Ruff going for GDP: What can be seen from the latest data?

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Photo: Ruffed Grouse, Pennsylvania State Bird, credit LisaTaylorPhoto
COVID-19 still dictating economic outcomes

New COVID-19 Cases
7D moving avg

- EU
- US
- LATAM
- Asia Pacific, excluding South Asia
  - South Asia: India, Pakistan, Bangladesh, Sri Lanka

Source: KPMG Economics, Johns Hopkins University (October 30, 2020), Bloomberg
U.S. sees case surge throughout the Midwest and West

New Daily Confirmed COVID-19 Cases – Seven-Day Moving Average

Note: Top nine states by 14-day % change in confirmed cases
Source: KPMG Economics, Johns Hopkins University (Oct. 29, 2020), Haver Analytics
Firewall needed until vaccine can restore full economic activity

Real GDP
Bil. 2012 $

Forecast

Recession
Fiscal/Monetary Assistance
Pre-Vaccine Rollercoaster Recovery
Post-Vaccine Recovery

Upside Scenario - Fiscal stimulus, unemployment benefits extended to 70 wks or more
Baseline
Downside Scenario - Surge in cases, fall in employment

Note: Forecasts are inherently time sensitive and projections are dated as of October 30, 2020.
Source: KPMG Economics, BEA (Q3 2020), Haver Analytics, Moody's
Firewall still needed around the COVID-19 impacted economy

Three Components of Fire
- Fuel
- Oxygen
- Heat

Fire Triangle

Three Components of Recession
- Income
- Loss
- Business Exit
- Financial
- Intermediation
- Impairment

Recession Triangle
COVID-19 Pandemic Causes Largest Real GDP Drop in History
U.S. Recession Cycles Indexed to Start of Recession

- The economic firewall created by the CARES Act assumed COVID-19 would be under control by Q3 2020.
- With COVID-19 cases rising in the U.S. and globally, a firewall to prevent larger economic fallout from the parts of the services economy still impacted is needed to prevent spillovers to services where workers can work from home as well as the goods economy.
- Based on current data, the swoosh shape recovery is the best case scenario.

Source: KPMG Economics, Bureau of Economic Analysis (Q3 2020), Haver Analytics
Unprecedented decline in service sector due to COVID-19

COVID-19 Unusual Shock to Services
U.S. Real Services Consumption Indexed to Start of Recession

Global Financial Crisis

COVID-19 Pandemic

Past Recessions

Pre-recession level

— Normally in recessions, the growth of services consumption slows but it does not decline below pre-recession levels.
— This is because demand for many services, such as utilities and healthcare, is maintained even if unemployment is high, largely due to a broad social safety net.
— During the pandemic, health care services consumption has dropped along with the consumption of many other services such as restaurants and in-person entertainment.
— Much of this consumption will only return if we get a handle on the virus.

Source: KPMG Economics, Bureau of Economic Analysis (Q3 2020), Haver Analytics

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Services normally comprise 44% - 47% of GDP

Services Component of GDP Far Below Recent Range

Source: KPMG Economics, Bureau of Economic Analysis (Q3 2020), Haver Analytics
Services consumption held back by FOGO

U.S. Public Transit Demand

- Balance between fear of missing out (FOMO) and fear of going out (FOGO) dictates aversion behavior.
- Public transit services are suffering due to FOGO.
- The ability to work remotely, aversion behavior (FOGO), and the high level of unemployment are among the primary reasons for underutilized public transport.
- Even in cities with limited formal restrictions, such as Dallas, an increase in virus cases holds back economic activity.

Source: KPMG Economics, Moovit, Bloomberg (October 28, 2020)

Note: baseline comparison with week of Jan 15, 2020
Pandemic has shifted where people spend their time

United States: Change in Visits to Community Areas
Change Relative to Jan 5 - Feb 6 Baseline

- Parks
- Residential
- Grocery & Pharmacy
- Retail & Recreation
- Transit Stations
- Workplaces

Source: KPMG Economics, Google Community Mobility Trends (October 27, 2020), Haver Analytics
FOGO and restricted capacity determine restaurant recovery

OpenTable’s statistics on seated diners at restaurants provide a valuable barometer of people’s willingness to engage in activities in close proximity to others.

