CenterState
CORRESPONDENT DIVISION

Market Update

Economic News

June 5, 2020

The May Employment Report is out and if you like surprises this report is loaded with them. Instead of an expected loss of 7.75 million jobs, the report found 2.5 million jobs created versus 20.7 million jobs lost in April. The surprises don't stop there. The unemployment rate was expected to rise to 19.5% from 14.7%, but instead fell to 13.3%. Those numbers obviously have the Treasury market backpedaling further with the 10-year currently at 0.92%, off one point. That's quite the move after spending the last two months in a tight range between 0.54% and 0.78%. We talk more about the rate rise in the section below. Also, the BLS once again noted a fly in the ointment with obvious errors in survey responses, just like in March and April, such that the unemployment rate could be 3% higher than the official figure. As you might expect from the job gains, the Labor Force Participation rate moved higher from 60.2% to 60.8%, still a level last seen 47 years ago. We look at some more of the details in this surprising report below.

- For the month, 2.5 million jobs were added to payrolls (3.1 million private sector less 585 thousand cut in government jobs), which is quite a bit better than the expectation of 7.75 million job losses. While March and April saw huge losses in the leisure/hospitality field, some of those laid off returned as that sector led all gains with 1.2 million new jobs as the partial reopenings started to impact employment. The total for service sector job growth was 2.4 million. Another sector that was hard hit in March and April, the Retail sector in May saw 367 thousand jobs gained. Health care and social assistance had a good month as well with 391 thousand new jobs. The good job news didn't stop at the services sector as goods-producing jobs increased by 669 thousand with construction adding 464 thousand and manufacturing 225 thousand jobs.

- The unemployment rate fell from 14.7% to 13.3%, much better than the 19.5% expectation, but for the third month in a row, the BLS noted obvious errors in survey responses, that if adjusted would have added up to 3% to the official rate. The issue revolves around the response to being out of work as either a "temporary layoff" which counts as unemployed or "employed but absent from work." They noted a huge increase in the latter response, just like in March and April, which resulted in the undercount of unemployed, per the BLS. There was also a lower response rate (67% vs. an average 82%) which makes the numbers a bit less reliable. The Household Survey—which is used to generate the various employment ratios— reported that 2.1 million persons left the unemployment rolls (20.1 million versus 23.0 million) while 1.7 million persons joined the labor force (158.2 million vs. 156.5 million). So both the gain in the labor force (denominator) and the drop in unemployed (numerator) worked to lower the unemployment rate in May. The underemployment rate (unemployed plus part-time workers wanting a full-time job and those wanting a job but not currently looking) fell from 22.8% to 21.2%.

- With the better-than-expected job growth, average hourly earnings in May took a hit as the lower paying sectors (hospitality, leisure, retail) were the biggest gainers. Average hourly earnings fell by -1.0%, missing the +1.0% growth forecast. Year-over-year earnings rose 6.7% versus 8.0% in April. Like the last two months, the YoY increase is more a function of lower-wage workers getting hit with the initial wave of layoffs, while higher-wage employees survived the early cuts. That will be another reason for the Fed to remain ultra-accommodative (read near zero fed funds rate) well into next year.

Have You Considered Pre-Investing Your PPP Loan Forgiveness Funds?

