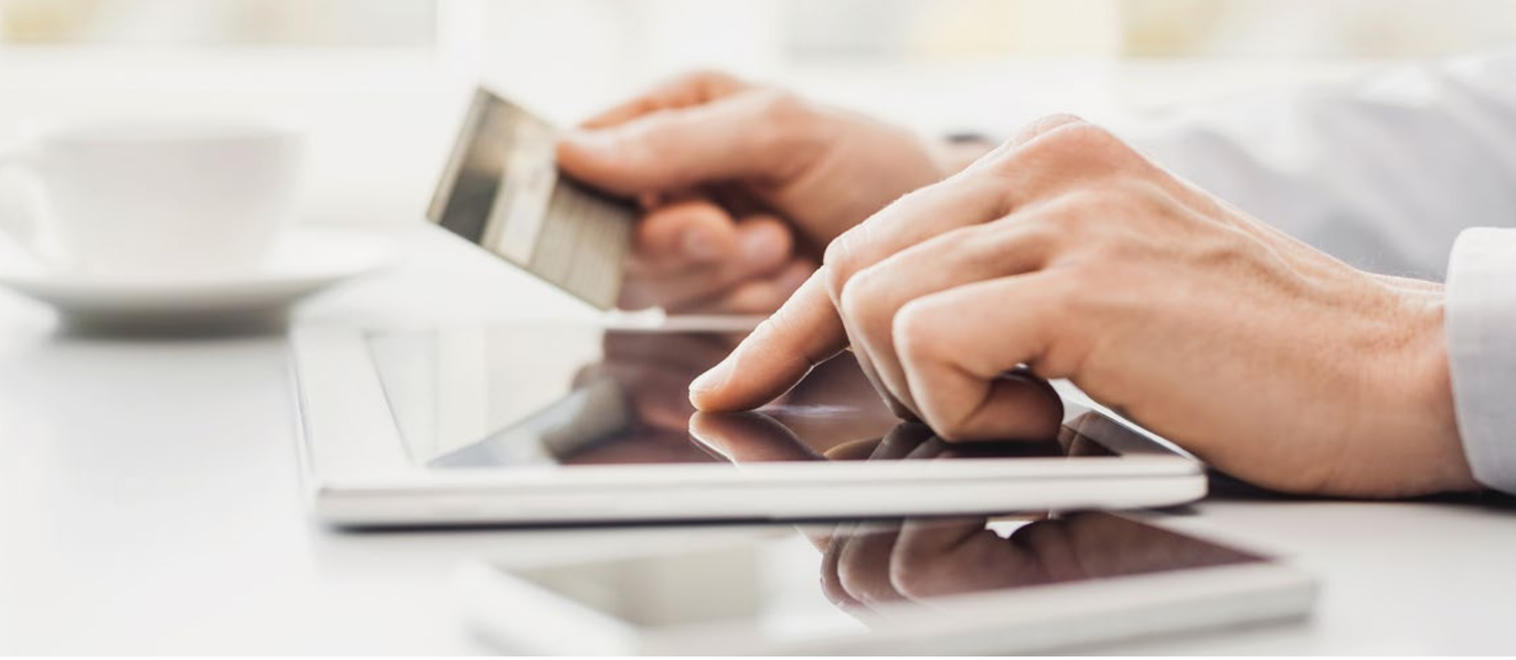
CONSUMERS ALREADY ON A SPREE (CONT.)

- Hotel capacity fell from 65% to 22% when the pandemic struck. It then slowly improved to 40% by the beginning of February 2021, but since then it has rapidly accelerated to 58% in less than two months.
- Perhaps most importantly, an Evercore/ISI survey which asked respondents how comfortable they are with a variety of activities that would put them at risk of Covid, turned positive in March for the first time since early last year. In other words, for the first time since the pandemic struck, people are now more comfortable getting out vs. less comfortable.





source: STR, ISI/Evercore, WSJ, Allianz Research



MANUFACTURING ACTIVITY TO CONTINUE STRONG

The consumer has supported the manufacturing sector since the beginning of the pandemic with increased demand for autos, household furnishings, and building materials. We expect this demand will continue throughout the year.