On April 27, 2020, the first U.S. cities began allowing some restaurants to reopen, although under strict controls that limit capacity.

Many restaurants may struggle to remain going concerns without continued government assistance.

| Source: OpenTable, Worldometers (November 2, 2020) |
|---|---|---|---|---|---|---|---|---|---|---|
| State | 9/15 to 9/21 | 9/22 to 9/28 | 9/29 to 10/5 | 10/6 to 10/12 | 10/13 to 10/19 | 10/20 to 10/26 | 10/27 to 11/1 | State cases/1M |
| Arizona | Phoenix | -50% | -46% | -42% | -46% | -49% | -46% | -46% | 34,000 |
| | Scottsdale | -27% | -25% | -20% | -20% | -18% | -14% | -13% | 32,946 |
| | Las Vegas | -39% | -38% | -40% | -32% | -37% | -34% | -29% | 37,593 |
| Florida | Fort Lauderdale | -24% | -23% | -9% | -20% | -23% | -25% | -26% |  |
| | Naples | -12% | -7% | -2% | -19% | -20% | -25% | -30% |  |
| | Tampa | -26% | -24% | -16% | -17% | -18% | -23% | -16% |  |
| | Miami | -37% | -34% | -23% | -25% | -30% | -27% | -22% |  |
| | Atlanta | -47% | -45% | -39% | -42% | -41% | -43% | -34% |  |
| | Austin | -42% | -40% | -28% | -31% | -35% | -35% | -38% |  |
| | Dallas | -44% | -42% | -36% | -38% | -38% | -40% | -36% |  |
| | Houston | -21% | -37% | -29% | -31% | -32% | -32% | -31% |  |
| Texas | Nashville | -56% | -57% | -47% | -46% | -48% | -50% | -48% |  |
| | New Orleans | -59% | -61% | -53% | -64% | -57% | -60% | -67% |  |
| | Charlotte | -36% | -37% | -27% | -34% | -30% | -33% | -30% |  |
| | Raleigh | -58% | -56% | -42% | -50% | -50% | -50% | -53% |  |
| | Baltimore | -56% | -61% | -40% | -56% | -54% | -54% | -58% |  |
| | New York | -66% | -61% | -58% | -62% | -62% | -61% | -69% |  |
| | Cincinnati | -32% | -34% | -13% | -35% | -39% | -33% | -30% |  |
| | Columbus | -31% | -30% | -28% | -34% | -36% | -40% | -40% |  |
| North Carolina | Boston | -58% | -54% | -48% | -52% | -58% | -54% | -63% |  |
| | Raleigh | -81% | -76% | -77% | -77% | -78% | -77% | -77% |  |
| | Portland | -72% | -66% | -60% | -63% | -65% | -67% | -64% |  |
| | Denver | -34% | -34% | -26% | -28% | -34% | -42% | -32% |  |
| | Louisville | -47% | -65% | -50% | -49% | -54% | -49% | -47% |  |
| | Los Angeles | -71% | -68% | -68% | -68% | -66% | -66% | -61% |  |
| | San Francisco | -85% | -84% | -82% | -82% | -78% | -79% | -74% |  |
| California | Source: OpenTable, Worldometers (November 2, 2020) |  |  |  |  |  |  |  |
Air travel volumes remain down around 60% y/y

U.S. TSA Checkpoint Passenger Volume
7-Day Moving Average

Source: KPMG Economics, TSA, Bloomberg (October 29, 2020)
COVID-19 shock caused dramatic shift to goods consumption

Multiple factors contributed to the increase in consumption of goods.

- Pandemic assistance boosted spending power and contributed to the rebound in autos.
- More time at home, FOGO, boosted demand for goods that improved the quality of home life.
- Increased churn in the housing market boosted demand for furniture and other home goods.
- Demand is not expected to be sustained at this pace.