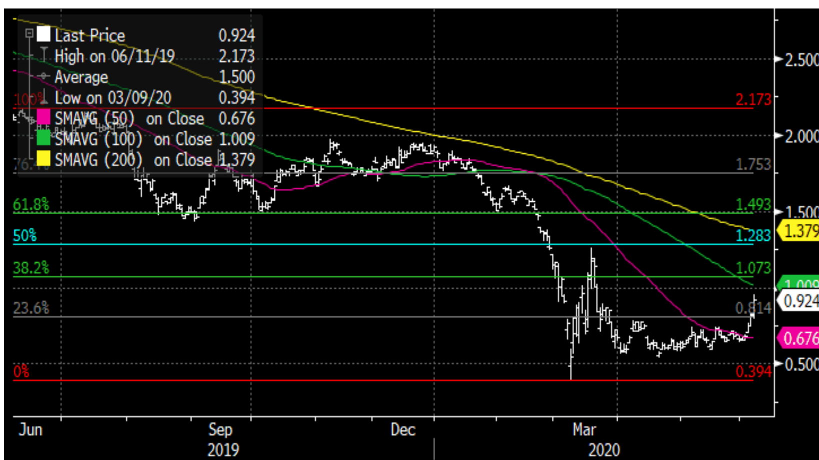
With the rollout of the second tranche of the SBA Paycheck Protection Program, many bankers are experiencing bloated balance sheets as loan proceeds (both originated in-house and elsewhere) slosh around in demand deposit accounts. Stimulus checks are creating a similar situation as the physical check aspect of the one-time payments make there way into deposit accounts. Those bloated cash balances represent a tempting target for reinvestment but that liquidity is very likely to disappear.

Certainly the stimulus checks, both direct deposit and otherwise, are likely to dribble away over the coming weeks and months as customers draw on the funds to cover living expenses and/or pay down debt. Given the employment numbers covered earlier, expect very little to remain as a long-term source of investment. The PPP loan funds are a more interesting situation. While those cash balances should be expected to diminish as businesses draw on the funds to make payroll and other covered operating expenses, the ultimate forgiveness of those loans does provide an interesting opportunity for reinvestment.

Once eight weeks elapses after loan funding the business should apply for loan forgiveness (SBA Form 3508) through the bank that made the loan. The lender then has 60 days to issue a decision to the SBA. Within 90 days after the lender issues its decision to the SBA, the SBA will, subject to any SBA review of the loan or loan application, remit the appropriate forgiveness amount to the lender, plus any interest accrued through the date of payment. Assuming a lender makes quick work of their review, the bank could receive the forgiveness funds within six months of initial loan funding. That puts those forgiveness funds arriving as soon as October given the early April rollout of the program. It's those funds that offer a real long-term reinvestment opportunity. What's more, rather than wait for those funds to arrive, a banker has the opportunity to fund an investment today with short-term FHLB borrowings that can be repaid once forgiveness funds are received. For each $1mm invested and earning a net 1%, or better, will provide $4,500 in additional earnings by October versus earning almost nothing at the Fed.

If you're interested in exploring this low-risk opportunity to enhance earnings for this year, please contact your CenterState representative.

10-Year Treasury Yield Breaks 2-Month Range



After spending more than two months stuck in a range between 0.54% and 0.78% the 10-Year Treasury finally broke decisively above the range reaching 0.91% this morning. The yield move has been mostly methodical which lends credence that there might be more to come. The increase comes as equities have staged a rally since the March 23 low. While the 30-year bond yield has climbed from 1.20% in mid-April to 1.72%, the 10-year had been much more reluctant to join the higher rate parade. While the range break is notable, there remains plenty of support levels just above as noted in the graph. Moving average and Fibonacci levels represent significant support so further yield increases should be grudging.

Market Rates

Treasury Curve	Today	Chg Last wk.	LIBOR Rates	Today	Chg Last wk.	FF/Prime	Rate	Swap Rates	Rate
3 Month	0.15%	+0.01%	1 Mo LIBOR	0.17%	-0.01%	FF Target Rate	0.00%-0.25%	3 Year	0.339%
6 Month	0.17%	+0.02%	3 Mo LIBOR	0.33%	-0.01%	Prime Rate	3.25%	5 Year	0.504%
2 Year	0.21%	+0.05%	6 Mo LIBOR	0.48%	-0.03%	IOER	0.10%	10 Year	0.897%
10 Year	0.90%	+0.25%	12 Mo LIBOR	0.62%	-0.05%	SOFR	0.07%		

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