ECONOMIC AND FINANCIAL DIGEST

LANTERN INVESTMENTS, INC.

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R.I.P: The Longest Expansion

The U.S. as well as the global economy has descended into the harshest recession since the Great Depression. The descent from positive growth has been more abrupt and unexpected than anyone could have imagined. About two months ago, when the Covid-19 coronavirus first hit the headlines we, along with most economists, thought the nation could weather the storm if proper policies were quickly implemented and the outbreak contained before becoming a global pandemic. Bolstering this optimistic assessment, the U.S. economy was cruising along, albeit at a lackluster pace, before the shock struck like a thunderbolt. The job market was humming, generating more paychecks in January and February than expected, consumer confidence remained elevated and the financial markets were pricing in continued growth in activity and earnings, although at a diminished pace. Indeed, stock prices hit a record high on February 19.

Simply put, it was thought that the economy had enough of a cushion to absorb a temporary setback. But hopes for a “soft landing” came crashing down as cases of the virus spread like wildfire and fear gripped the public. Ultimately, social-distancing mandates by the Federal and local governments to contain outbreaks delivered the fatal blow to the economy, prompting households to self-quarantine, factories to shut down and small businesses to close for lack of foot traffic. Daily life ground to a halt, as did commerce, and the financial markets got swallowed up in a tumultuous firestorm. In the space of a few weeks, the stock market gave up all of its gains achieved since President Trump’s inauguration and the Federal Reserve resurrected and then expanded the emergency measures employed during the financial crisis, including slashing interest rates back to zero, reviving asset purchases on a massive scale and establishing lending facilities to prevent critical sectors of the financial markets from seizing up.

Adding to the economy-crushing impact of the pandemic, another oil price war broke out between Russia and Saudi Arabia, sending oil prices plunging and leaving the energy industry in shambles. The precipitous fall in oil prices put more downward pressure on inflation and inflationary expectations, giving the Federal Reserve extra urgency and leeway to jump-start growth. But the Fed is already operating at full throttle, and more of the heavy lifting is now being passed on to Washington. While the gargantuan package of fiscal measures announced in recent weeks should help contain the carnage, the crisis will not end until the pandemic is brought under control, something that requires the heroic efforts of health experts more than policy makers.

End Of An Era

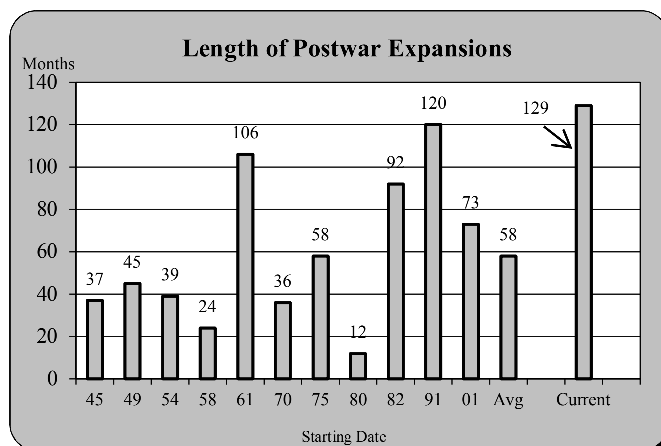
The longest U.S. economic expansion on record has come to an end. After growing for over 10 years, the economy entered contraction territory in mid-March when a perfect storm of depressants on demand and supply coalesced to shut down virtually all forms of business activity. Not in recorded history has the fall from grace been as swift and brutal as the one now unfolding. While the economy may have been in decent shape prior to the coronavirus outbreak, it certainly was not immune to its effects.

We expect the economy to contract by an record double digit pace in the second quarter and unemployment to soar to levels not seen since the 1930s. The existential threat the pandemic poses to the economy has mobilized Congress, the Fed and the administration into a frenzy of policy moves that boggles the mind.

But while desperate times warrant desperate measures, these extreme policy moves are not designed to combat the pandemic wreaking havoc on the economy. Instead, they are meant to contain the economic fallout and provide all the ingredients needed to jump-start growth once the virus is brought under control. Until that outcome is realized, the depth of the economic downturn now unfolding can only be guessed at.