Source: KPMG Economics, Census Bureau (Q3 2020), Haver Analytics
FOGO drives increased need for housing utility

Loan Applications Rise with Mortgage Rate Decline

Source: KPMG Economics, Mortgage Bankers Association (October 23, 2020), Bureau of Economic Analysis (Q3 2020), Haver Analytics

Recession
## Retail Sales by Industry

<table>
<thead>
<tr>
<th>Retail Industry</th>
<th>12-Month % Change</th>
<th>1-Month % Change</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Jun</td>
<td>Jul</td>
</tr>
<tr>
<td>Total Retail Sales</td>
<td>2.2%</td>
<td>2.7%</td>
</tr>
<tr>
<td>Clothing &amp; Accessory Stores</td>
<td>-24%</td>
<td>-23%</td>
</tr>
<tr>
<td>Food Services &amp; Drinking Places</td>
<td>-22%</td>
<td>-19%</td>
</tr>
<tr>
<td>Gasoline Stations</td>
<td>-19%</td>
<td>-17%</td>
</tr>
<tr>
<td>Electronics &amp; Appliance Stores</td>
<td>-20%</td>
<td>-6%</td>
</tr>
<tr>
<td>Miscellaneous Stores Retailers</td>
<td>-2%</td>
<td>3%</td>
</tr>
<tr>
<td>Furniture &amp; Home Furnishing Stores</td>
<td>0%</td>
<td>3%</td>
</tr>
<tr>
<td>Health &amp; Personal Care Stores</td>
<td>-1%</td>
<td>4%</td>
</tr>
<tr>
<td>Motor Vehicle &amp; Parts Dealers</td>
<td>8%</td>
<td>7%</td>
</tr>
<tr>
<td>General Merchandise Stores</td>
<td>3%</td>
<td>2%</td>
</tr>
<tr>
<td>Sporting Goods, Hobby, Book &amp; Music Stores</td>
<td>22%</td>
<td>17%</td>
</tr>
<tr>
<td>Food &amp; Beverage Stores</td>
<td>12%</td>
<td>11%</td>
</tr>
<tr>
<td>Building Materials, Garden Equipment &amp; Supply Dealers</td>
<td>20%</td>
<td>16%</td>
</tr>
<tr>
<td>Nonstore Retailers (Online Sales)</td>
<td>24%</td>
<td>24%</td>
</tr>
</tbody>
</table>

Source: KPMG Economics, Census Bureau (September 2020), Haver Analytics
COVID-19 purchases hint a limit for online sales

**E-Commerce as a Share of Retail Sales**

- Electronic & Mail Order Sales as a % of Non-gasoline Store Retail Sales

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Aversion behavior and lockdown procedures forced many stores to close during the early stages of the pandemic.

- Consumers responded by cutting their spending at brick and mortar stores and significantly increasing their online purchases.

- The online share of retail sales peaked at 19% in April from 12.5% prior to the pandemic.

- Note: We exclude gasoline store sales because these sales must occur in person at the gas pump.

Source: KPMG Economics, Census Bureau (August 2020), Haver Analytics
Surge in online sales varies significantly by industry

Online Sales as a % of Industry Retail Sales

- Clothing and clothing accessories
- Furniture and home furnishings
- Miscellaneous including gasoline stations
- Sporting goods, hobby, musical instrument and books
- General merchandise
- Building materials, garden equipment and supplies
- Motor Vehicles and Parts
- Food and beverage
- Health and personal care

Source: KPMG Economics, Census Bureau (Q2 2020), Haver Analytics
COVID-19 impacts different sectors than the 08-09 crisis

Total Change in Employment by Industry
% Change during Recession Period

Leisure & Hospitality
Mining and Logging
Health Care & Social Assistance
Utilities
Finance & Insurance Services
Real Estate
Retail Trade
Professional & Technical Services
Administrative & Waste Services
Manufacturing
Construction

COVID-19 Pandemic
Global Financial Crisis

Source: KPMG Economics, Bureau of Labor Statistics (September 2020), Haver Analytics

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Impact of pandemic lingers, especially for small businesses

Three-quarters of SMEs Still Experiencing Negative Shock
Pandemic Effect on Business, % of Firms

