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# The Pandemic of 2020-2021: A Stress Test for the United States Economy

Presentation by Jim Millstein\*

Co-Chairman, Guggenheim Securities

Presentation to the American College of Bankruptcy

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\*Prepared with the assistance of Josh Mendelsohn of Guggenheim Securities

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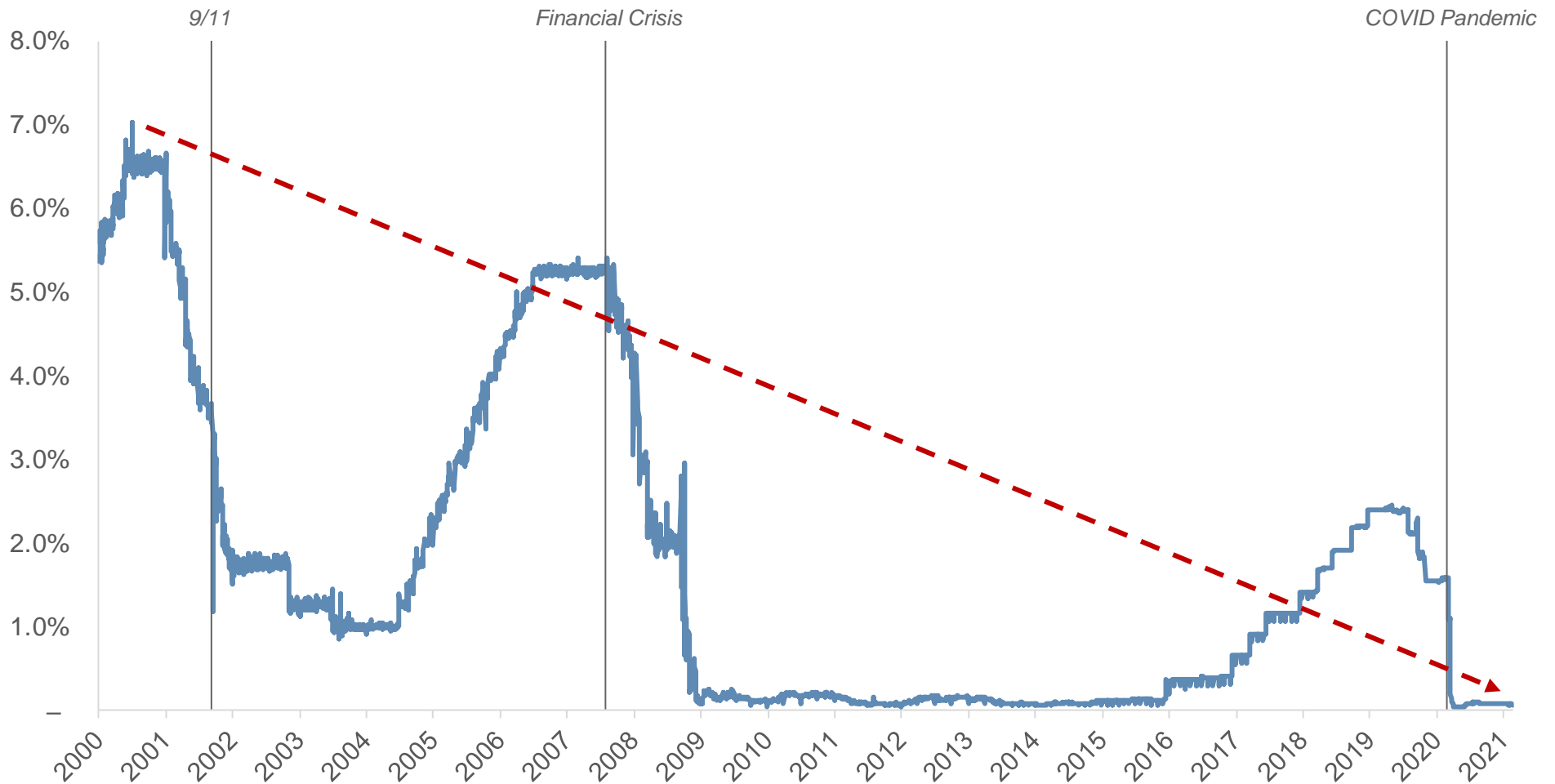
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# Evolution of the Fed Funds Rate – A Long Slide Down to the Zero Bound

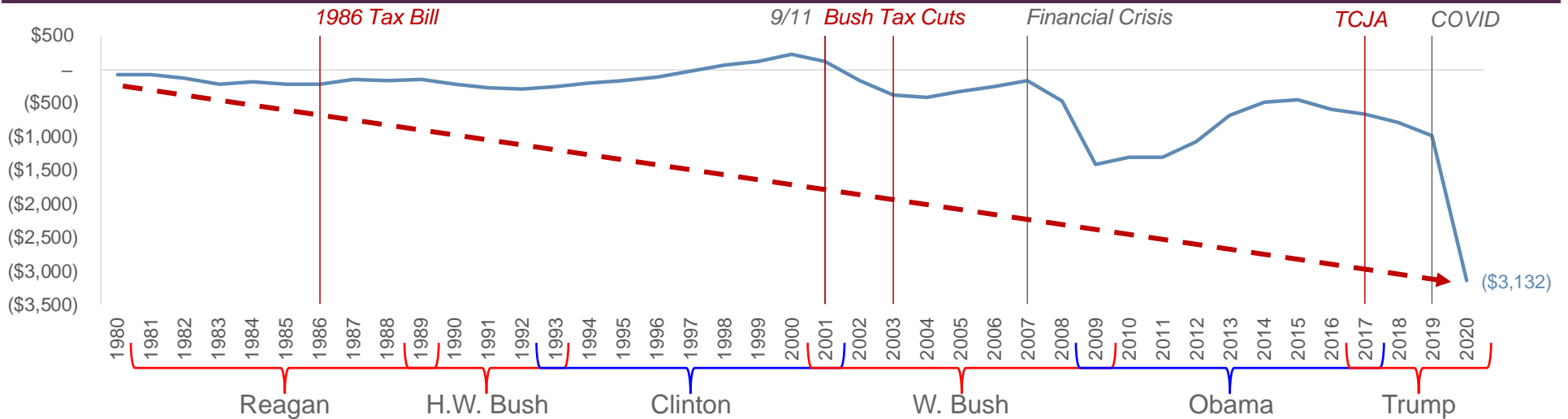
Effective Federal Funds Rate



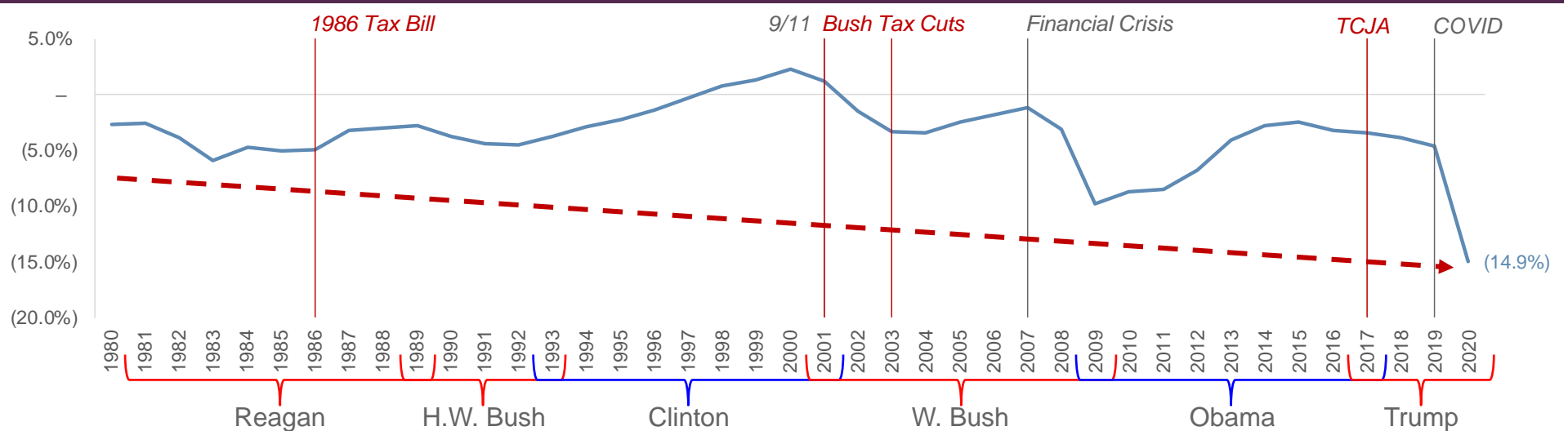
Source: Bloomberg.