One carefully watched measure of the manufacturing sector is the Institute of Supply Management (ISM) Manufacturing Index. The index is based on a ten-part survey, and when the result is above 50, the manufacturing sector is in expansion. The March ISM survey showed a blistering pace as the overall result reached a 37-year record high. Two components of the survey which indicate the amount of work in the pipeline, and can therefore tell us how well the manufacturing sector will contribute to the economy in the next few months, were equally as impressive. The New Orders Index rose to a 17-year high, and the Backlog of Orders Index reached its highest in 28 years of record keeping.

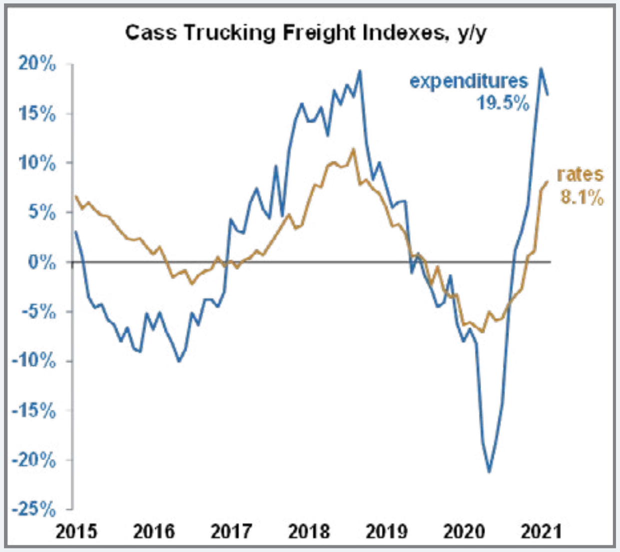
Transportation measures, which are closely related to manufacturing, are also skyrocketing. The Cass Systems index of trucking expenditures and rates are now up 19.5% and 8.1% y/y respectively. In addition, all of the regional Federal Reserve manufacturing surveys show sharp increases in activity.