Source: KPMG Economics, U.S. Census Bureau, Haver Analytics
Looking Past the Pandemic
Economists become more optimistic about growth path

**Recovery Shape of Economist Forecasts**

WSJ October 2020 Economist Survey, KPMG Shape Classification

Source: KPMG Economics, WSJ October 2020 Survey 62 responses
However variance gives indication of growth contour

— Most prominent economists are seeing a swoosh recovery path.
— In the most recent October survey, forecasts for the next year have converged to show a tighter variance versus earlier surveys.
— When viewed on a year-over-year basis, quarterly GDP gains in Q3 do not make up for the weakness in Q1 & Q2. We are still 2/3 below pre-pandemic GDP levels.

### Forecast vs Actual

<table>
<thead>
<tr>
<th>Quarter</th>
<th>Forecast</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q1</td>
<td>0.3%</td>
<td>-9.0%</td>
</tr>
<tr>
<td>Q2</td>
<td>-9.0%</td>
<td>-2.9%</td>
</tr>
<tr>
<td>Q3</td>
<td>-2.9%</td>
<td></td>
</tr>
</tbody>
</table>

Source: KPMG Economics, Macroeconomic Advisors by IHS, WSJ Economist Survey October 2020
The rubber meets the road with jobs forecasts

<table>
<thead>
<tr>
<th>Nonfarm Payroll Growth</th>
<th>Average of the Monthly Change for the Next Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Top 5 Average</td>
<td>1,112,704</td>
</tr>
<tr>
<td>Average</td>
<td>705,590</td>
</tr>
<tr>
<td>KPMG</td>
<td>460,462</td>
</tr>
<tr>
<td>Bottom 5 Average</td>
<td>299,043</td>
</tr>
</tbody>
</table>

Source: KPMG Economics, Macroeconomic Advisors by IHS, WSJ Economist Survey October 2020

The recovery path of labor markets is highly dependent on the path of the virus and government policies to control the spread.

With COVID cases presently rising rapidly throughout the U.S., we forecast economic activity to slow in the winter months as lockdowns increase and FOGO (fear of going out) leads to greater aversion behavior.

Additionally, government stimulus that preserves incomes and spending is key to the economic outcome.

Our concern around lack of stimulus and growing COVID cases is reflected in our below consensus payroll forecast.
The key to yields is potential Fed yield curve control

Economists’ interest rate forecasts depend in large part on their assumptions regarding additional stimulus and the impact on jobs and inflation.

KPMG assumes a combination of weak global conditions, very slow U.S. growth, low inflation, and Fed action (if necessary) will keep long-term interest rates low to spur growth.

10-Year U.S. Treasury Bond Yield

Forecast

- Top 5 Average
- Average
- Bottom 5 Average
- KPMG

Source: KPMG Economics, Macroeconomic Advisors by IHS, WSJ Economist Survey October 2020
Pandemic is disproportionately hurting lowest income HHs

**Expected Loss of Employment Income**
Next four weeks, surveyed week of 10/13

- 23% of households expect a loss of employment income in the next four weeks

**Difficulty Paying Usual Expenses**
Last seven days, surveyed week of 10/13

- 32% of households had some difficulty in paying usual household expenses in the last seven days

Source: KPMG Economics, U.S. Census Bureau, Haver Analytics
Anatomy of a K – the growth rate does not tell the story

- Can Work From Home – 4.8% Unemployment Rate
- Bachelor’s Degree or Higher – $72,000 Median Income
- Total Assets (51st to 90th Percentile) – $740,000
- Home Ownership Rate (Above Median Income) – 80.5%

- High Density/Work at Employer – 9.4% Unemployment Rate
- Less than Bachelor’s Degree – $39,000 Median Income
- Total Assets (0 to 50th Percentile) – $94,000
- Home Ownership Rate (Below Median Income) – 55.2%

Economists have termed the uneven impact of the pandemic a K shaped recovery, meaning it is a recovery for the top leg of the K and not for the bottom leg.

- Unemployment is highest in the services industry where workers tend to need less than a bachelor’s degree.
- The average leisure and hospitality worker earns below $36,000/year, putting them below the national median income and in the bottom portion of the K.

