



2020 Advisory Conference

October 27–29

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THE REAL ECONOMY

Helping middle market clients anticipate and address their unique challenges

October 27, 2020

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Speaker



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Industry Eminence Program Leader

Kevin Depew is an Emmy Award-winning writer and producer. Prior to joining RSM, he worked in economics for Bloomberg LP. Kevin has also worked for Dorsey Wright and Associates, PaineWebber and AG Edwards. His former roles include chief strategist, director of research, financial markets analyst and portfolio manager.

Kevin attended St. John's College in Annapolis, Maryland and graduated from the University of Kentucky with a BA in Philosophy.

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Agenda

Topic	Minutes
Setting the stage, pre-pandemic forecast	12
Current economic forecast	12
Middle market economics	12
Reopening the economy amid a pandemic	12
Conclusion: What could go right?	12



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Objectives

By the end of this course, you will be able to:

- Understand how the middle market fits into current economic conditions
- Prepare for uneven economic growth across the economy driven by industry differences



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Economic outlook...pre-pandemic (slide from January)

Primary themes

- **Growth deceleration**
 - GDP 1.8% 2019
 - Deceleration to 1.5% 2020
 - Consumer propping up economy
 - Weak fixed business investment
- **Employment growth solid**
 - Unemployment rate at 3.6%
- **Fed on hold**
- **Inflation back toward 2%**
- **Risks to outlook**
 - Policy errors: trade and/or central banking
 - Liquidity event: COVID-19

This was the RSM baseline forecast pre-pandemic; useful guide for baseline economic outlook prior to the pandemic and economic shocks.



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Pandemic economics, recovery and beyond



U.S. economy: Recovery in progress... now stalling

- Supply, demand and financial shocks beginning to ebb
- Household consumption a risk due to lack of fiscal support
- Major risk to the economic outlook: second wave of pandemic



Policy response

- Policy impasse over fiscal aid downgrades growth prospects in Q4'20 & Q1'21
- Main Street Lending Program needs modifications
- Until there is a vaccine, or multiple major therapeutic breakthroughs, no full recovery



Shape of recovery

- K-shaped recovery? No, K-shaped economy
- Elongated and frustrating in some industries
- Housing and manufacturing lead rebound = 17% of total economy
- Large firms seeing pickup in activity
- Middle market moves out of recession
- Long-term damage to small businesses and services sector



Source: RSM US LLP

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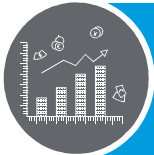


Pandemic economics, recovery and beyond



U.S. growth picture

- Q1'20: minus 5%
- Q2'20: minus 31.4%
- Q3'20: RSM forecast 33.5%
- Q4'20: RSM forecast 2.25%



Financial conditions

- Financial conditions only modestly supportive of growth
- Equity prices back to near all-time highs
- Equity market not connected to conditions in the real economy
- Real negative rates



Important upcoming dates

- November 3, 2020 U.S. Election
- Federal protection for employment has already expired
- Risk of permanent unemployment rising



Source: RSM US LLP

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Pandemic economics, recovery and beyond



U.S. employment

- Mass unemployment: Over 62 million experienced some form of unemployment & loss of income
- 7.9% unemployment, 12.8% under-employment
- Real unemployment rate likely 3 percentage points higher



U.S. savings rate at 14.1%

- Upper income earners: pulled back spending by 7.1% since January 2020; net savers
- Low-income earners: spending up 0.3% since January 2020; net spenders



Government support key to propping up economy

- Long period of fiscal aid will be necessary
- \$15 billion per week in lost government income support due to policy impasse



Inflation

- Disinflation/deflation in the near to medium term
- Inflation longer term
- 1965-80 economy

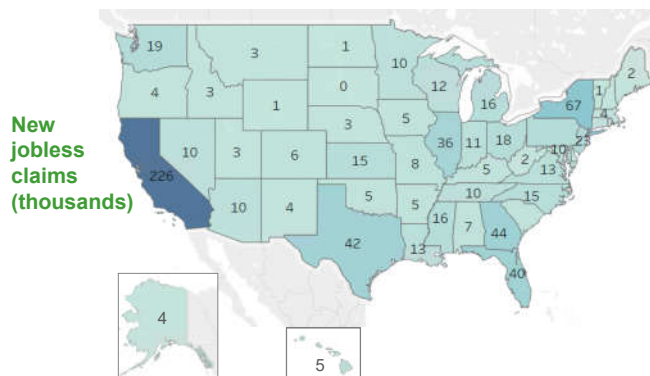


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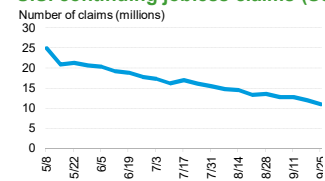
Real Economy shock: Labor market

New and continuing jobless claims only slowly declining; remain elevated (840,000/10/9mm through Sept. 25)

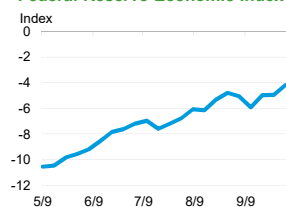


Source: BloombergNEF, Department of Labor, U.S. Federal Reserve Bank of New York; Note: The Weekly Economic Index tracks 10 weekly indicators of real economic activity, scaled to have the units of four-quarter percent change of real GDP.