THE NEW ORDERS INDEX ROSE TO A

17-year high

BACKLOG OF ORDERS INDEX REACHED ITS

highest in 28 years



source: ISM, Cass Systems, Allianz Research

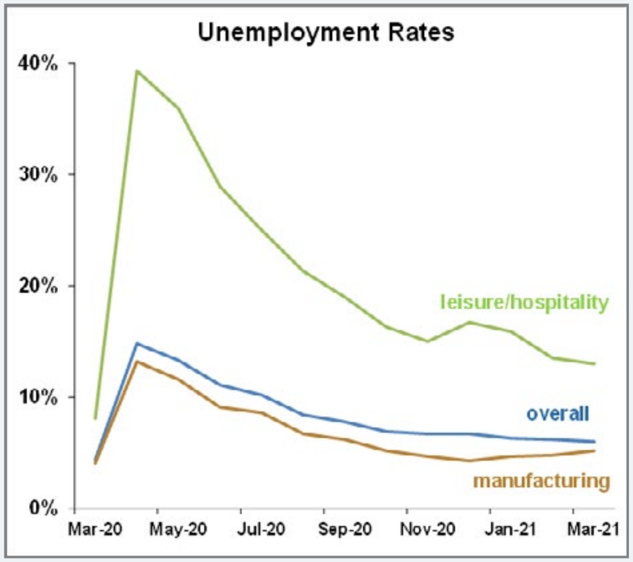
SERVICE SECTOR CATCHING UP RAPIDLY

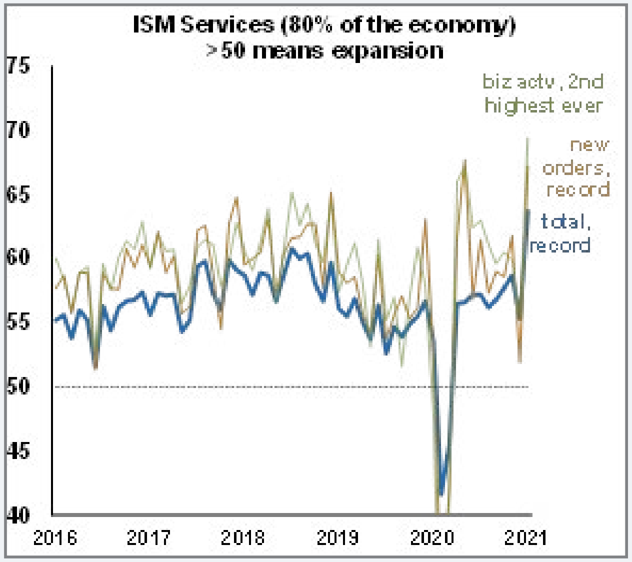
While the manufacturing sector recovered very quickly from the Covid-related shutdowns, the services sector, which accounts for approximately 80% of all economic activity, faced a significant obstacle from the beginning; many service sector jobs required face-to-face contact. For instance, workers in retail, restaurants, bars, hotels, airlines and others all had jobs that were customer-facing, and as the Covid-related shutdowns went into place, unemployment rates in these industries soared.

Current unemployment can't tell us much about the future, but a more forward-looking indicator of the services sector is the Services ISM Index. And like its manufacturing counterpart, the Services Index put in a blistering performance in March. The overall Index hit the highest ever in over 23 years of record keeping. The New Orders component also hit a record high, while the Business Activity component was the second-highest ever. Clearly as more state restrictions are lifted on establishments such as bars, restaurants, and retailers, the services sector will continue to expand.

IN MARCH, THE OVERALL INDEX HIT

the highest ever in over 23 years





source: BLS, ISM, Allianz Research

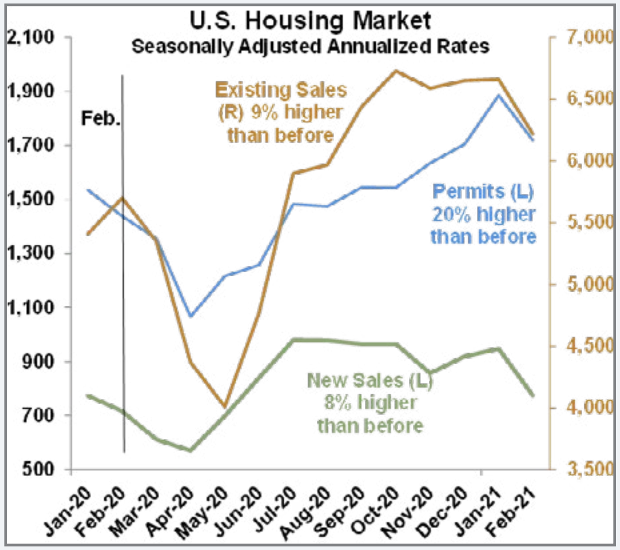
HOUSING MARKET SIZZLING

Housing is another sector of the economy that is growing rapidly. Fear of Covid quickly drove city residents into less urban areas early in the pandemic. Those fears have only partially abated, and now that working from home has been proven viable, demand for housing remains strong.

As shown below, several measures of housing demand are above where they were before the pandemic started. Permits to build new homes are 20% higher, new home sales are 8% higher, and existing home sales (a market about eight times as large as new home sales) are 9% higher. At the same time that demand remains elevated, supply is near record lows. With mortgage rates near record lows as well, the housing market will continue to boost the economy.