# Running Historic Government Deficits During an Economic Expansion

Federal Deficit (\$B)

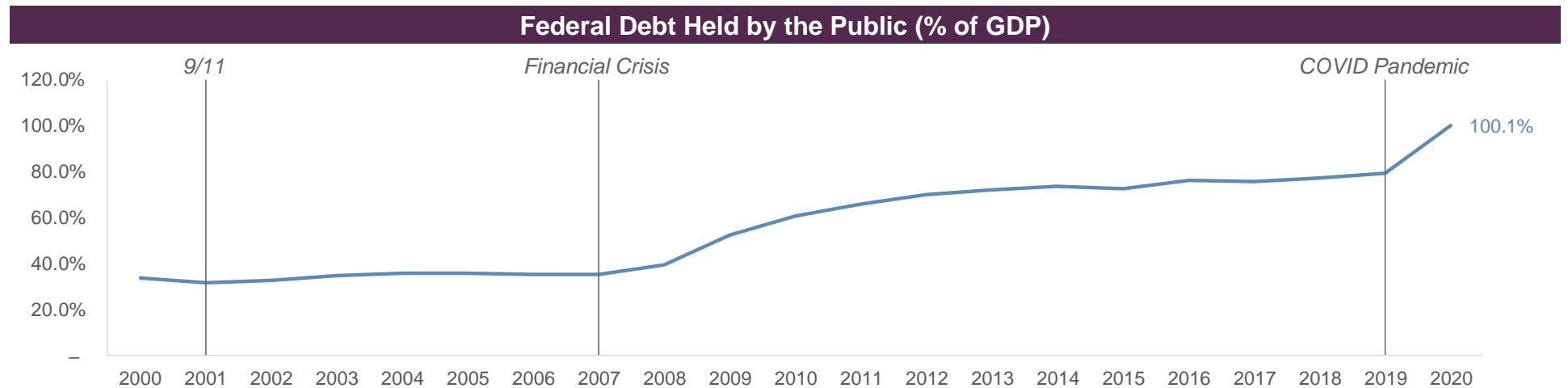
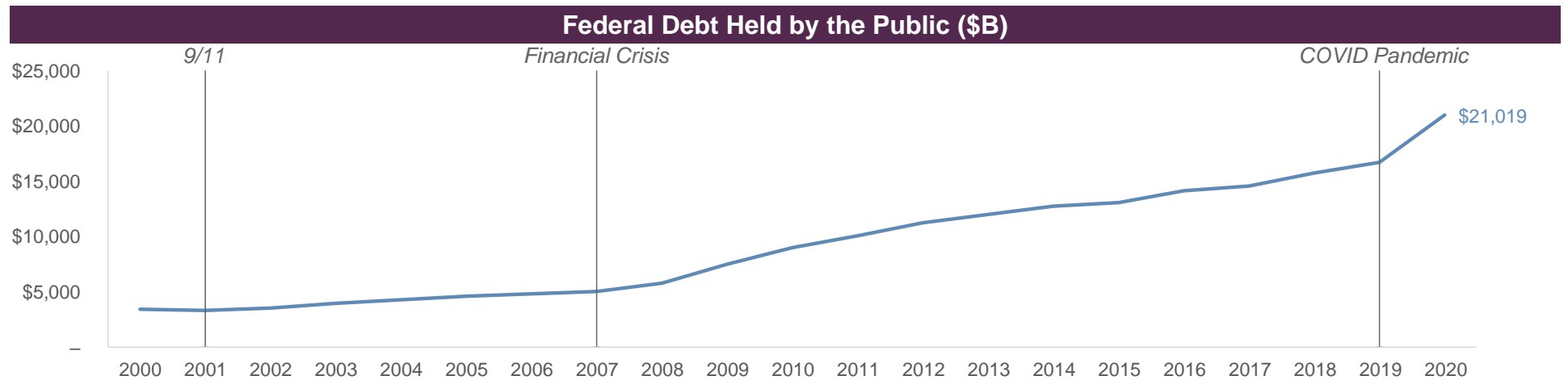


Federal Deficit (% of GDP)



Source: Congressional Budget Office.

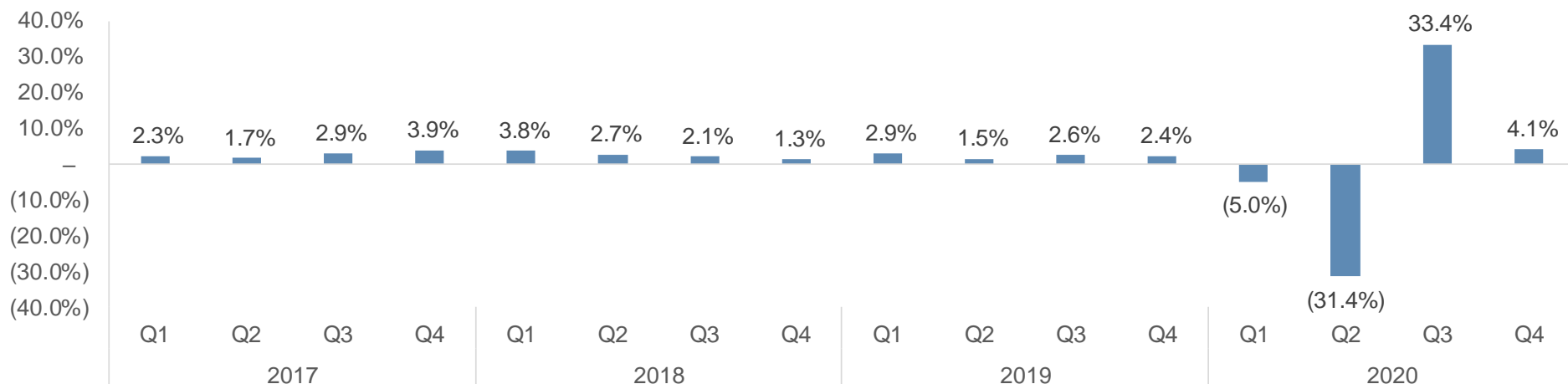
# And Growing Public Debt Faster than the Economy Was Growing