U.S. continuing jobless claims (Sept. 25)



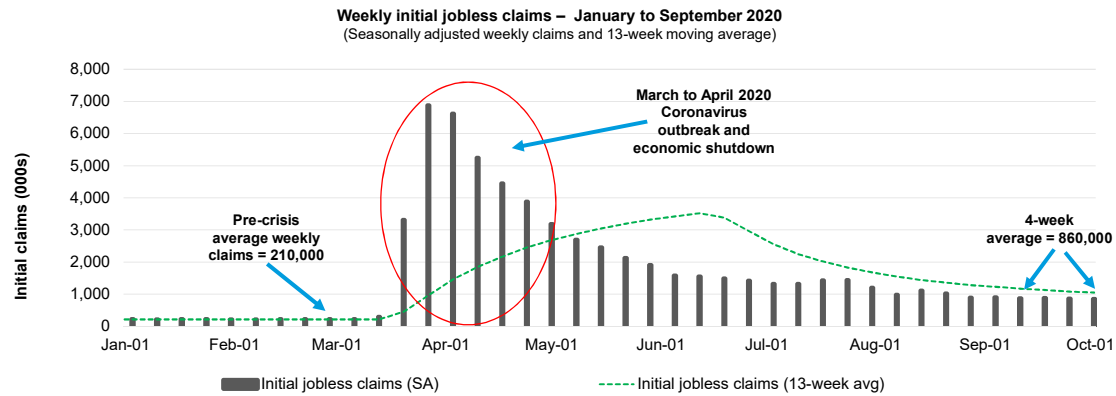
Federal Reserve Economic Index



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Real Economy shock: Labor market



Source: BLS; Bloomberg; RSM US

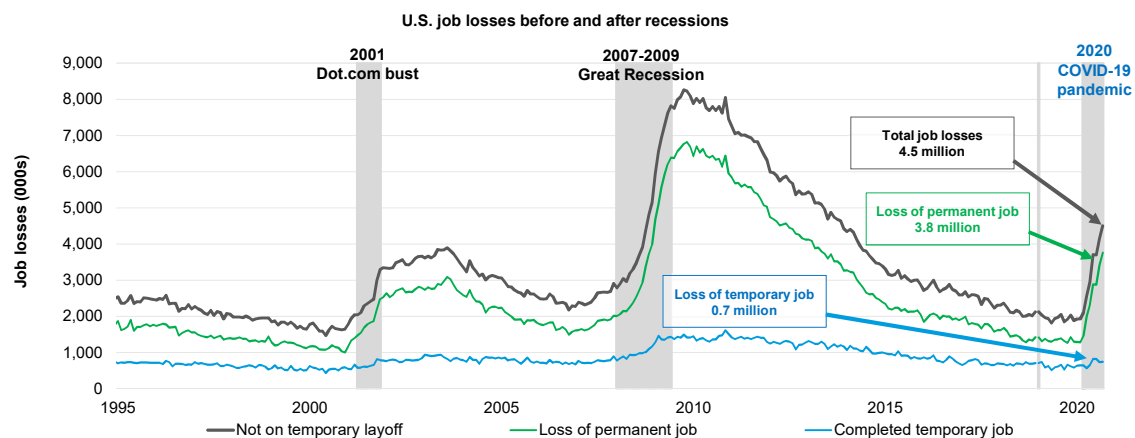


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Real Economy shock: Labor market



Source: BLS; NBER; RSM US



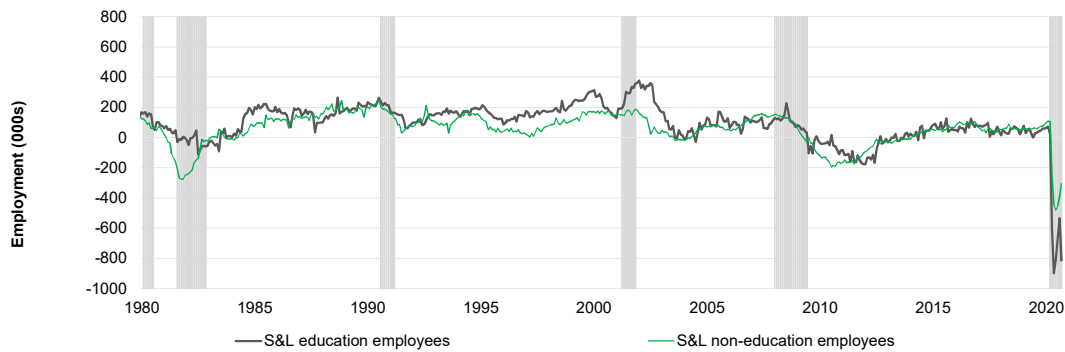
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Real Economy shock: The next shoe...