Source: KPMG Economics, Bureau of Labor Statistics, Census Bureau, Federal Reserve Board, Haver Analytics
Fiscal relief has been significant, but more needed

The U.S. entered the COVID-19 crisis with a high budget deficit (-4.6% in 2019) and high debt levels (102% of GDP).

The considerable fiscal relief required to bridge the economy past COVID-19 and prevent a depression raised the FY20 budget deficit to -16.1%.

Similar to the WWII fiscal spending, the present situation corresponds to a sharp increase in savings and search for productivity enhancements by organizations.

It may be worthwhile to revisit some of the post-WWII policies that elevated education levels and improved infrastructure, enabling the post-war productivity boom.

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Fiscal Response Added to High Pre-Crisis Deficit Levels
Budget Balance as a % of GDP

- 2020 Fiscal Year
- WWII Average (1942-1945)
- GFC (2009)
- Post-GFC Average (2010-2012)
- 1983
- 1934

Source: KPMG Economics, U.S. Treasury Department, Federal Reserve Board, Haver Economics
Massive savings increase finances the fiscal deficit

- Savings have risen for several reasons:
  - consumers are consuming less high-contact services such as recreation, dining out, and health care.
  - consumers are engaging in precautionary savings as future visibility on the economy is limited.
- Once the virus is tamed, savings will likely be a catalyst for renewed economic activity provided further economic deterioration can be forestalled until then.

Source: KPMG Economics, Bureau of Economic Analysis (September 2020), Haver Analytics
Without income support, this picture would look very different

NBER Dating Committee Recession Indicators
Logged and Indexed, June 2009=0

- Total Nonfarm Employment
- Real Personal Income ex. Transfers
- Industrial Production
- Real Manufacturing & Trade Sales
- Gross Domestic Product

Recession

— Key economic indicators followed by the National Bureau of Economic Research (NBER) to conduct business cycle dating reveal the sharp drop in economic activity due to the shock of the pandemic.

— The NBER Business Cycle Dating Committee declared that the current recession began in February 2020.

— Job losses from the pandemic erased all of the gains from the prior expansion at the nadir.

Source: KPMG Economics, Macroeconomic Advisors by IHS Markit, BEA, BLS, Haver
Note: Data are logged and indexed. Data are seasonally adjusted. Total sales is Real Manufacturing & Trade Sales for All Industries
Income support buoyed consumption and all other factors

One of the indicators used by the dating committee is real personal income excluding transfers; this excludes federal and state unemployment benefits, and any other benefits to households such as social security or disability payments.

Normally unemployment benefits boost income slightly at the outset of a recession and then fall during a recovery.

The extraordinary increase in benefits during COVID-19 boosted household incomes more than normal (dotted blue line). This has provided significant support to consumers and helped maintain consumption rates.
The monetary policy response is unprecedented

The Federal Reserve Leads the Way on Monetary Policy
Money Supply: M2

— The Federal Reserve acted swiftly to provide liquidity and increase money supply, going well beyond what was supplied during the global financial crisis.

— China was the world’s monetary engine post-global financial crisis. During COVID-19, the U.S. is the world’s monetary engine.

— The Federal Reserve is acting in its role as lender of last resort in two key ways: direct purchases of fixed income securities (Treasuries, Agencies MBS, Municipal Bonds, Corporate Fixed Income) and creating lending facilities for corporations.

Source: KPMG Economics, Bank of Japan, European Central Bank, Federal Reserve Board, Haver Analytics (Sept. 2020)
Significant lending boost evident as firms accessed credit lines

Commercial & Industrial Loans in Bank Credit: All Commercial Banks

Source: KPMG Economics, Federal Reserve Board (September 2020), Haver Analytics
Federal Reserve action reduced cost of capital for large firms

U.S. Corporate Bond Credit Spreads

Note: CPFF: Commercial Paper Funding Facility, PMCCF: Primary Market Corporate Credit Facility, SMCCF: Secondary Market Corporate Credit Facility
Source: KPMG Economics, Bloomberg (October 29, 2020)
Despite broad improvement, two sectors still under duress

High Yield Credit Spreads vs. Corporate Leverage

Note: Bubble size represents total outstanding high yield debt by market value.
Source: KPMG Economics, Bloomberg (October 30, 2020)
The pace of corporate bankruptcy filings has slowed for large companies in recent months. October 2020 totaled 17, the same as in September 2020, and 20 in August 2020.