The Worst Is Yet To Come

Since the severity and duration of the coronavirus remains unknown, it is almost impossible to assess how much damage it will impose on the economy. But given the abrupt shutdown in activity that took place over the second half of March, there is little question that the second quarter will be starting off in a deep hole. Some projections are already off the charts for the period, pegging



a contraction in GDP of as more than 30 percent at an annual rate. That's a freefall not even approached during the Great Depression.

Even the administration is no longer putting on a brave face, as Treasury Secretary Mnuchin hinted that unemployment could soar to 20 percent in the most dire of circumstances. Needless to say, legislators are moving swiftly and aggressively to prevent the worst-case scenario from happening. The list of preventive measures rolling out of Capitol Hill is both breathtaking as it is groundbreaking, including sending checks directly to households, providing copious aid to small businesses and propping up the most severely-impacted industries, most notably the airlines. The price tag for the bailout measures so far plus proposals currently being considered in Congress is estimated to total over $5 trillion, about 25% of the economy.

As enormous as that sum is, it is not generating the partisan scorn that legislative proposals have usually incited in this highly polarized Congress. One reason, of course, is that there is bipartisan sentiment to stave off what could be the worst calamity to hit the American economy since the depression of the 1930s. Another is more practical. Many believe that with interest rates at historically low levels, the government can borrow as cheaply as never before. If this isn't the time to take on more debt, when is?

Back To The Future

Some are comparing the current crisis to the 2008-2009 Great Recession and global financial crisis. But there are a few big differences. For one, the media coverage of the last recession did not include a daily mortality rate, which is stoking widespread fear and a wartime bunker mentality into the mindset of the nation and its leaders. While that is having a more jarring impact on the economy and creating more immediate carnage, it is also mobilizing policymakers into a greater sense of urgency and cooperation than was the case a decade ago.

For another, the 2008-09 episode posed a more existential threat to the economy as the financial system — the economy's lifeblood - was exceptionally fragile and under attack from a housing collapse and mountain of failing subprime loans. It took time for policymakers to acknowledge the magnitude of the threat and only then did they embark on a series of unprecedented measures to save banks and other institutions and keep vital credit flowing to households and businesses. Back then, the Fed and fiscal authorities were learning on the fly; but that experience provides current policymakers with a blueprint to draw on. Meanwhile, new regulations and legislative oversight since the financial crisis have prodded banks and other institutions to build up capital and reserves, putting them in a stronger balance sheet position to weather adversity.

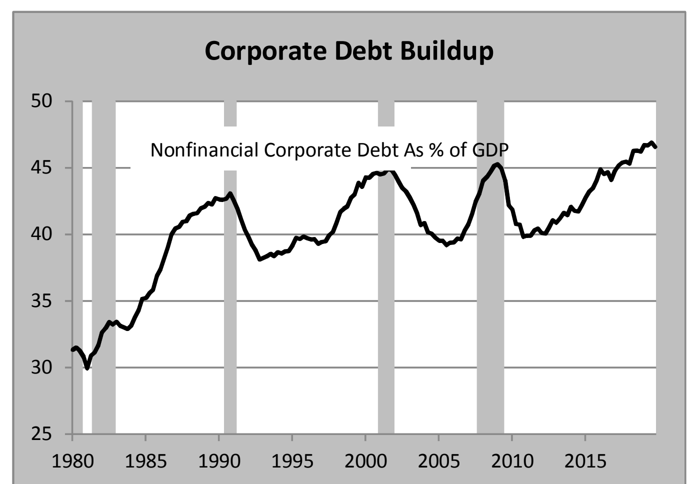
But while most financial institutions are not in danger of collapsing as they were a decade ago, the capital markets are coming under considerable stress, weighed down from years of turbo-charged debt financing from corporations taking advantage of historically low interest rates. A major share of corporate bond issuance in recent years has come from companies with a lower credit rating, which makes them a riskier asset when the economy - and hence earnings - weakens. Until the coronavirus struck that was not a concern, as investors were willing to trade risk for yield in a healthy economy. But that trade-off has now been flipped. Investors are running for the hills, shunning risky assets for safe havens, most notably Treasury securities, sending corporate bond yields sky-high relative to government yields. With hundreds of billions of dollars of these issues coming due over the next year, many companies will not be able to refinance maturing debt, raising the prospect of cascading defaults and bankruptcies.