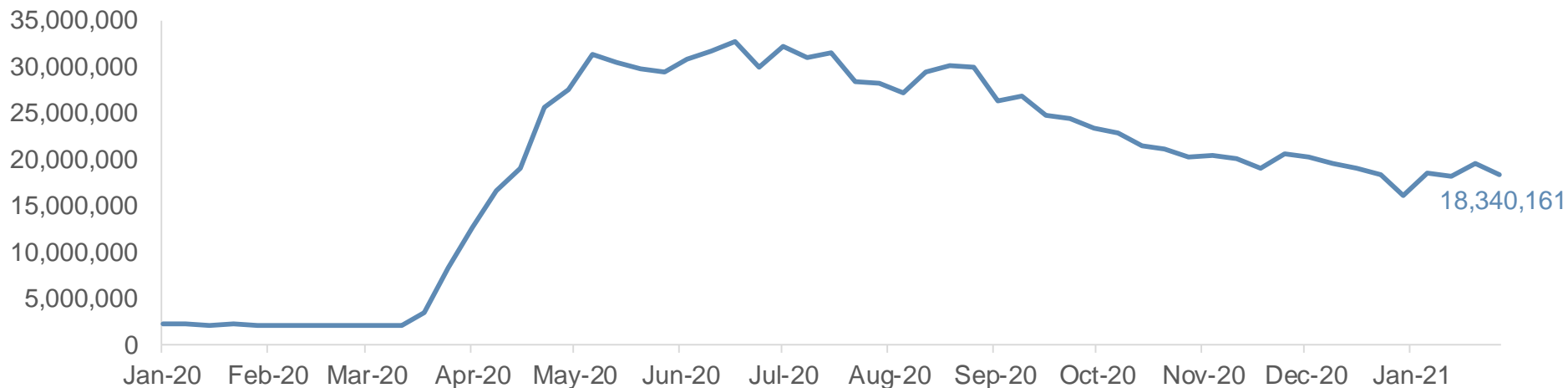
Source: Congressional Budget Office.

# Then the Pandemic Struck in Q1 2020 and the Staggered State Shutdowns and Persistent Infection Rates Significantly and Adversely Affected GDP and Employment

**Real Gross Domestic Product (% Change from Preceding Period, Seasonally Adjusted at Annual Rates)**



**Total Number of People Claiming Benefits in All Programs<sup>(1)</sup>**



Source: BEA, United States Department of Labor.

(1) Includes regular state, federal employee, newly discharged veteran, pandemic unemployment assistance, pandemic emergency UC, extended benefits, state additional benefits, and STC / Workshare unemployment programs.

# The Federal Government's Response to Date

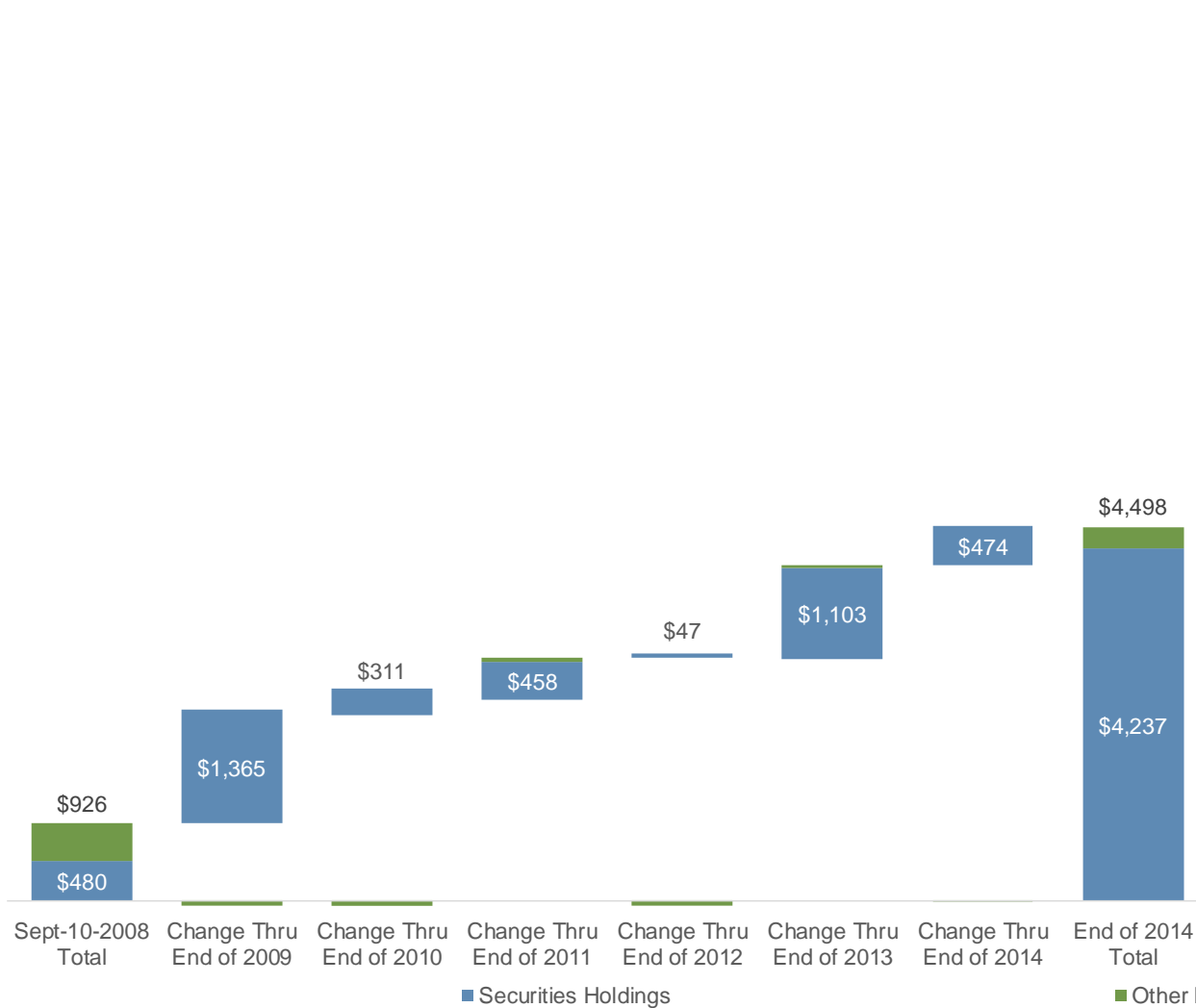
<b>U.S. COVID-19 Response</b>			
	<b>Allocated Amount</b>	<b>Committed / Disbursed</b>	<b>Deficit Impact</b>
<b>Federal Reserve</b>	<b>\$5.81 trillion</b>	<b>\$2.76 trillion</b>	<b>N/A</b>
<b>Administrative</b>	<b>\$663 billion</b>	<b>\$482 billion</b>	<b>\$93.9 billion</b>
<b>Legislative</b>	<b>\$5.94 trillion</b>	<b>\$3.03 trillion</b>	<b>\$5.26 trillion</b>
+ Loan Programs	\$1.61 trillion	\$992 billion	\$1.21 trillion
+ <i>Payroll Protection Program</i>	<i>\$828 billion</i>	<i>\$669 billion</i>	<i>\$805 billion</i>
+ <i>Economic Injury Disaster Loans</i>	<i>\$475 billion</i>	<i>\$200 billion</i>	<i>\$50 billion</i>
+ <i>Airline Industry Support</i>	<i>\$94.5 billion</i>	<i>\$60.7 billion</i>	<i>\$65.4 billion</i>
+ <i>Other</i>	<i>\$209.5 billion</i>	<i>\$62.3 billion</i>	<i>\$293.3 billion</i>
+ Income Support	\$944 billion	\$539 billion	\$915 billion
+ <i>Unemployment Benefits</i>	<i>\$828 billion</i>	<i>\$459 billion</i>	<i>\$820 billion</i>
+ <i>Other</i>	<i>\$116 billion</i>	<i>\$80 billion</i>	<i>\$95 billion</i>
+ Health Spending	\$617 billion	\$277 billion	\$607 billion
+ Direct Payments	\$860 billion	\$412 billion	\$860 billion
+ Tax Policy	\$522 billion	\$333 billion	\$375 billion
+ State & Local Funding	\$880 billion	\$306 billion	\$880 billion
+ Other Spending	\$502 billion	\$175 billion	\$413 billion

Source: CRFB's COVID Money Tracker as of February 22, 2021, CBO's Estimated Budgetary Effects of the Amendment in the Nature of a Substitute to the American Rescue Plan Act of 2021. Note: Includes \$915 billion in COVID relief provisions in the Consolidated Appropriations Act, 2021 (Public Law 116-260). Also includes estimated breakdown of \$1.9 trillion American Rescue Plan Act of 2021 per CBO analysis as of March 4, 2021.