EXISTING HOME SALES ARE

9% higher than before the pandemic



source: NAR, Census, Allianz Research

FINANCIAL MARKETS ALSO SIGNALING AN ONCOMING SURGE

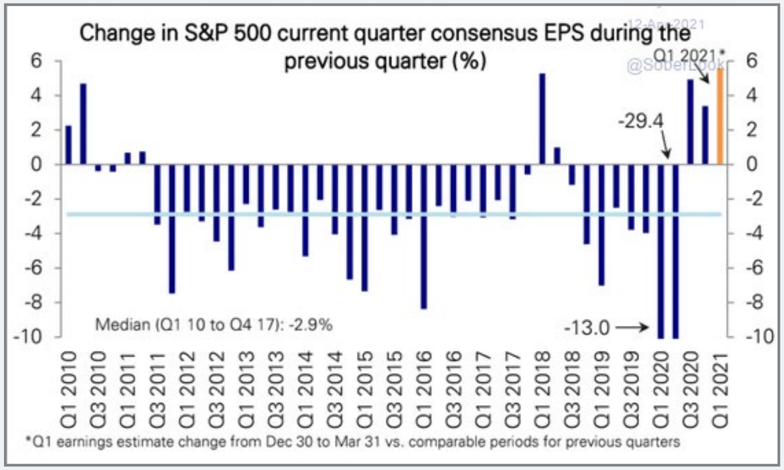
At the beginning of every quarter, stock market analysts make forecasts for how much money companies in the S&P 500 will earn over the quarter. Typically the analysts start off overly optimistic, and as more information becomes available through the quarter, they have to lower their forecasts. It's unusual for the analysts to revise their estimates up.

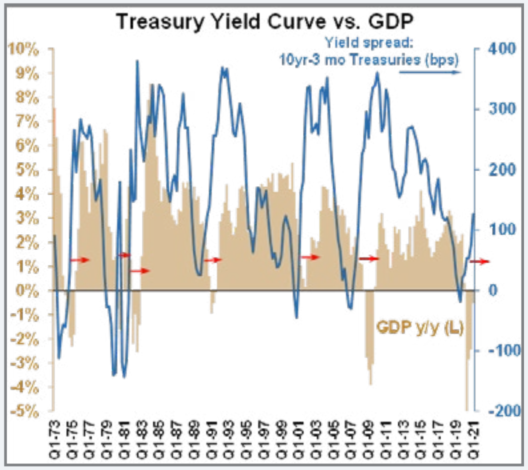
In fact, in the 10-year period from 2010 to Covid, analysts revised their estimates up in only six of 40 quarters. But since the recovery in Q3-20, analysts have had to revise their forecasts up for three straight quarters, and the upward revision for Q1-21 is the biggest on record. In other words, even analysts who are normally overly optimistic keep getting surprised by how much the outlook continues to improve.

The Treasury bond market is also signaling strength. And the Treasury bond market view of the future is typically more firmly rooted in reality than is the stock market. The Treasury yield curve (as represented by the blue line in the image below) has a virtually perfect record of forecasting economic growth ahead. As shown in the chart, every time the yield curve has gone positive over the past 45 years, GDP growth has also gone positive. At the moment, the yield curve is strongly positive, forecasting with virtual certainty continued economic vigor for the next three to five quarters.

THE UPWARD REVISION FOR Q1-21

is the biggest on record





source: WSJ, Bloomberg, Deutsche Bank, Fed, BEA, Allianz Research

STRONG LABOR MARKET

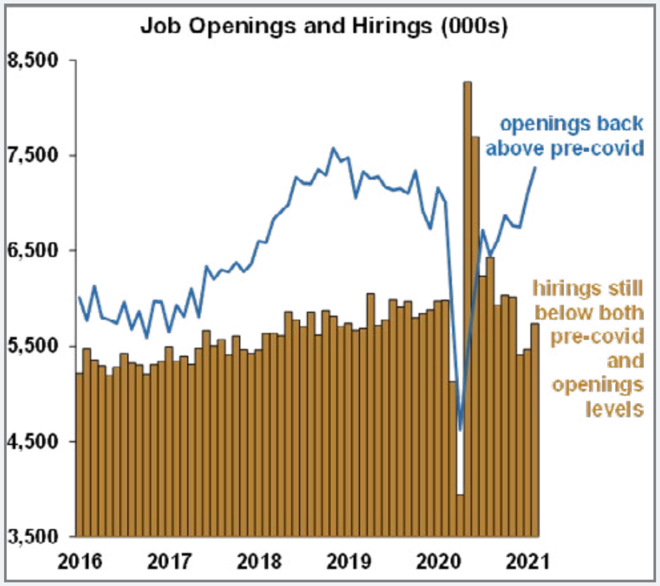
Demand for labor is feverish as states start to re-open their economies and lift restrictions. In March, the economy created a blistering 916k jobs, far outpacing already high expectations of 700k. Leisure and hospitality gained 280k jobs, the second consecutive strong month after February's 384k. Clearly the lifting of restrictions on bars and restaurants is driving potent growth in this industry, and there will certainly be more gains to come.