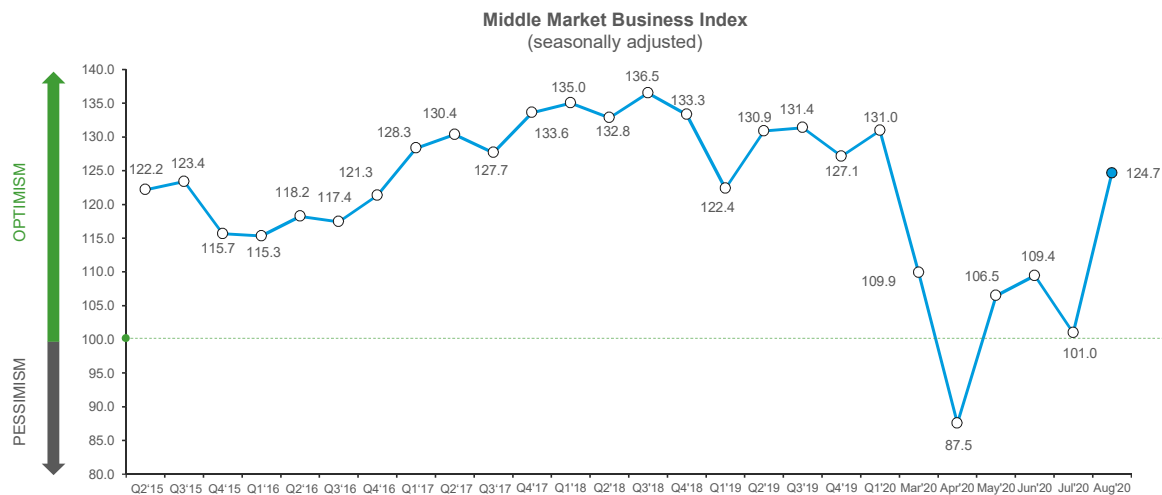
Change in state & local employment in education and non-education positions during recession episodes
(Year-over-year change in employees)



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The RSM US Middle Market Business Index in August is statistically higher compared to July



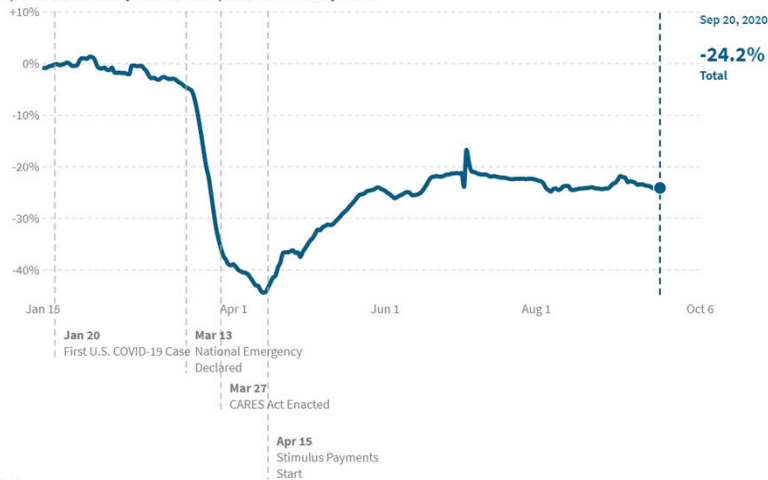
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Real Economy: Small businesses open

In the United States, as of September 20, 2020, the number of small businesses open decreased by **24.2%** compared to January 2020.

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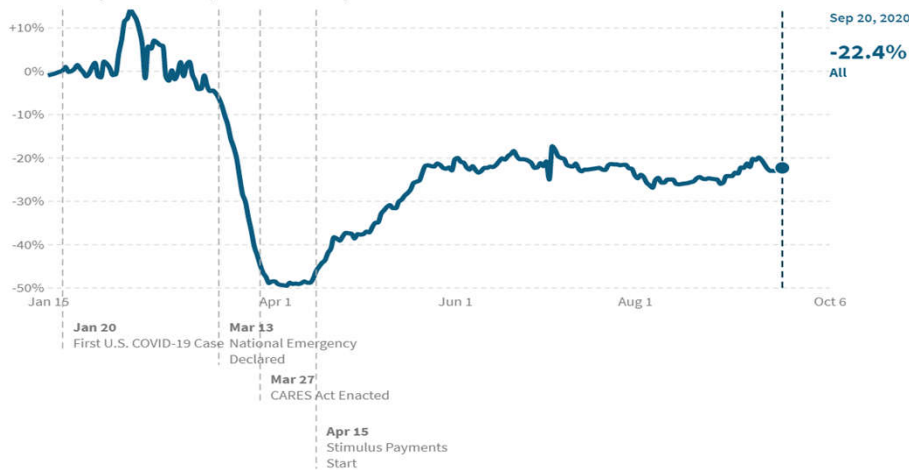
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Real Economy: Small businesses revenues

In the United States, as of September 20, 2020, total small business revenue decreased by **22.4%** compared to January 2020.

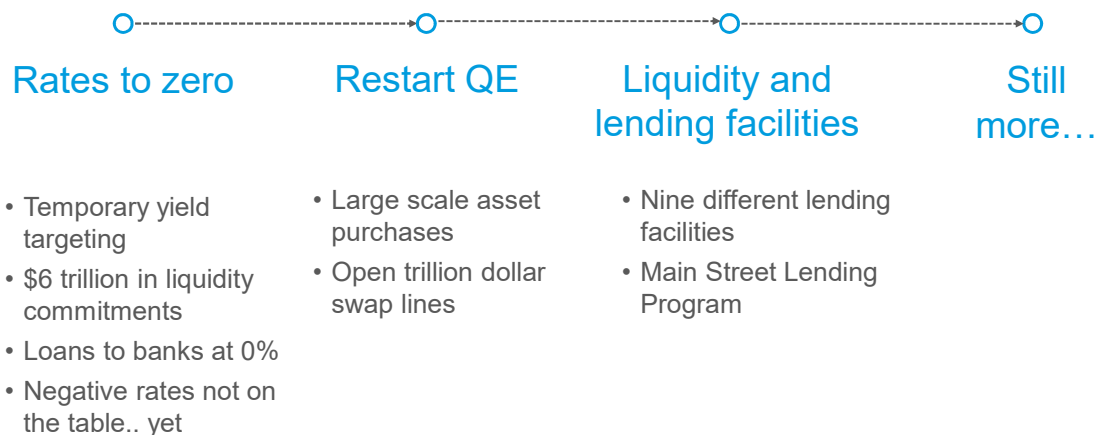
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Monetary policy response: The kitchen sink