# The Federal Reserve Went Where No Fed Has Gone Before: Intervention in the Corporate Credit Markets, Disintermediating the Banks

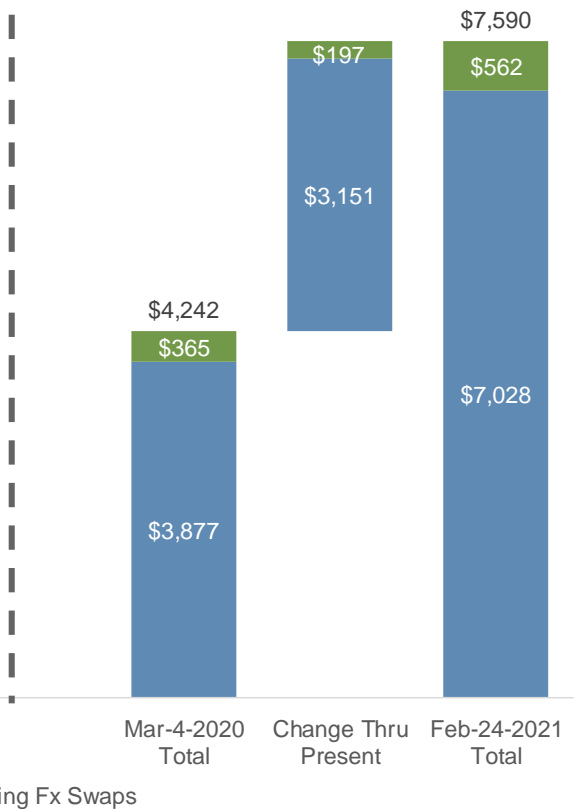
## Contributions to the Fed Balance Sheet (\$B)

### Global Financial Crisis and Aftermath



### Coronavirus Crisis

During 2020, the Fed established credit facilities to provide up to \$2.3 trillion of support to business and governments. Most programs expired on Dec 31, 2020 and only ~\$40 billion of such loans were outstanding as of Jan 31, 2021

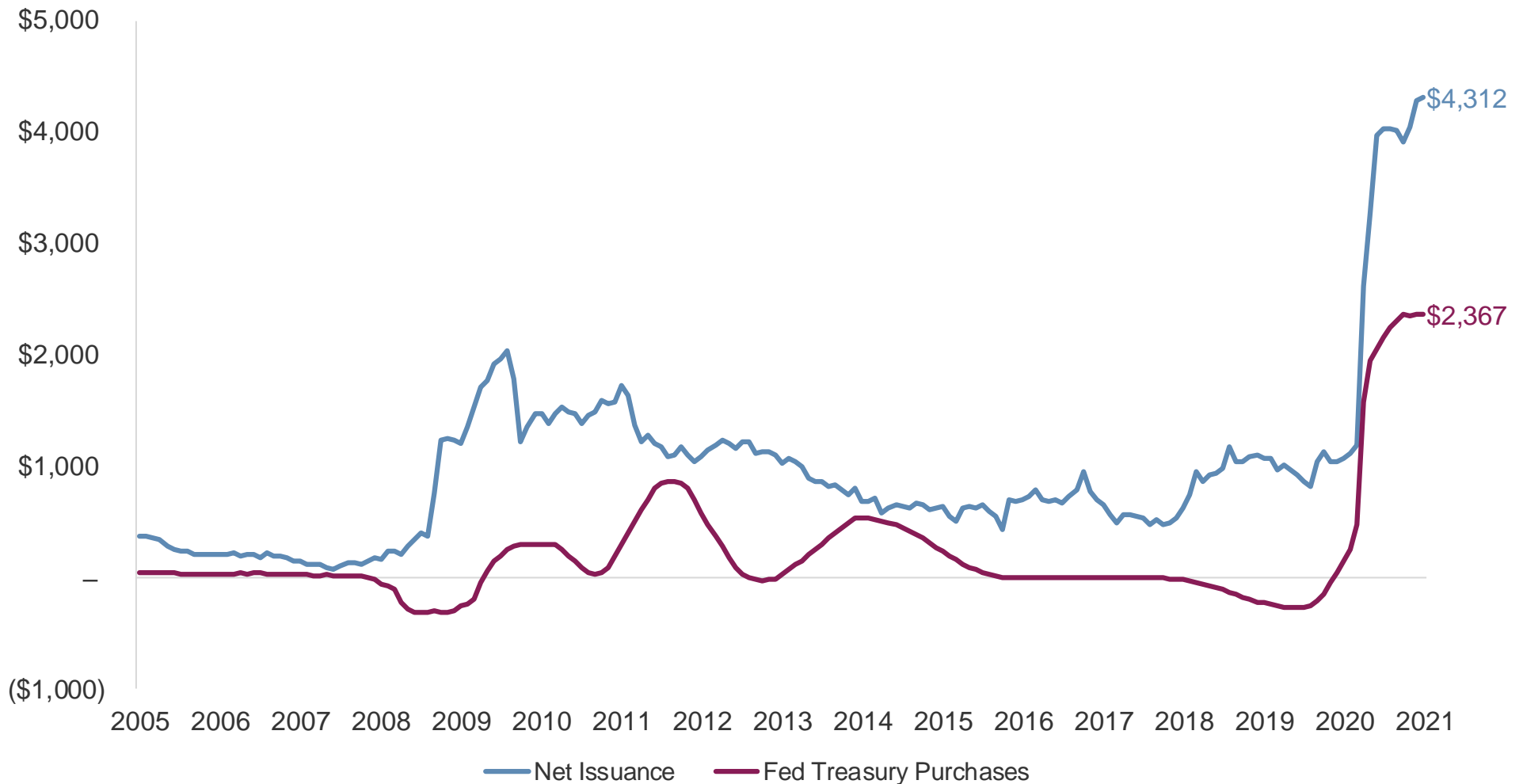


Source: Bao et. al., Johns Hopkins University, Center for Financial Stability.



# And Dramatically Increased the Pace of Its Bond Purchases in the Secondary Market to Keep Up with Treasury's Net Issuance so as to Hold Treasury's Borrowing Costs Down as the Federal Deficit Skyrockets

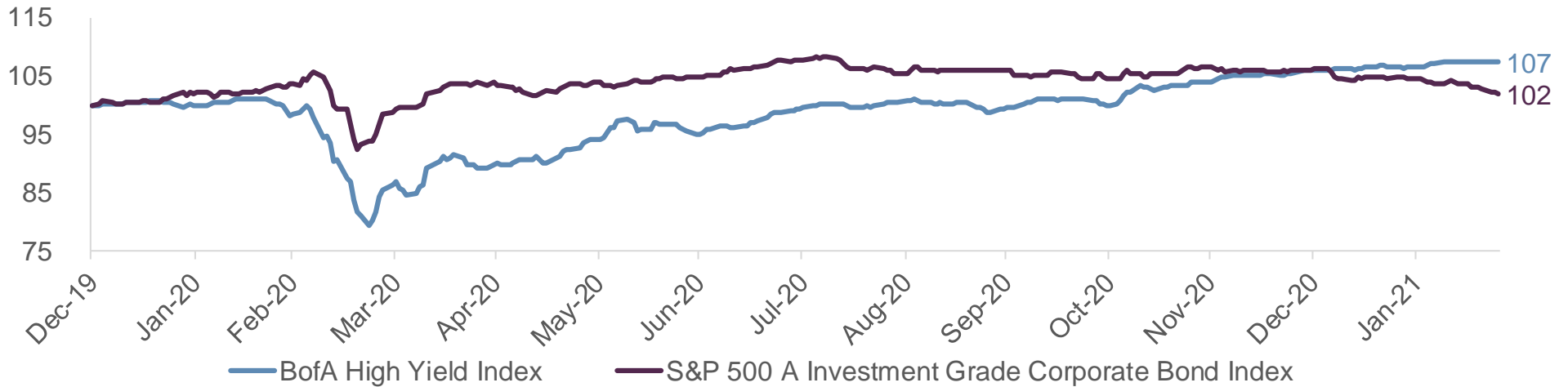
U.S. Government Bond Issuance and Central Bank Bond Buying (12-Month Rolling Sum, \$B)