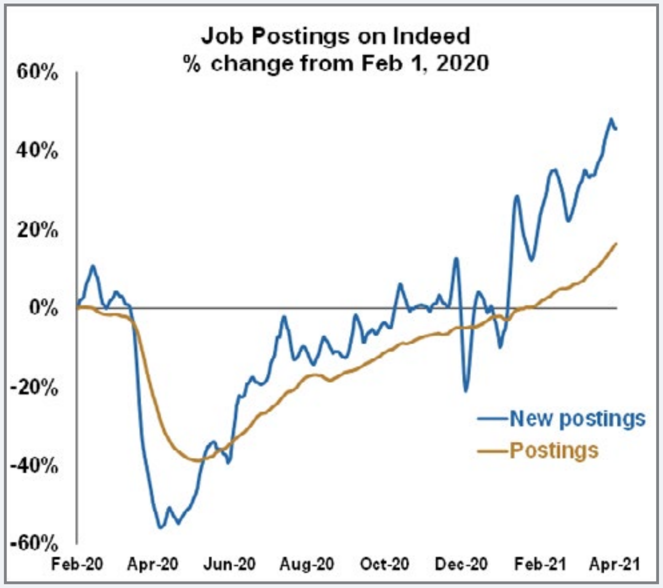
Construction also made a powerful rebound from February's foul weather, and gained 110k in March, which outside of the pandemic recovery months, was the most in 31 years. More warm weather and a red-hot housing market will drive even further gains this year.

Jobs in education and health services rose a steep 101k as students started to return to school, another trend we expect to see continue. These factors, which created so many jobs in March, will also drive potent job growth over the next few months.

In fact, job openings are already back above pre-Covid levels, and job postings on the Indeed hiring website are up a remarkable 39% from last February. The employment outlook is bright in terms of demand for labor.

IN MARCH, CONSTRUCTION gained 110k, WHICH OUTSIDE OF THE PANDEMIC RECOVERY MONTHS, WAS THE most in 31 years





source: BLS, Indeed, Allianz Research

NOT EVERYTHING IS PERFECT THOUGH

The supply of labor however, is a different issue; employers are desperate for workers. As seen above, Job Hirings remain well below the plentiful Job Openings. Some reasons for this situation, such as people leaving the labor force due to discouragement or retirement, are more difficult to fix. But other problems can improve.

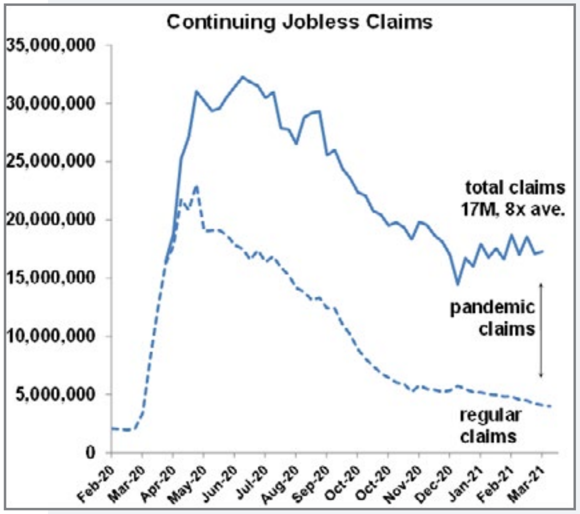
A recent study from the Census Bureau found approximately 4.2 million workers haven't returned to the labor force because of the fear of contracting Covid in the workplace; that's half of the 8.4 million jobs which are still missing from last year. Fortunately, as Covid becomes more under control, some of these apprehensive people will return to the workforce. In addition, overly-generous jobless benefits are providing an incentive not to work, leaving 17 million people still on the jobless rolls.