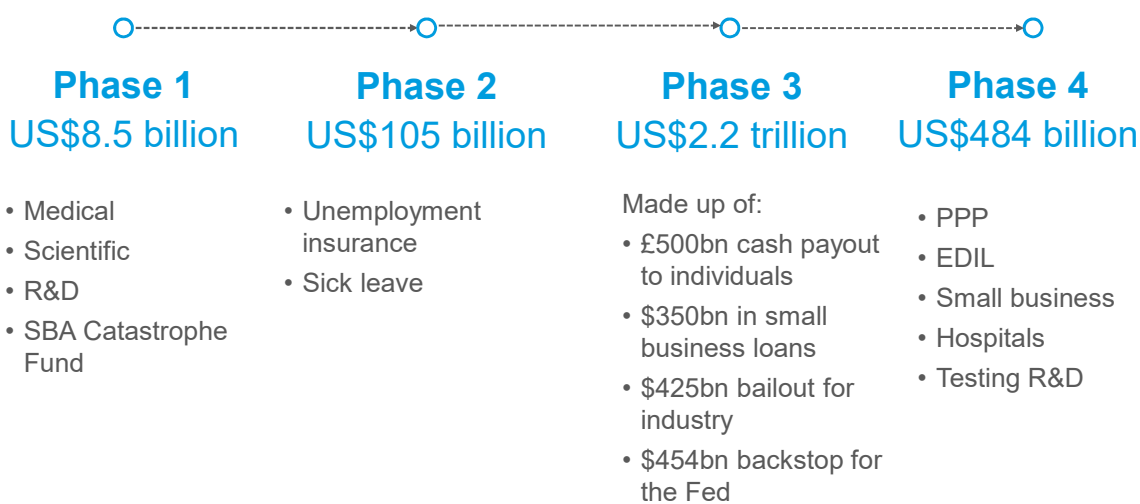


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Fiscal policy response: 11.4% of GDP

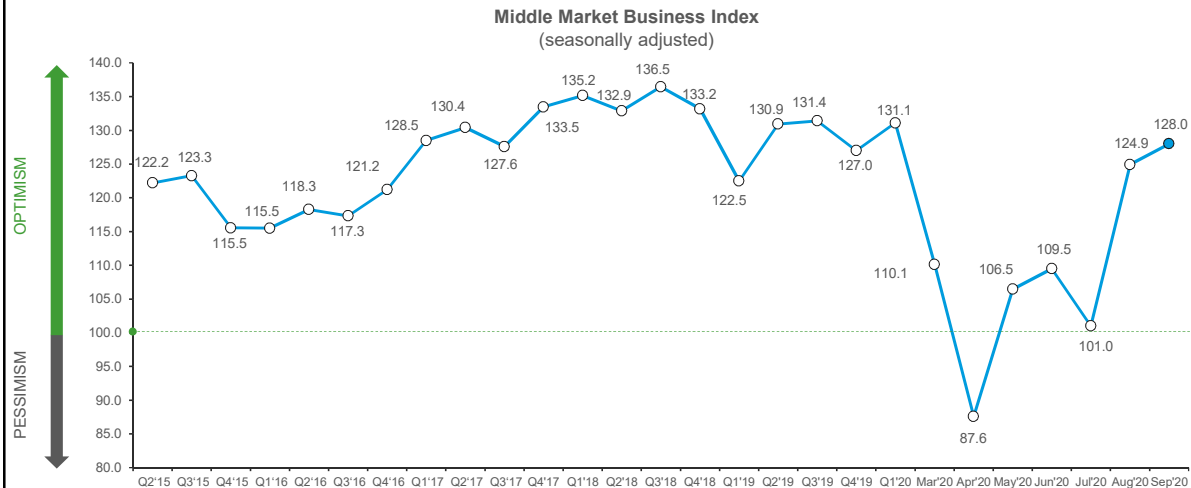


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The RSM US Middle Market Business Index in September is statistically higher compared to August

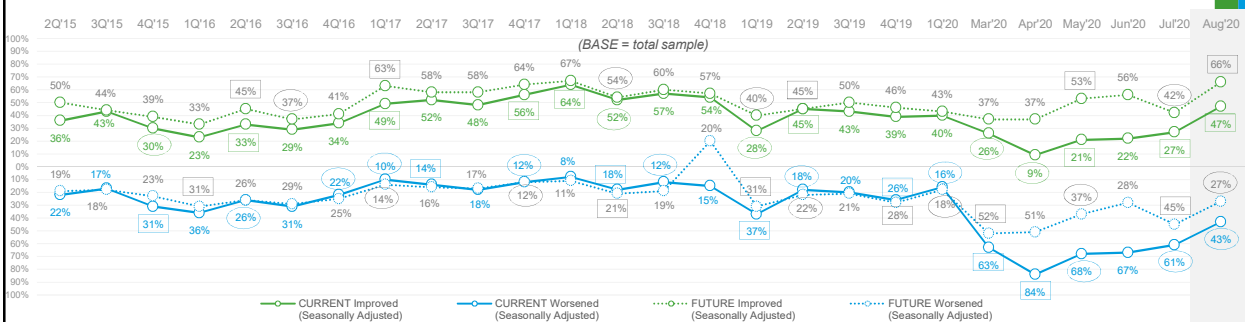


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General economy performance (total) needs updating