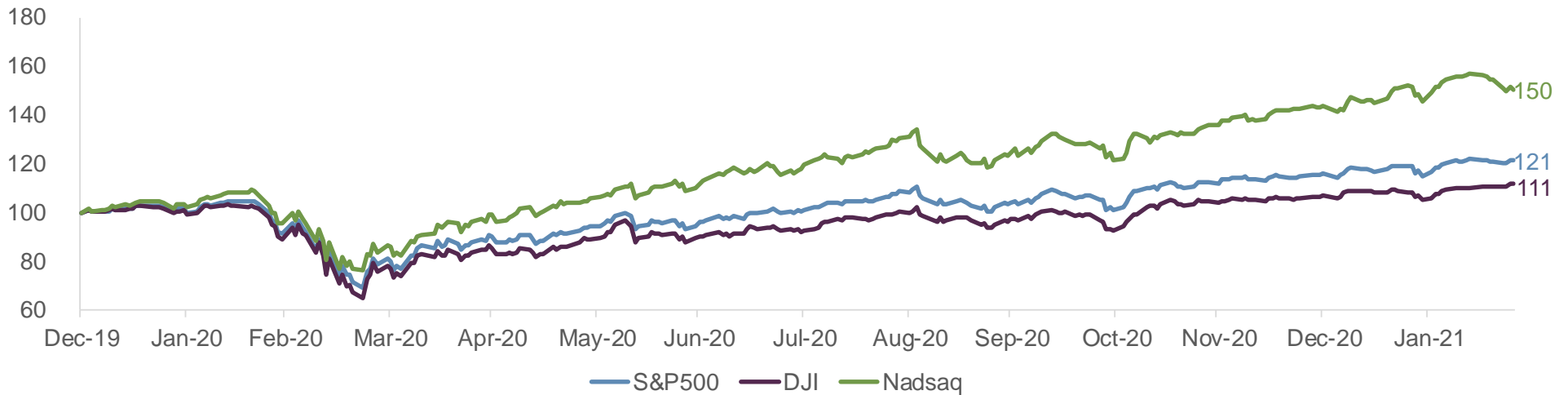
Source: Sifma, FRED.

# The Federal Government's Response to Date Has Rallied Corporate Credit and Equity Markets from March Lows

Credit Indices (Indexed Relative to 12/31/2019)

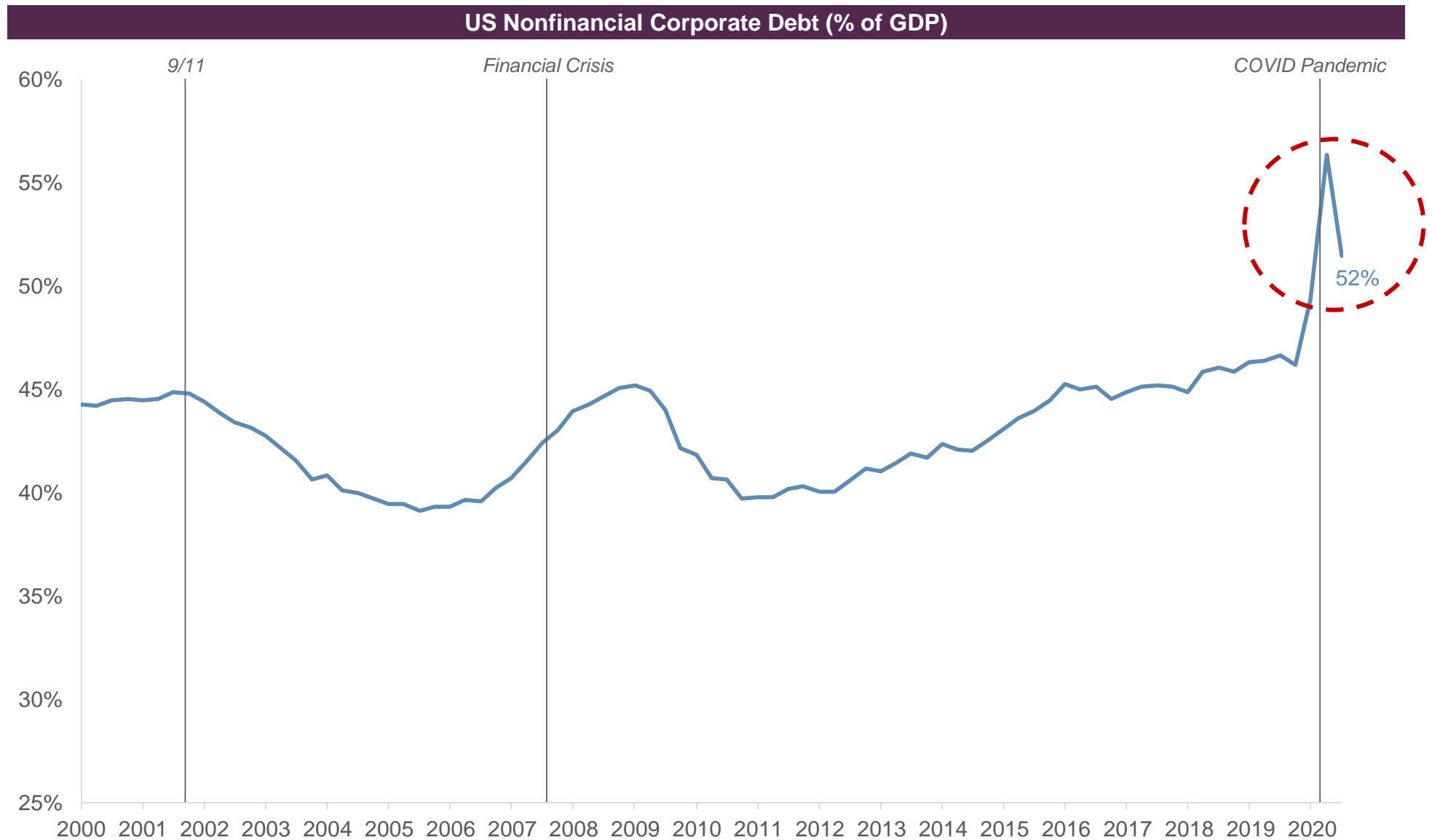


Equity Indices (Indexed Relative to 12/31/2019)



Source: Bloomberg.