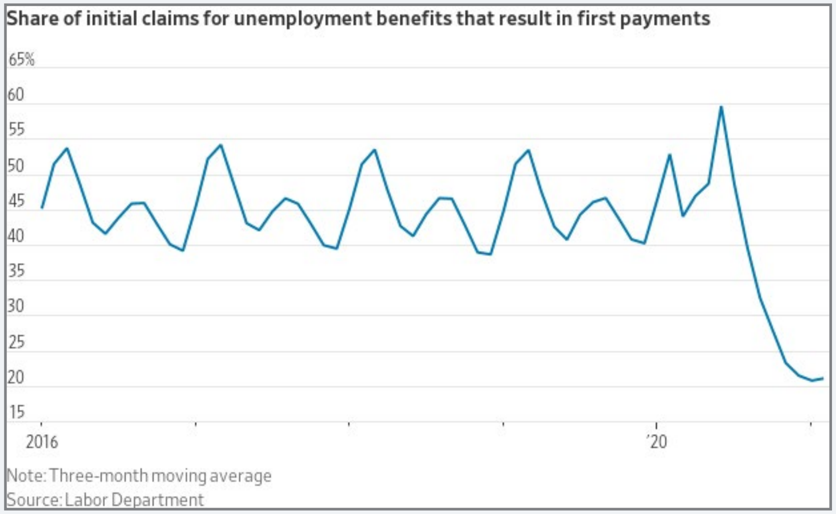
Furthermore, the share of jobless claim applications that are approved and result in a payment have fallen from an average of about 45% over the last five years to only 20% this year. The data suggests that because the benefits are so generous, many people who wouldn't otherwise qualify may simply be taking the chance of getting approved, allowing them to stay home. However the special pandemic unemployment programs, which comprise 70% of all continuing claims, are scheduled to expire in September of 2021, which will then provide an incentive for people to return to the workforce.