General Economy Performance (Total)



		% REMAIN UNCHANGED (Non-Seasonally Adjusted)																									
FUTURE	CURRENT	Q2'15	Q3'15	Q4'15	Q1'16	Q2'16	Q3'16	Q4'16	Q1'17	Q2'17	Q3'17	Q4'17	Q1'18	Q2'18	Q3'18	Q4'18	Q1'19	Q2'19	Q3'19	Q4'19	Q1'20	Mar'20	Apr'20	May'20	Jun'20	Jul'20	Aug'20
		(n=210)	(n=252)	(n=208)	(n=424)	(n=404)	(n=400)	(n=406)	(n=409)	(n=400)	(n=406)	(n=399)	(n=412)	(n=402)	(n=402)	(n=404)	(n=404)	(n=409)	(n=402)	(n=400)	(n=399)	(n=401)	(n=403)	(n=402)	(n=402)	(n=404)	(n=404)
		41%	43%	41%	37%	41%	42%	45%	37%	34%	37%	34%	23%	31%	34%	32%	31%	38%	40%	36%	40%	9%	6%	9%	11%	14%	12%
		(n=210)	(n=252)	(n=208)	(n=424)	(n=404)	(n=397)	(n=402)	(n=409)	(n=406)	(n=399)	(n=412)	(n=405)	(n=402)	(n=404)	(n=404)	(n=404)	(n=409)	(n=401)	(n=400)	(n=399)	(n=401)	(n=402)	(n=402)	(n=402)	(n=400)	(n=403)
		31%	41%	41%	31%	29%	37%	36%	17%	26%	27%	26%	16%	25%	24%	25%	24%	33%	31%	27%	34%	8%	11%	12%	18%	16%	11%

170 First, thinking about the general economy this quarter versus last quarter, how would you describe the current general economy? Would you say the general economy has ...

171 What are your expectations regarding the general economy over the next six months? Do you expect the general economy will ...

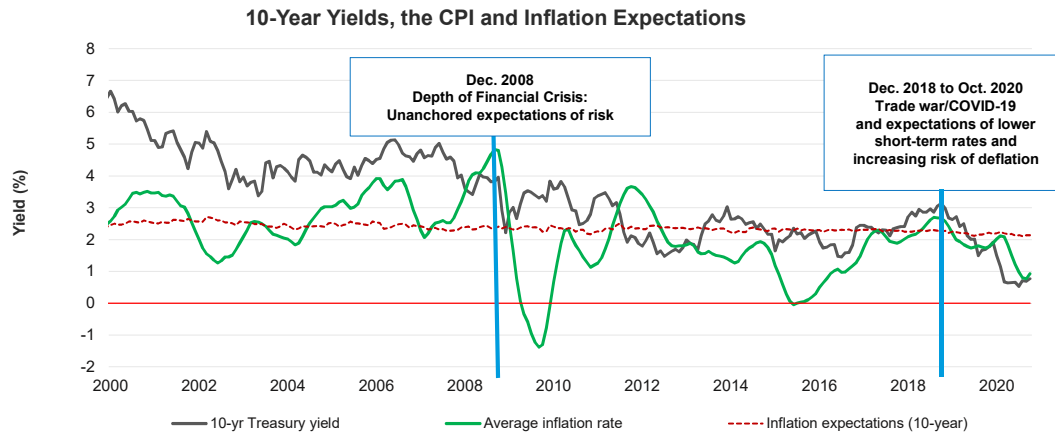
NOTE: Due to Seasonal Adjustment, % top 2 box, % bottom 2 box, and % remained unchanged may not add to 100%
 SQUARE/CIRCLE = Significantly higher/lower than previous wave, respectively, at .05 level of significance



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Interest rates: Market pricing in disinflation



Source: Philly Fed; Bloomberg; RSM US



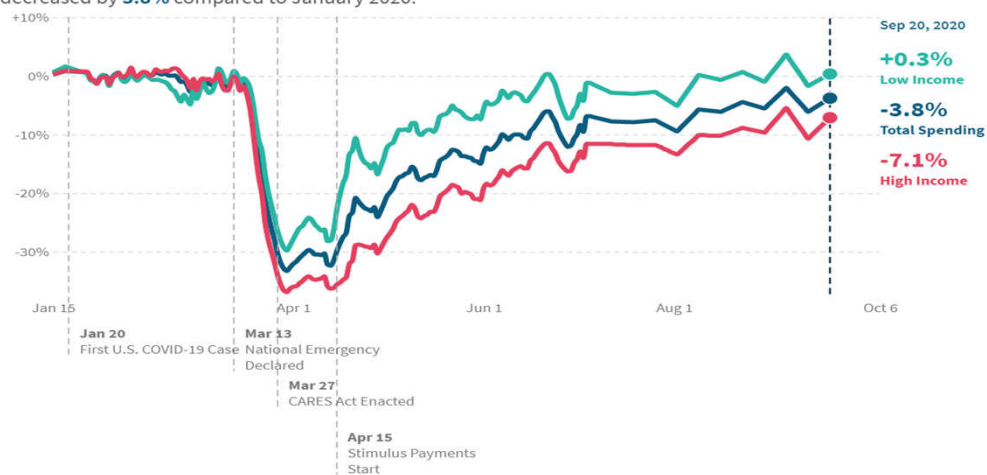
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Consumer spending

In the United States, as of September 20 2020, total spending by all consumers decreased by **3.8%** compared to January 2020.