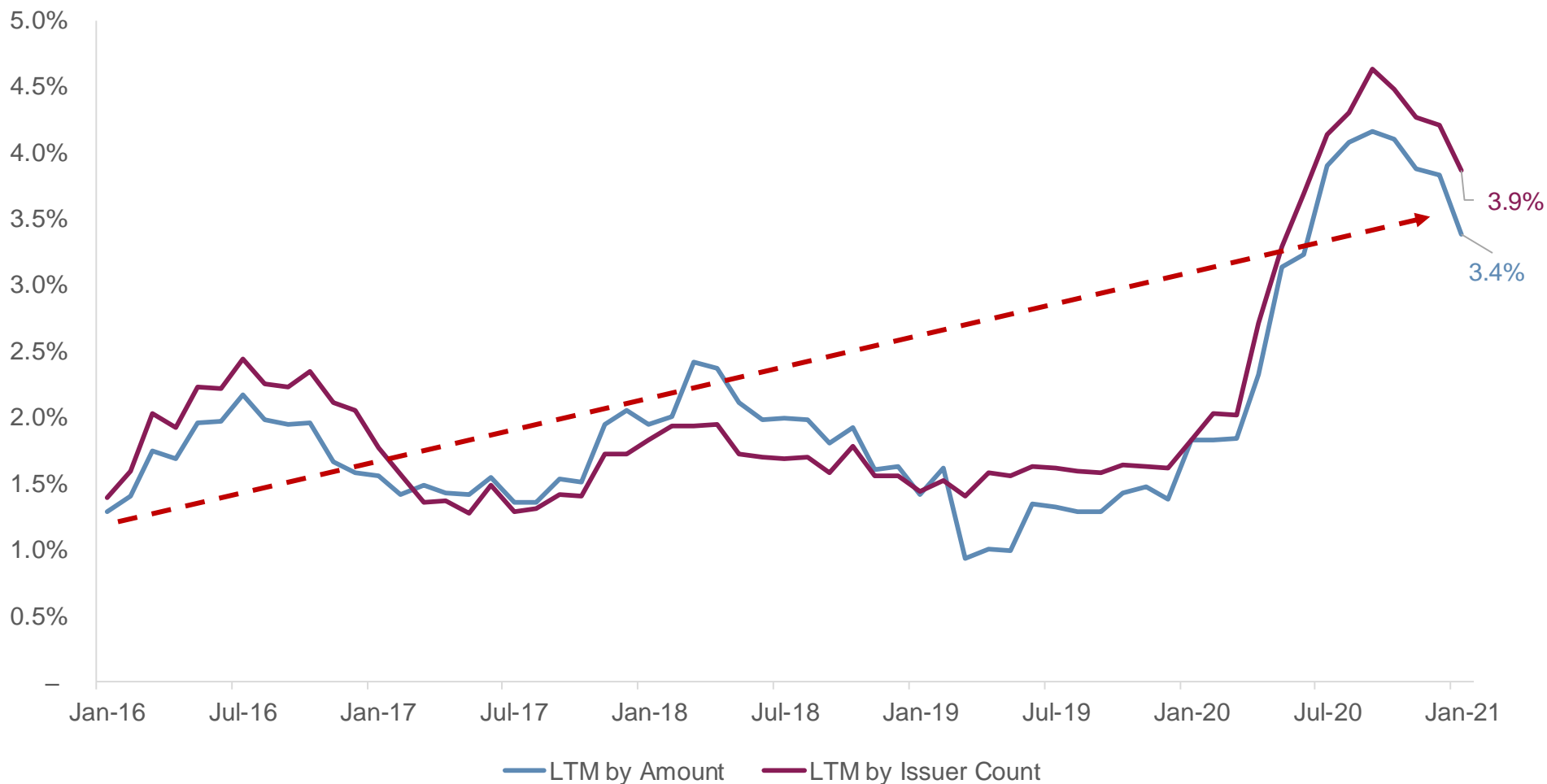
# Highest Corporate Debt to GDP in American History



Source: FRED.

# The Economic Dislocation and Demand Shock Created by the Failure to Get the Spread of the Virus Under Control Led to a Significant Increase in Leveraged Loan Default Rates

S&P/LSTA Leveraged Loan Index Default Rate<sup>(1)</sup>

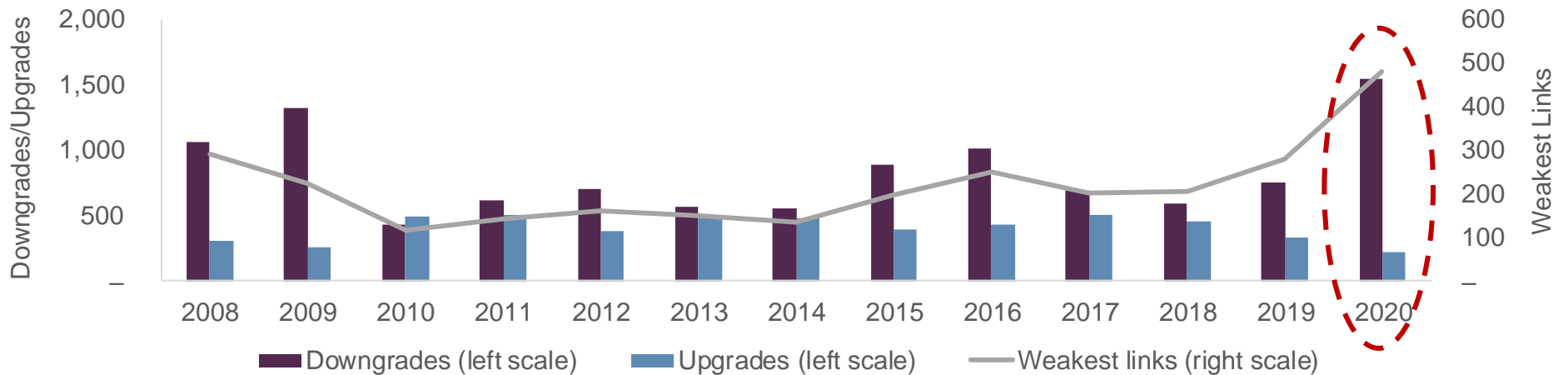


Source: LCD.

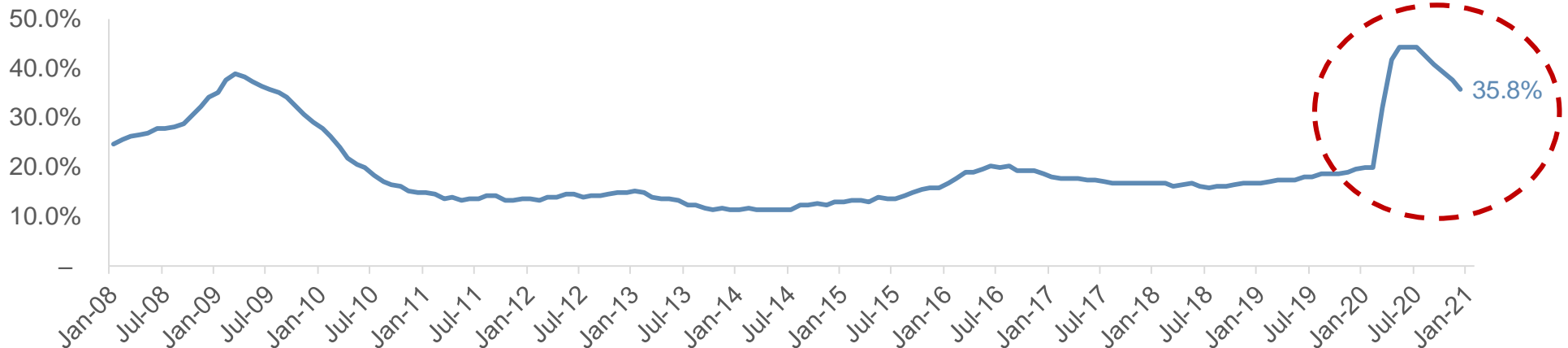
(1) Default defined as (1) company filing for bankruptcy, (2) facility gets downgraded to D by S&P (not due to below par buybacks), (3) interest payment is missed without a forbearance. LTM default rate by amount is equal to the sum of all defaulted amounts in the last 12 months divided by the total amount outstanding of performing loans 12 months ago. LTM default rate by issuer count is equal to the count of defaulted issuers in the last 12 months divided by total issuers not in default 12 months ago.