This compares to a peak of 32 filings in July 2020, which nearly matched the GFC high of 33 (March 2009).

Comparing 2020 to the peak year during the GFC in 2009, bankruptcies are running at 80% of the 2009 pace.

Another significant difference is that Chapter 11 filings, those that indicate reorganizations, have risen to be 28% of filings in September 2020 (vs. 13% in 2009) and Chapter 7 filings have fallen to 56% vs. 68% in 2009.
FOMO vs FOGO seen in the clear winners and losers

Industries that struggle to recover from COVID-19 due to a combination of lower demand offerings, insufficient capital and high debt will likely experience a hard reset to their businesses.

Some firms are poised to surge despite the overall adverse operating conditions. These firms have strong balance sheets and can capitalize on consumer behavior that has been altered during the crisis.

Most organizations need to transform in order to emerge from the impact of the pandemic in a position that allows them to thrive and operate effectively in what is likely to be an altered landscape.

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**S&P 500 Industry Valuations vs. Leverage**

- **Hard Reset**
  - Apparel & Textile Products

- **Surge**
  - Medical Equipment & Devices
  - Internet Media & Svcs

- **Transform to Re-emerge**
  - Leisure Products
  - Food Production
  - Whl - Cons Staples
  - Transportation & Logistics
  - Aerospace & Defense
  - Retail - Cons Disc
  - Construction Materials
  - Chemicals
  - Electronic Equipment
  - Biotechnology & Pharmaceuticals
  - E-Commerce Disc
  - Internet Media & Svcs

- **Modified Business as Usual**
  - Home Construction
  - Entertainment Content
  - Technology Hardware
  - Transportation Equipment
  - Specialty Finance
  - Asset Management
  - Health Care Facilities
  - Automotive
  - Steel

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*Note: EBITDA and Net Debt (most recent quarterly filing), EV (October 7, 2020), dotted lines = median values*

*Source: KPMG Economics, Bloomberg LLP*
Do low real rates run risk of sustaining zombie firms?

Zombie Companies
Percent in Russell 3000

Note: Bank of International Settlements defines zombie firms as firms with interest coverage ratio less than one for more than three years; 4Q moving average
Source: KPMG Economics, Bloomberg (Q2 2020)
It is not always the same zombies

Pre-tech Bubble Zombie Firms by Sector (Dec 31, 1999)

- Technology: 27%
- Health Care: 19%
- Consumer Discretionary: 13%
- Industrials: 3%
- Materials: 3%
- Consumer Staples: 3%
- Energy: 2%
- Utilities: 0.3%
- Communications: 30%

Pre-GFC Zombie Firms by Sector (June 30, 2007)

- Health Care: 34%
- Technology: 19%
- Consumer Discretionary: 13%
- Communication: 12%
- Consumer Staples: 12%
- Utilities: 1.6%
- Energy: 7%
- Industrials: 6%
- Materials: 2%

Note: Russell 3000 companies with interest coverage ratio less than one for more than three years
Source: KPMG Economics, Bloomberg
Is all zombification bad or does it just mean a long R&D cycle?

