CPIC Market Update

September 18, 2020

Economic and Financial Markets

- Total nonfarm payroll employment rose by 1.4 million in August, and the unemployment rate fell to 8.4%. These improvements in the labor market reflect the continued resumption of economic activity that had been curtailed due to the COVID-19 pandemic and efforts to contain it
    - In August, the unemployment rate declined by 1.8% to 8.4%, and the number of unemployed persons fell by 2.8 million to 13.6 million. Both measures have declined for four consecutive months but are still significantly higher than in February, by 4.9% and 7.8 million, respectively. We also expect this trend to continue.
- The labor force participation rate increased by 0.3% to 61.7% in August but is 1.7% below its February level and total employment rose by 3.8 million in August to 147.3 million but is 11.4 million below February 2020
- In the United States, multiple federal stimulus packages in the total amount of approximately $3 trillion have passed in an attempt to shore up financial markets and mitigate the impacts on businesses and individuals and we still expect more to come potentially in the additional amount of $1-1.5 trillion (may be after November).
- The U.S. Federal Reserve reduced its Fed Funds target from 1.50%-1.75% to 0.00%-0.25% in two March 2020 cuts – the first on March 3rd was 0.50% to a range of 1.00%-1.25% and the second on March 15th was 1.00% to a range of 0.00%-0.25%
- In addition, the Fed is also in full Quantitative Easing mode and its current balance sheet is at $7.0 trillion as compared to $4.2 trillion on December 31, 2019
- Before the contraction due to COVID, U.S. GDP had grown nearly unimpeded since the Great Recession of 2007-2009. During the record expansion, the unemployment rate fell to a 50-year low of 3.5%, and the U.S. economy added jobs for 113 months in a row
- Real GDP decreased at an annual rate of 31.7% in the second quarter of 2020. In the first quarter, real GDP decreased 5.0%. Current-dollar GDP at the end of the second quarter was $19.49 trillion as compared to $21.43 trillion at the end

of 2019 or a net decrease of approximately $2 trillion in the first 6 months of 2020.

- Third quarter real GDP will be released on October 29th and is expected to increase by approximately 30%-32% , however, compared to the end of 2019, by the fourth quarter of 2020 real GDP is projected to be 4%-5% lower and 1.5%-2% by the end of 2021

Equity Market

- The equity market took a significant downturn as a result of COVID in the spring but has recovered and both the S&P500 and DJIA are effectively unchanged for the year – however – this primarily reflects Fed's intervention, low interest rates, and expectation of economy starting to recover in the first half of 2021

Interest Rates

- Fixed income markets have seen interest rates crater to historical low levels with the 30-year Treasury rate closing at 0.99% on March 9th and the 10-year Treasury rate went as low as 0.54% on March 9th – current 5 and 10 year treasury rates are 28 and 69 basis points respectively
- Currently, the 1-10 year yield curve is between 67% and 91% below its 5-year averages and 69% and 84% lower than its 10-year averages

U.S. Treasury Rates								
	1-Year	2-Year	5-Year	7-Year	10-Year	3Mo-5Yr Spread	6Mo-10Yr Spread	2-10 Yr Spread
Current (9/17)	**0.12**	**0.13**	**0.28**	**0.47**	**0.69**	**0.19**	**0.58**	**0.56**
1-Yr Prior	1.88	1.74	1.66	1.73	1.79	(0.27)	(0.13)	0.05
2-Yrs Prior	2.58	2.81	2.96	3.03	3.07	0.79	0.70	0.26
5-Yrs Prior	0.32	0.67	1.44	1.84	2.13	1.43	2.04	1.46
5-Yr Average	1.33	1.46	1.76	1.96	2.10	0.62	0.85	0.64
10-Yr Average	0.75	0.94	1.54	1.90	2.23	0.94	1.55	1.29
Current as % Above / Below 5-Yr Average	-91%	-91%	-84%	-76%	-67%	-69%	-32%	-12%
Current as % Above / Below 10-Yr Average	-84%	-86%	-82%	-75%	-69%	-80%	-63%	-57%

Fixed Income Market

- As compared to year-to-date 2018 and 2019, year-to-date 2020 corporate issuance is 55% and 79% higher, respectively, with $1.5 trillion of issuance while year-to-date 2020 municipal issuance is higher by 10% and 24%, respectively, with $252 billion of issuance as issuers are taking advantage of historically low interest rates and building up liquidity to meet the potential cash flow needs.

	Corporate Issuance		Municipal Issuance			
Year	Par ($B)	% Change from Prior Yr	Tax-Exempt ($B)	Taxable ($B)	Par ($B)	% Change from Prior Yr
2011	$1,044	-4%	$264	$31	$295	-32%
2012	$1,389	33%	$351	$32	$383	30%
2013	$1,413	2%	$300	$35	$335	-12%
2014	$1,472	4%	$316	$23	$339	1%
2015	$1,511	3%	$377	$28	$399	18%
2016	$1,542	2%	$423	$29	$446	12%
2017	$1,669	8%	$415	$34	$439	-2%
2018	$1,372	-18%	$321	$25	$346	-21%
2019	$1,415	3%	$359	$67	$426	23%
2019YTD	$853		$180	$24	$204	
2020YTD	$1,526	79%	$170	$81	$252	24%

Source: SIFMA

Risk Transfer Market

- Reinsurance pricing conditions softened from 2015 through 2017, but the insurance industry has incurred approximately $19 billion of losses from Hurricanes Irma and Michael and is projected to ultimately incur approximately $21 billion in losses. Globally there were over $275 billion of insured losses from 2017 and 2019

- Global reinsurance industry is impacted by negative market forces largely driven by the COVID-19 pandemic, social inflation and previous years' catastrophe events that are being offset by positive forces of hardening rates and a re-assessment of third-party capital investor appetite as well as alternative investment opportunities

    - The impacts of COVID-19 and social inflation combined with an overcapitalized sector have translated into "companies struggling to meet their cost of capital" according to A.M. Best

- Despite the COVID-19 pandemic, the catastrophe bond segment of the insurance-linked securities industry rebounded during the second quarter of 2020 with over $10 billion issued year-to-date and $42 billion currently outstanding

- In the first half of 2020, global economic losses from natural catastrophes and man-made disasters totaled $75 billion and global insured property losses from disasters were $31 billion – these numbers exclude COVID-19
- There have already been approximately $20-$25 billion of pandemic-related claims on insurers' books, and industry estimates put the ultimate total at roughly $40-$50 billion
- Capital raising in the insurance sector has been opportunistic in the current low interest rate environment with $16 billion of new capital raised in the first half of 2020
- Early estimates of increases in loss ratios for the full year 2020 fluctuate from 5% on the low end to more than 20%