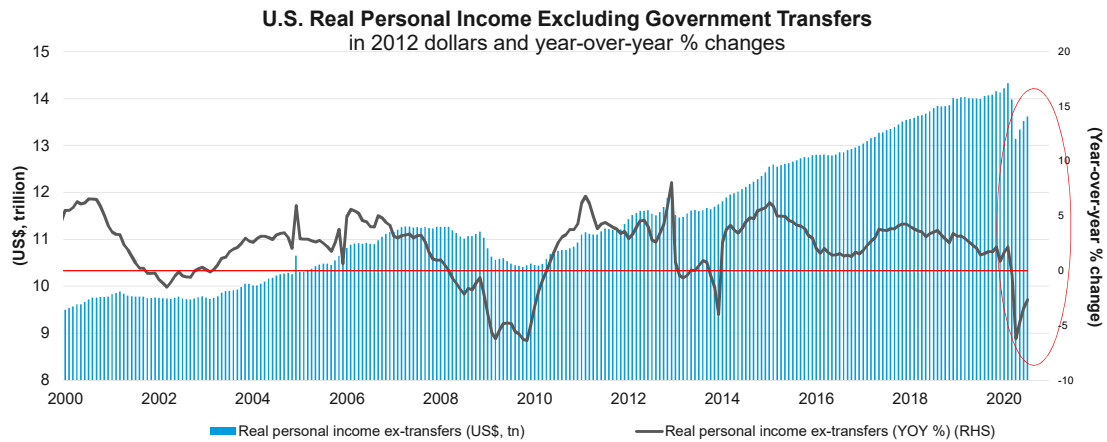
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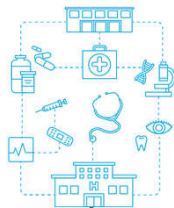


Consumer spending propped up by government transfers



“There is the risk of permanent damage...” – Jerome Powell

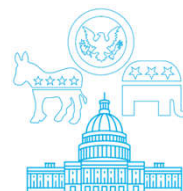
Health and Public Safety



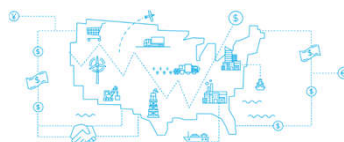
Economic Preservation



Political Views & Personal Freedoms

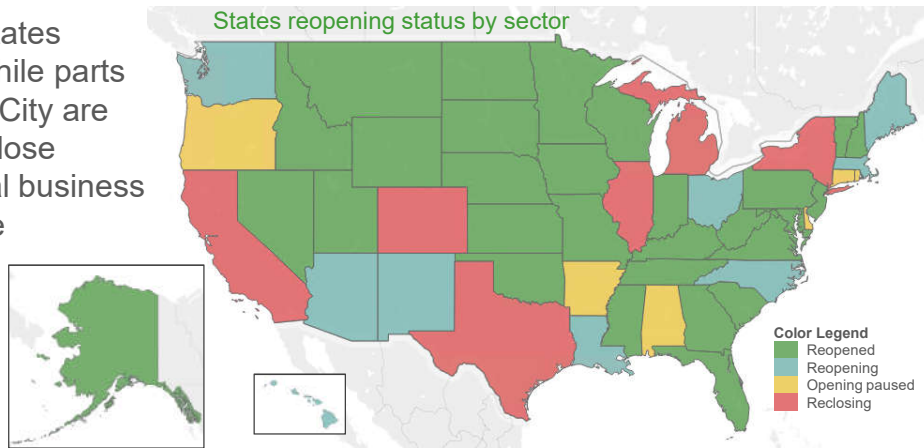


Reopening the Economy



Stay-at-home restrictions

Four more states reopened, while parts of New York City are forced to reclose non-essential business as cases rise



Source: BloombergNEF, New York Times; Note: Data as of October 7, 2020.



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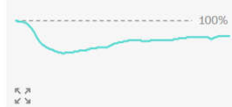
Real economy shock: The “Back-to-Normal” Index

The Back-to-Normal Index

The pandemic economy is far from normal. So Moody's Analytics and CNN Business have partnered to create a proprietary Back-to-Normal Index, comprised of 37 national and seven state-level indicators. The index ranges from zero, representing no economic activity, to 100%, representing the economy returning to its pre-pandemic level in March.

United States

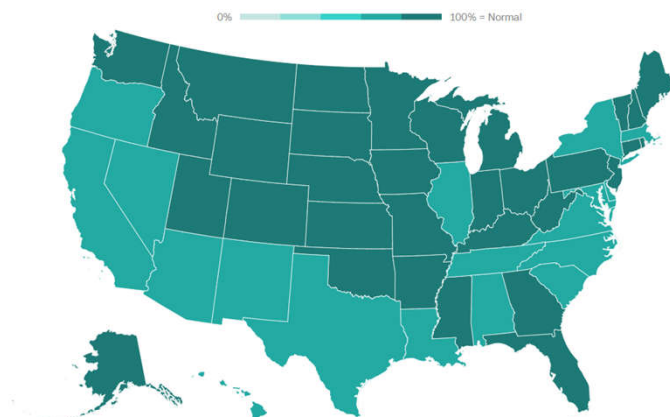
80%



The economy in the United States is operating at 80% of where it was in early March.