Massive Policy Response

The potential liquidity crisis emerging in the debt markets has spurred the Federal Reserve into action, much as it did during the financial crisis. In addition to slashing its policy rate to near zero and reviving the asset purchase program, it also relaunched a number of funding facilities to support the commercial paper market, money market funds and primary dealers that can use municipal bonds and a range of other securities as collateral to obtain funds. There is every chance the Fed will also ask Congress for authority to purchase corporate bonds directly, which would help stem the prospective turmoil that would otherwise occur as investors shun these securities.

To be sure, the enormous fiscal and monetary stimulus that is flooding the economy and financial system is aimed at jump-starting economic growth after the pandemic runs its course as much as limiting the carnage that is already baked in. Assuming the coronavirus is contained over the summer, the economy should snap back to life late in the year, with GDP posting decent gains by the fourth quarter. Admittedly, that optimistic assessment assumes the fallout from the carnage now being felt in the economy and financial markets does not leave a lasting scar that impairs consumer and business behavior over the longer term. Some believe that the harsh recession a decade ago is at least partly responsible for the economy's subpar - albeit lengthy-recovery, as memories of the wealth destruction and surge in unemployment prompted consumers to restrain spending more than they otherwise would have.

But the last recession stretched out over a lengthy 18-month period and the maladies that brought the economy to its knees took a long time to heal. The current downturn should be much shorter but its catalyst may well have a lasting effect on economic behavior even after a cure is found. Indeed, the new normal won't look much like the old one. As Dr. Anthony Fauci said in a recent press conference: "If back to normal means acting like there never was a coronavirus problem, I don't think that's going to happen until we completely protect the population." Unlike a light switch that's flipped on instantly, this recovery will resemble a dimmer that's gradually eased up over months.



KEY ECONOMIC AND FINANCIAL INDICATORS

*FINANCIAL INDICATORS**

	March	February	January	December	November	October	September	12-Month Range High	12-Month Range Low
Prime Rate	3.81	4.75	4.75	4.75	4.75	4.99	5.15	5.50	3.81
3-Month Treasury Bill Rate	0.29	1.52	1.52	1.54	1.54	1.65	1.89	2.38	0.29
5-Year Treasury Note Rate	0.59	1.32	1.56	1.68	1.64	1.53	1.57	2.33	0.59
10-Year Treasury Note Rate	0.87	1.50	1.76	1.86	1.81	1.71	1.70	2.53	0.87
30-Year Treasury Bond Rate	1.46	1.97	2.22	2.30	2.28	2.19	2.16	2.94	1.46
Tax-Exempt Bond Yield	2.54	2.44	2.59	2.75	2.82	3.68	2.81	3.82	2.44
Corporate Bond Yield (AAA)	3.02	2.78	2.94	3.01	3.06	3.01	3.03	3.69	2.78
Conventional 30-Year Mortgage Rate	3.45	3.47	3.62	3.72	3.70	3.69	3.61	4.14	3.45
Dow Jones Industrial average	22637	28520	28880	28167	27797	26737	26900	28880	22637
S&P 500 Index	2652	3277	3278	3177	3105	2978	2982	3278	2652
Dividend Yield (S&P)	2.30	2.07	1.88	1.86	1.90	1.95	1.98	2.30	1.86
P/E Ratio (S&P)	17.0	19.4	21.2	21.3	20.9	20.2	19.7	21.3	17.0
Dollar Exchange Rate (vs. Major Currencies)	121.3	116.7	115.3	115.9	116.6	116.8	117.4	121.3	114.8