2020 Zombie Firms by Sector

- Health Care: 42%
- Technology: 19%
- Consumer Discretionary: 10%
- Communications: 8%
- Industrials: 8%
- Energy: 7%
- Materials: 3%
- Consumer Staples: 3%
- Utilities: 0.5%
- Energy: 7%

Note: Russell 3000 companies with interest coverage ratio less than one for more than three years
Source: KPMG Economics, Bloomberg (Q2 2020)
Low rate environment should help support M&A transactions

US M&A Value/S&P500 Market Cap
(3mma)

M&A incl. minority investment, joint ventures, buybacks
Source: KPMG Economics, Bloomberg (September 2020)
2020 M&A activity led by healthcare ($241bn/$1.3tn)

### U.S. M&A Value (2020)
- **$85bn** Basic Materials (6%)
- **$85bn** Energy (7%)
- **$190bn** Financial (16%)
- **$315bn** Consumer Noncyclical (23%)
- **$218bn** Consumer Cyclical (9%)
- **$162bn** Biotechnology
- **$162bn** Pharmaceuticals
- **$162bn** Healthcare Products
- **$162bn** Healthcare Services
- **$162bn** Food
- **$162bn** Beverages
- **$162bn** Cosmetics/Personal Care
- **$162bn** Agriculture
- **$162bn** Household Products
- **$11bn** Basic Materials (1%)
- **$0.6bn** Diversified

### U.S. M&A Value (2019)
- **$119bn** Consumer Cyclical (9%)
- **$165bn** Utilities (12%)
- **$96bn** Industrial (7%)
- **$128bn** Energy (6%)
- **$613bn** Consumer Noncyclical (33%)
- **$22bn** Basic Materials (1%)
- **$0.4bn** Diversified
- **$186bn** Utilities (10%)
- **$166bn** Consumer Cyclical (9%)
- **$114bn** Industrial (6%)
- **$219bn** Communications (12%)
- **$219bn** Technology (14%)
- **$221bn** Financial (13%)
- **$186bn** Communications (12%)
- **$219bn** Technology (14%)
- **$221bn** Financial (13%)

Source: KPMG Economics, Bloomberg (Sept 2020 YTD), Total = $1.362tn

Source: KPMG Economics, Bloomberg (Sept 2019 YTD), Total = $1.869tn
Business formation rebound funded by savings and low rates

Change in Cumulative New Business Applications
Likely Employers - YoY Change in Cumulative Total

- 2019 to 2020
- 2017-2019 Average
- 2008-2009 Average

Source: KPMG Economics, U.S. Census Bureau
Real interest rates forecast to be negative for many years

— Short-term real interest rates are expected to remain in negative territory for an extended period.

— The Federal Reserve will do all it can to promote economic growth in order to return the economy to full employment.

— The anticipated prolonged duration of the economic recovery and the lack of meaningful inflation means the yield curve is likely to remain flat.

— On a real basis, longer-term interest rates will also join their shorter-term counterparts in negative territory in the years immediately ahead.

Inflation not a concern due to significant demand shock

— The significant drop in output is more of a cause for worry about deflation than inflation, despite record levels of monetary and fiscal stimulus.

— Low inflation environments can reduce demand as low inflation expectations can lead to delayed consumption, low interest rates and increased savings rates.

— Stimulating demand in the face of a pandemic, which lowers both demand and income levels, is challenging. Full demand will return when medical solutions are in place.

— Often countries will engage in a “beggar thy neighbor” stimulus that weakens their currency to stimulate growth and inflation.

Source: KPMG Economics
Concluding Thoughts

• The pandemic is both a supply shock and a demand shock with the demand shock dominating economic activity.

• The demand shock has adversely impacted services consumption in Q3 due largely to FOGO inhibiting the demand for in-person activities at the same scale as prior to the pandemic.

• The demand shock has positively impacted goods consumption in Q3, due largely to FOGO increasing the demand for home improvements as well as fiscal assistance that boosted consumption of big ticket items such as autos.

• The demand for goods is unlikely to be sustained at the Q3 pace while the demand for services is at risk in the U.S. and Europe as the number of virus cases and deaths continue to rise.
  • The combination of these factors suggest there are significant risks to the pace of the U.S. recovery.
  • Our base case remains a tepid, nearly flat, pace of growth until there is a vaccine.

• An additional fiscal stimulus is needed to shore up the firewall around the COVID impacted parts of the economy.

• The Fed is expected to maintain loose monetary policy until inflation is sustained above 2%, something that will likely not occur until the output gap is closed and we are back above trend GDP levels.
Thank you

For more information, please see KPMG’s Covid-19 resource page:
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