New coronavirus cases in the last 7 days
292,971 ▼

Number of states with improved Index since last week
21



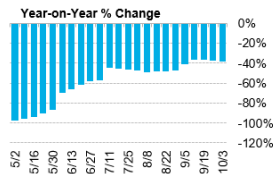
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Real-time economic activity

Restaurant dine-in activity improved dramatically led by GA, FL and TX. All three states have surpassed 75% of Feb. levels

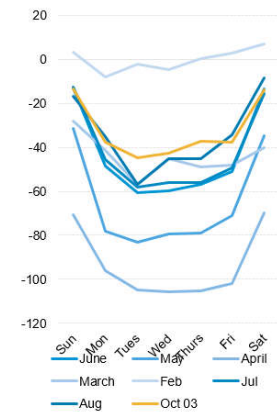
Retail activity



Restaurant dine-in activity

	Week-on-Week	vs Feb
New York	6%	-58%
California	3%	-45%
Georgia	13%	-22%
Florida	11%	-21%
Texas	8%	-25%
Illinois	0%	-47%
Mass	5%	-39%
U.S.	6%	-37%

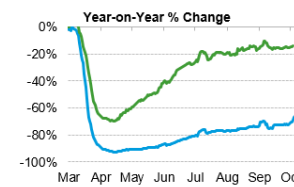
U.S. mobility and engagement



Public transport ridership

	Week-on-Week	vs Feb Avg
Boston	1%	-49%
Chicago	1%	-45%
Dallas	12%	-34%
Washington, DC	0%	-54%
Houston	2%	-56%
Los Angeles	1%	-58%
Miami	0%	-73%
New York City	3%	-40%
Philadelphia	2%	-41%
Pittsburgh	0%	-59%
San Francisco	0%	-73%
Seattle	-1%	-57%

NYC subway, vehicle entries



Source: BloombergNEF, OpenTable, ProCo, Moovit, and New York City Metropolitan Transportation Authority



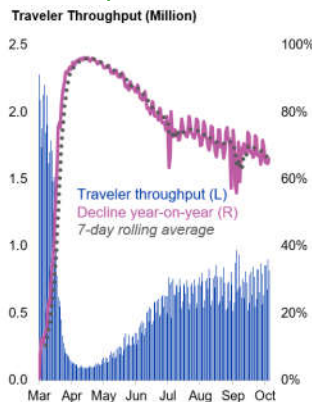
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Real-time economic activity

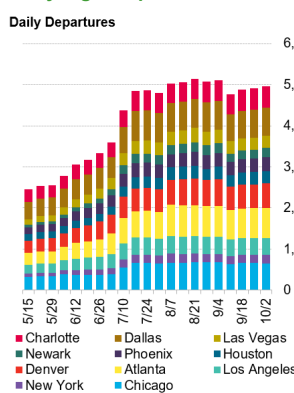
Jet fuel demand still sits at about half of where it was this time last year with relatively flat daily flight departures.

TSA checkpoint traffic



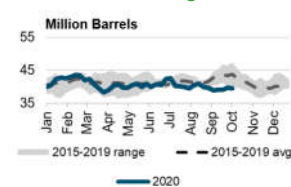
Source: BloombergNEF, TSA

Daily flight departures

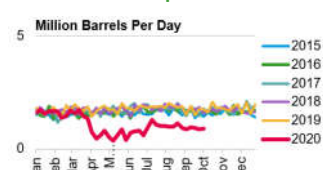


Source: BloombergNEF, FlightStats

Jet kerosene storage



Jet kerosene implied demand



Source: BloombergNEF, U.S. Energy Information Administration



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How long before the U.S. is back to full production?

• How long?

- **Scenario one: single pandemic wave**
 - US economy should begin to recover in Q4
- **Scenario two: second pandemic wave**
 - Regionalized lockdowns
 - Recovery in second half of 2021
- **Scenario three: persistent pandemic waves**
 - Regionalized lockdowns
 - Recovery in 2022

• Steps to *fully* reopening economy

- A consistent decrease in the number of cases
- The ability to test, isolate and trace
- Sufficient amount of health-care infrastructure available if re-emergence
- Effective therapies and vaccine available to entire population

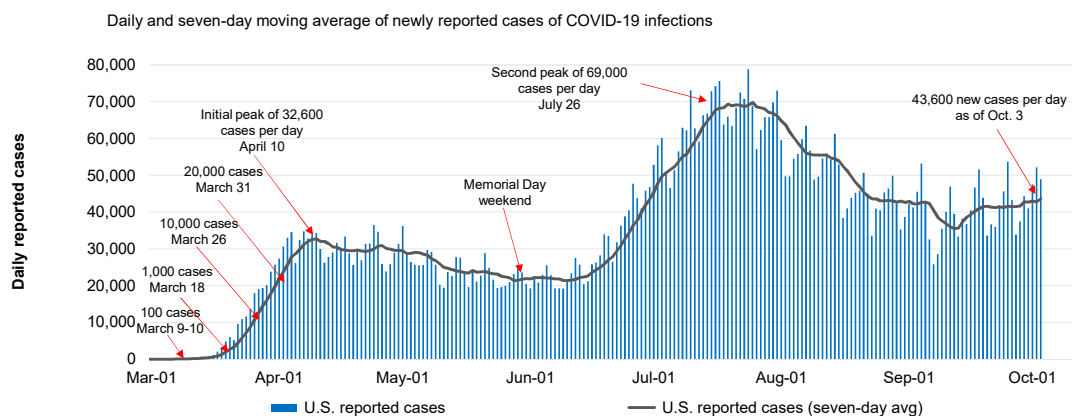


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U.S. daily reported coronavirus cases