** Monthly Averages*

ECONOMIC INDICATORS

	March	February	January	December	November	October	September	12-Month Range High	12-Month Range Low
Housing Starts (In Thousands)		1599	1624	1601	1381	1340	1266	1624	1199
New Home Sales (Thousands of Units)		765	800	724	700	707	725	800	598
New Home Prices (Thousands of Dollars)		346	325	328	328	322	316	346	308
Retail Sales (% Change Year Ago)	-6.2	4.6	5.1	5.4	3.3	3.1	4.0	5.4	-6.2
Industrial Production (% Change Year Ago)		0.0	-1.0	-0.9	-0.4	-0.8	-0.2	2.3	-1.0
Operating Rate (% of Capacity)		77.0	76.6	77.1	77.5	77.0	77.4	78.4	76.6
Inventory Sales Ratio (Months)		1.37	1.37	1.40	1.39	1.40	1.40	1.40	1.37
Real Gross Domestic Product (Annual % Change)				2.1			2.1	3.1	2.0
Unemployment Rate (Percent)	4.4	3.5	3.6	3.5	3.5	3.6	3.5	4.4	3.5
Payroll Employment (Change in Thousands)	-701	275	214	184	261	185	208	275	-701
Hourly Earnings (% Change Year Ago)	3.1	3.0	3.1	3.0	3.3	3.2	3.1	3.5	3.0
Personal Income (% Change Year Ago)		4.0	4.0	3.7	4.4	4.1	4.3	4.8	3.7
Savings Rate (Percent of Disposable Income)		8.2	7.9	7.5	7.8	7.7	7.8	8.4	7.4
Consumer Credit (Change in Blns. Of Dollars)		22.3	12.1	21.0	7.4	13.4	10.8	23.0	7.4
Consumer Prices (% Change Year Ago)	1.5	2.3	2.5	2.3	2.1	1.8	1.7	2.5	1.5
CPI Less Food & Energy (% Change Year Ago)	2.1	2.4	2.3	2.3	2.3	2.3	2.4	2.4	2.0
Wholesale Prices (% Change Year Ago)	0.7	1.3	2.1	1.3	1.1	1.1	1.4	2.2	0.7

LANTERN'S BOND OFFERINGS 800-860-1010

Rating Moody/S&P	Description	Coupon	Maturity	Yield to Maturity	Approx Price	Tax Equivalent Yield
AA2/AA+	**New York NY City Housing Dev** Callable 11/01/27 @ 100 Subject to Special Optional Redemption	2.300%	11/01/31	2.300%	100.000	4.03%
A1/A+	**Connecticut St General Oblig** Callable 10/15/26 @100	3.000%	10/15/32	2.250% YTC 2.570% YTM	104.511	3.95%
A3/A-	**New Jersey St GO General Obligation** Callable 06/01/27 @ 100	2.375%	06/01/36	2.500%	98.347	4.39%
AA3/A+	**New York State Dorm Authority State University** Callable 04/01/25 @ 100	3.000%	07/01/39	2.700% YTC 2.830% YTM	102.429	4.74%
AA1/AAA	**Boston MA Water & Swr Rev** Callable 11/01/23 @ 100	3.000%	11/01/41	2.250%YTC 2.840%YTM	102.540	3.95%
AA1/AA+	**New York State General Obligation** Callable 03/01/23 @ 100	3.500%	03/01/43	2.000% YTC 3.240%YTM	104.172	3.51%

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The bonds listed above are just a sample of the bonds we own or offer. Consult your investment representative to determine suitability. The tax-equivalent yield is calculated using the lower of yield to call and yield to maturity and a 37.00% federal tax rate plus an estimated 6.00% state tax rate (43.00% total) where applicable. You will only receive the quoted tax equivalent yield if you are in this tax bracket. Additional tax equivalent yields can be calculated upon request. All municipal bonds listed are exempt from federal taxes unless described as "subject to AMT" or listed as taxable and may be subject to state and local taxes. Discount bonds may be subject to capital gains taxes and/or ordinary income. All bonds are subject to price change and availability. All prices are as of 04/13/2020. If bonds are sold prior to maturity or call date, they may be worth more or less than their original investment. Official statements and material events information for some municipal bonds may be found on www.emma.msrb.org