# The Risk of Future Defaults Is Still High Following the Largest Number of Downgrades Since the Financial Crisis

S&P Upgrades, Downgrades and Weakest Links<sup>(1)</sup>



S&P Negative Bias (% of Ratings with Negative Outlook or CreditWatch with Negative Implication)

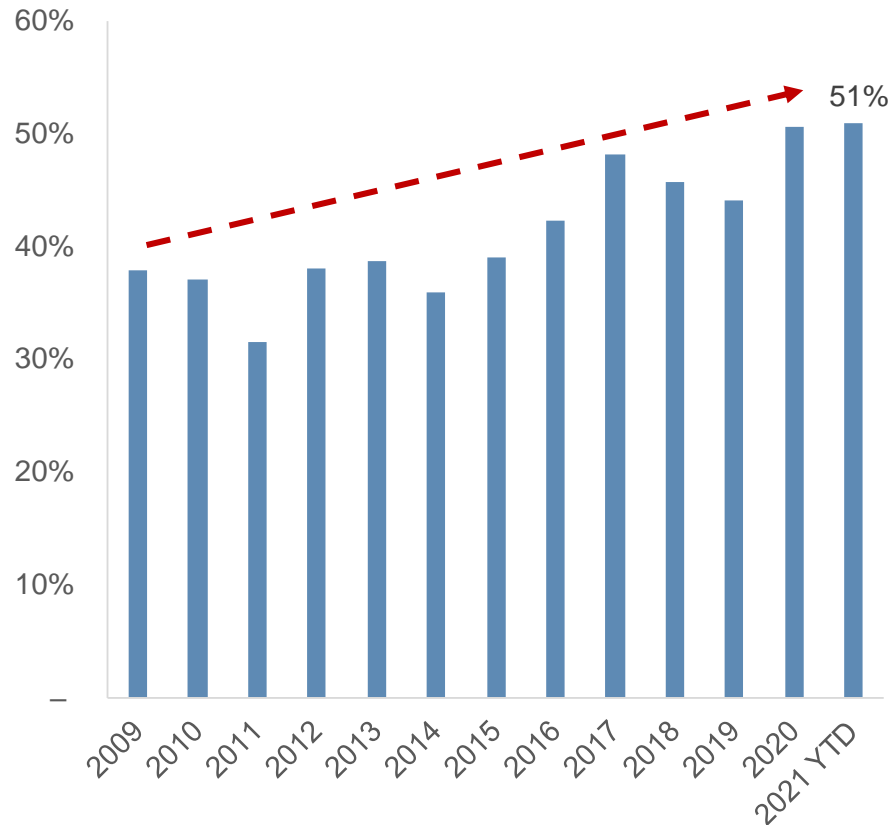


Source: S&P Global Ratings.

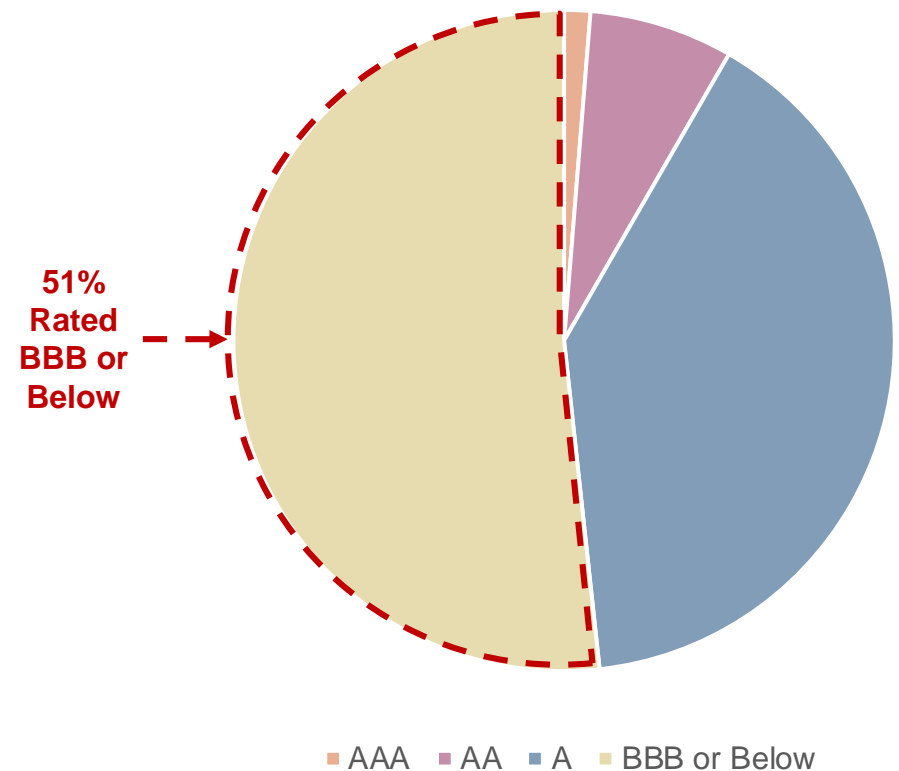
(1) Weakest Links defined as issuers rated 'B-' or lower by S&P Global Ratings with negative outlooks or ratings on CreditWatch with negative implications.

# More than 50% of Investment Grade Debt Issued and Outstanding Is Now at the Lowest Rung of the Credit Rating Scale

**% of Investment Grade Issuances Rated BBB or Below<sup>(1)</sup>**



**Composition of Investment Grade Debt Outstanding<sup>(2)</sup>**



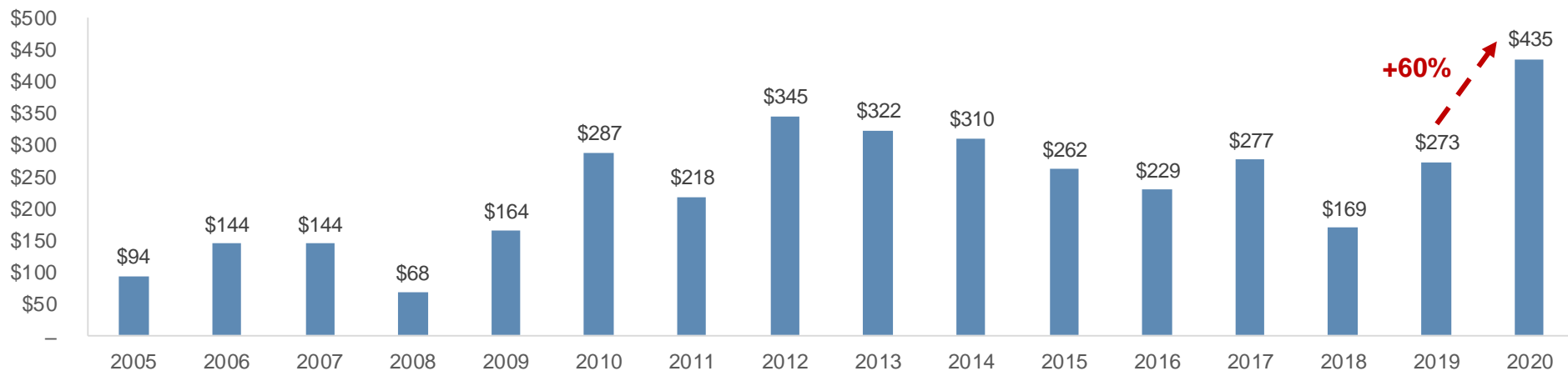
Source: LCD, Bloomberg, ICE BofA US Corporate Index.

(1) Per S&P LCD Comps.