A RECENT STUDY FROM THE CENSUS BUREAU FOUND APPROXIMATELY

4.2 million workers

HAVEN'T RETURNED TO THE LABOR FORCE BECAUSE OF THE FEAR OF CONTRACTING COVID IN THE WORKPLACE



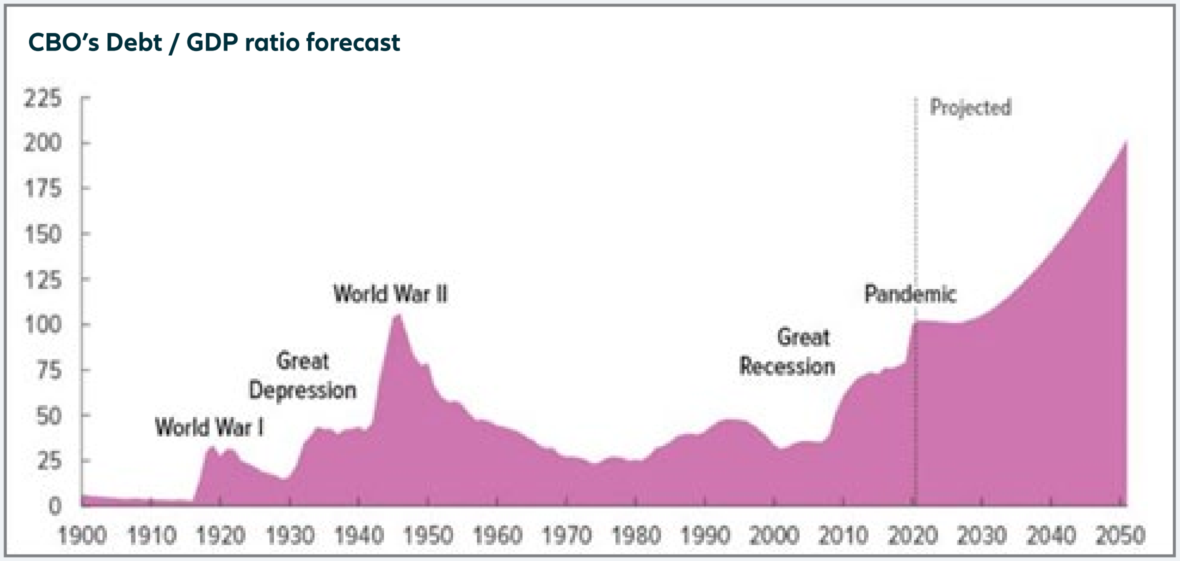


source: Dept. of Labor, Allianz Research

NOT EVERYTHING IS PERFECT THOUGH (CONT.)

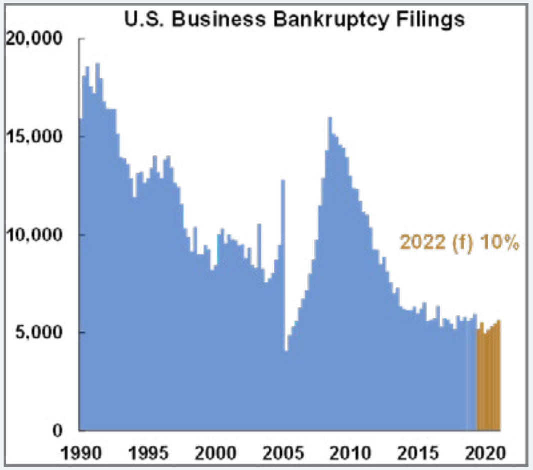
There are some other blemishes on the landscape. The astronomical amount of debt incurred to finance the massive fiscal and monetary stimulus programs will slow GDP growth to less than half its long-term average by 2025. Recently, the Congressional Budget Office (CBO) forecasted the amount of debt as a percentage of GDP over the next thirty years, showing that by 2050, the debt/GDP ratio will reach an astounding 202%. And that doesn't even include the recently-passed ARP or the proposed $2 trillion infrastructure spending program.

By comparison, from 1962 to the financial crisis, the debt/GDP ratio averaged only 32%. Perhaps Congress and the Administration should take a pause and let the economy flourish before spending more money that we don't have, incurring even more debt, and raising taxes in the process.



source: CBO, US Courts, Allianz Research

Finally, the beneficial effects from the stimulus packages meant to support businesses, such as the Paycheck Protection Program (PPP), will be wearing off. There isn't much money left in the program—as of April 11, 2021, $755 billion of the $813.5 billion appropriated has been distributed. It is unknown how much of that cash is still being used to keep businesses afloat, but it certainly delayed a surge in bankruptcies in 2020. Unfortunately, as that support wears off, we expect to see bankruptcies increase by a sharp 10% in 2022.



BUT IT'S GOING TO BE A GREAT YEAR

Despite problems such as a dearth of labor, a huge debt load, and oncoming bankruptcies, 2021 looks to be a smashing year. Consumers have an enormous amount of excess savings that they are energetically pumping into the economy. And measures of activity, such as credit card spending, dining, travel, and others, clearly show that with warmer weather, consumers are gleefully releasing pent-up demand after a ghastly year. Leading indicators of manufacturing also show undoubted strength while the services sector is in rapid ascent as restrictions are lifted. Housing demand is through the roof, and the demand for labor is dramatic.

2021 is going to be the best year in over three decades.

For more information, visit **eulerhermes.us/dan-north,** and follow us on **LinkedIn** for live updates.