Sources: Worldometers.info; RSM US

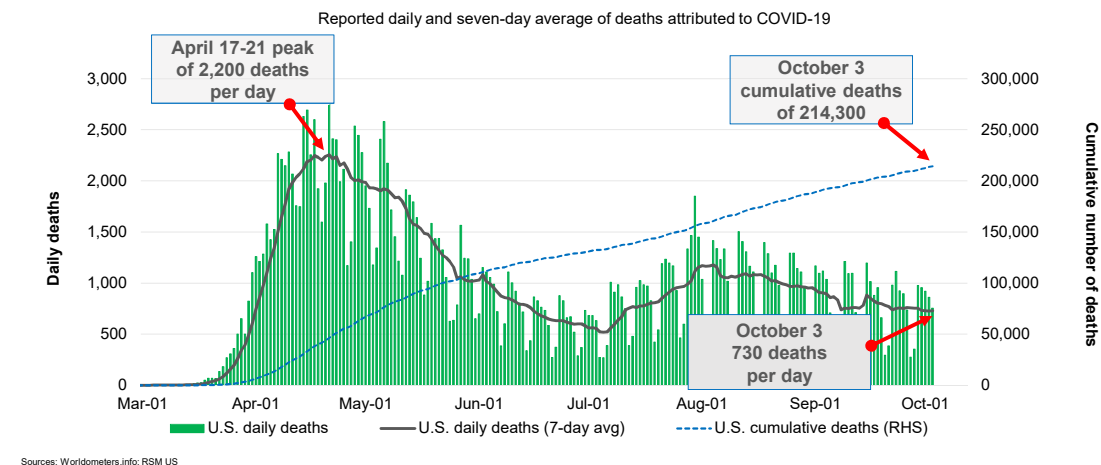


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U.S. daily and cumulative COVID-19 deaths



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U.S. outlook: What could go right?

Positive themes

• Growth acceleration

- Business investment awakens
- Innovation takes off
- 5G changes current urban vs rural divide (new demand driven)
- Health care spending as a percentage of GDP drops

• Employment growth solid

- Unemployment rate at historic low
- Wage growth resumes; household balance sheets clean for top two quintiles (60% of spending)

• Positive risks to the economic outlook

- Peak polarization passes; collaboration defines coming decades
- Policy addresses key challenges: labor-replacing technology, unbalanced growth (K-shaped economy)



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Starting the conversation

- What is the issue?
- Why does it matter?
- What are you going to do about it?



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Starting the conversation: *The Real Economy*

The Real Economy Cheat Sheet: May 2020

What is The Real Economy?

- The RSM US flagship publication, *The Real Economy*, was launched in January 2015 and provides economic analysis and insights about the productive side of the economy and the long-term investment that underscores the direction of growth, productivity and living standards in the United States.

What do we mean by "the real economy"?

- "The real economy" is that part of the economy organized around the production of goods and services, which accounts for about 40% of U.S. GDP and which employs one-third of the workforce.
- On a global basis, "the real economy" is an even larger component of worldwide growth.

The Real Economy: Volume 65

Curtailing the second wave: The case for a staggered reopening of the economy

By: Joseph Brusuelas

- As the number of coronavirus infections and deaths continued to rise in the U.S. in April, these figures presented a sobering reality. Despite the recent incremental decline in newly reported cases, Americans remain at risk. Recent relaxation of shelter-in-place orders being implemented by some states presents a clear risk for a second wave of the pandemic, according to epidemiological studies and related research. However, with a surge of people joining the ranks of the unemployed since late March, urgency to reopen the U.S. economy is mounting.



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Starting the conversation: The cheat sheet

Questions to engage your clients and contacts:

- What actions are you taking right now to address the impact of the coronavirus on your business?
- How long are you planning to manage the disruption?
- Have you taken advantage of emergency funding and do you require help in understanding terms and conditions, compliance, etc.?
- Are there tax implications or incentives that you should be considering during this time of recovery?
- How are your suppliers impacted during the outbreak, shutdown and eventual recovery?
- How are you managing incoming inventory?
- How can you scale down operations and position to scale back up?
- How are you communicating with and managing employees, both onsite and virtual?
- How are you enabling productivity for remote employees?
- How are you positioning the business for cash flow in a declining revenue market?

SERVICES CONSIDERATIONS

RSM services to further engage your clients and contacts:

- [Credits and incentives](#)
- [Contract compliance](#)
- [Private equity portfolio](#)
- [Business continuity and disaster recovery](#)
- [Cybersecurity and data privacy](#)
- [M&A advisory](#)
- [People and organization consulting](#)
- [Business intelligence](#)
- [Customer relationship management](#)
- [Application development and integration](#)
- [Enterprise resource planning](#)
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- For daily economic and industry insights visit [The Real Economy blog](#) at realeconomy.rsumus.com
- For more information on COVID-19, visit our [Coronavirus Resource Center](#), updated on a daily basis



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