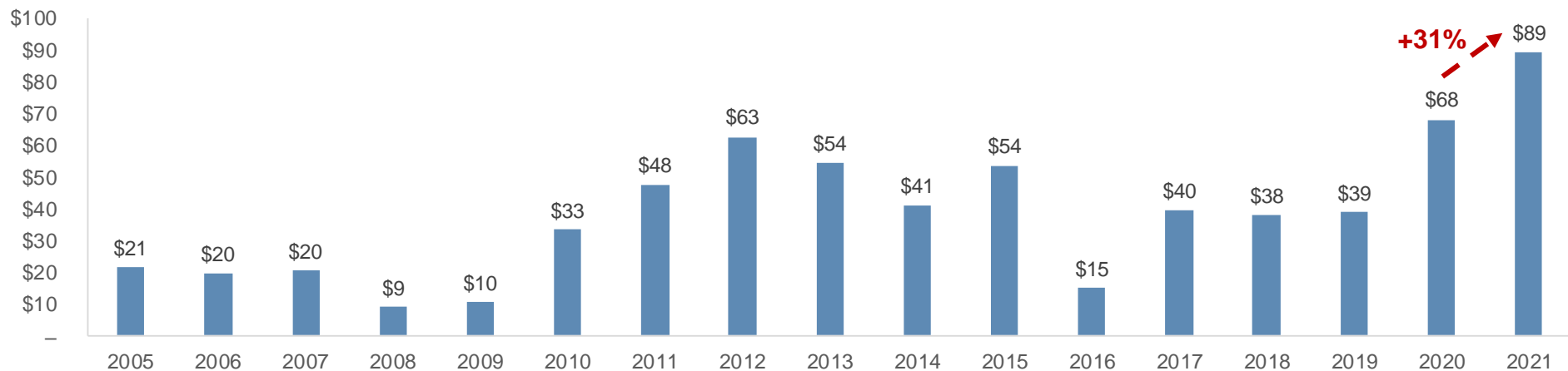
(2) Represents composition of ICE BofA US Corporate Index, which tracks the performance of US dollar denominated investment grade rated corporate debt publicly issued in the US domestic market. To qualify for inclusion in the index, securities must have an investment grade rating (based on an average of Moody's, S&P, and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P, and Fitch foreign currency long term sovereign debt ratings). Each security must have greater than 1 year of remaining maturity, a fixed coupon schedule, and a minimum amount outstanding of \$250 million.

# And Speculative Debt Issuances are Booming, as 2020 Saw Record High Yield Issuances and 2021 YTD Is Already 31% Above Last Year's Pace

High Yield Issuances (\$B)



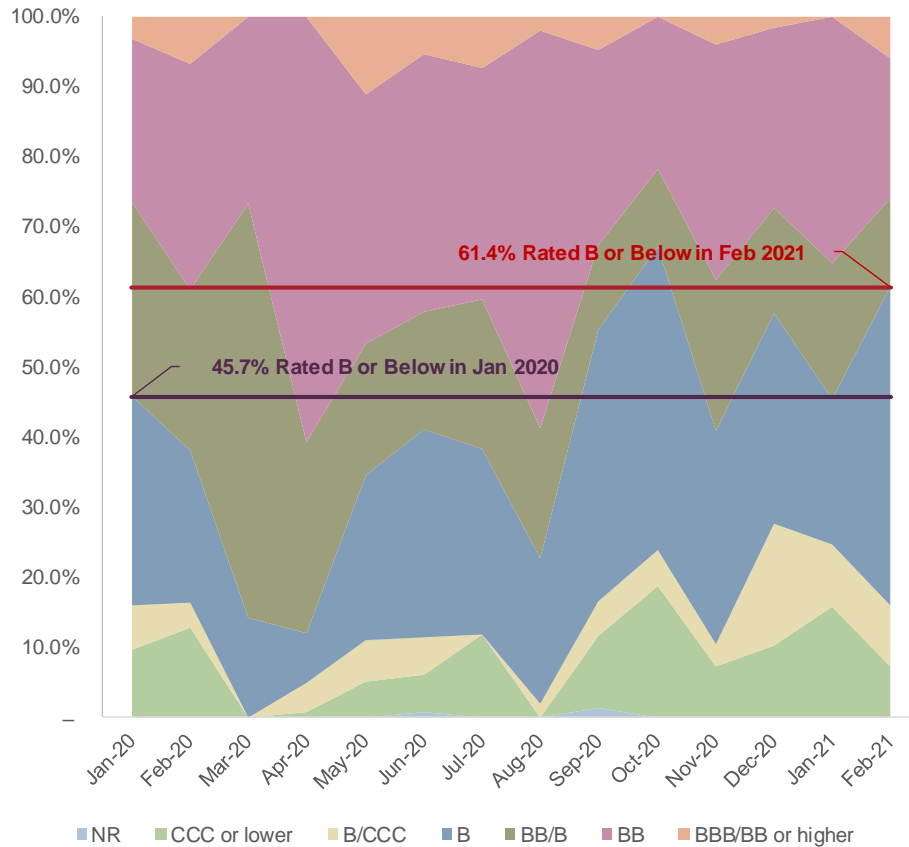
YTD High Yield Issuances Through End of February 2021 (\$B)



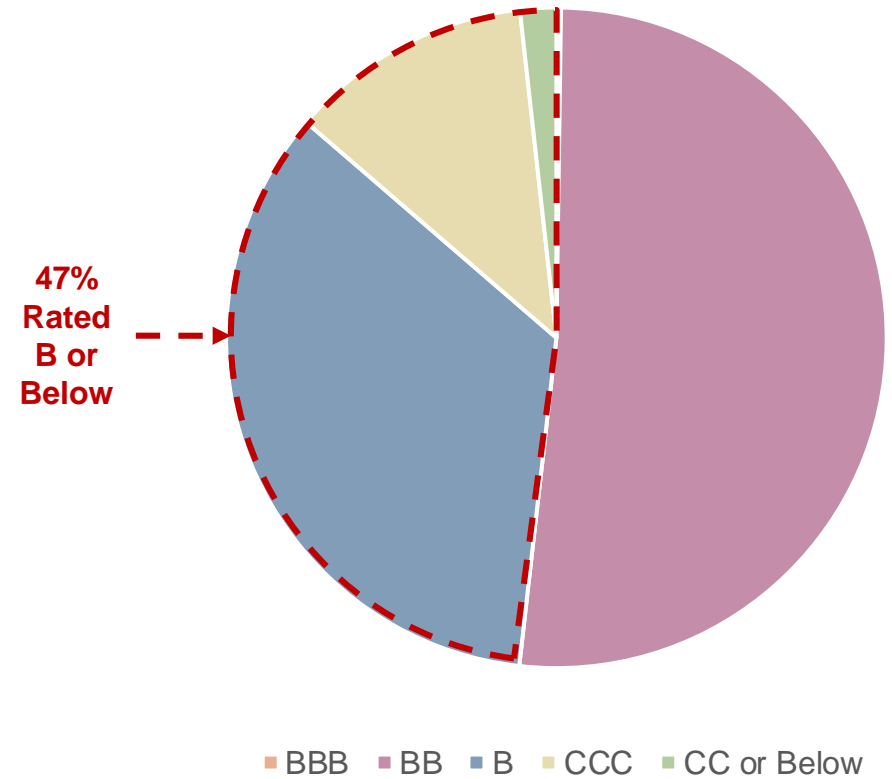
Source: S&P LCD Comps.

# Speculative Grade Issuances Appear to Be Deteriorating in Credit Quality

**Composition of High Yield Issuances (Jan '20-Feb '21)<sup>(1)</sup>**



**Composition of High Yield Debt Outstanding<sup>(2)</sup>**



Source: LCD, Bloomberg, ICE BofA US High Yield Index.

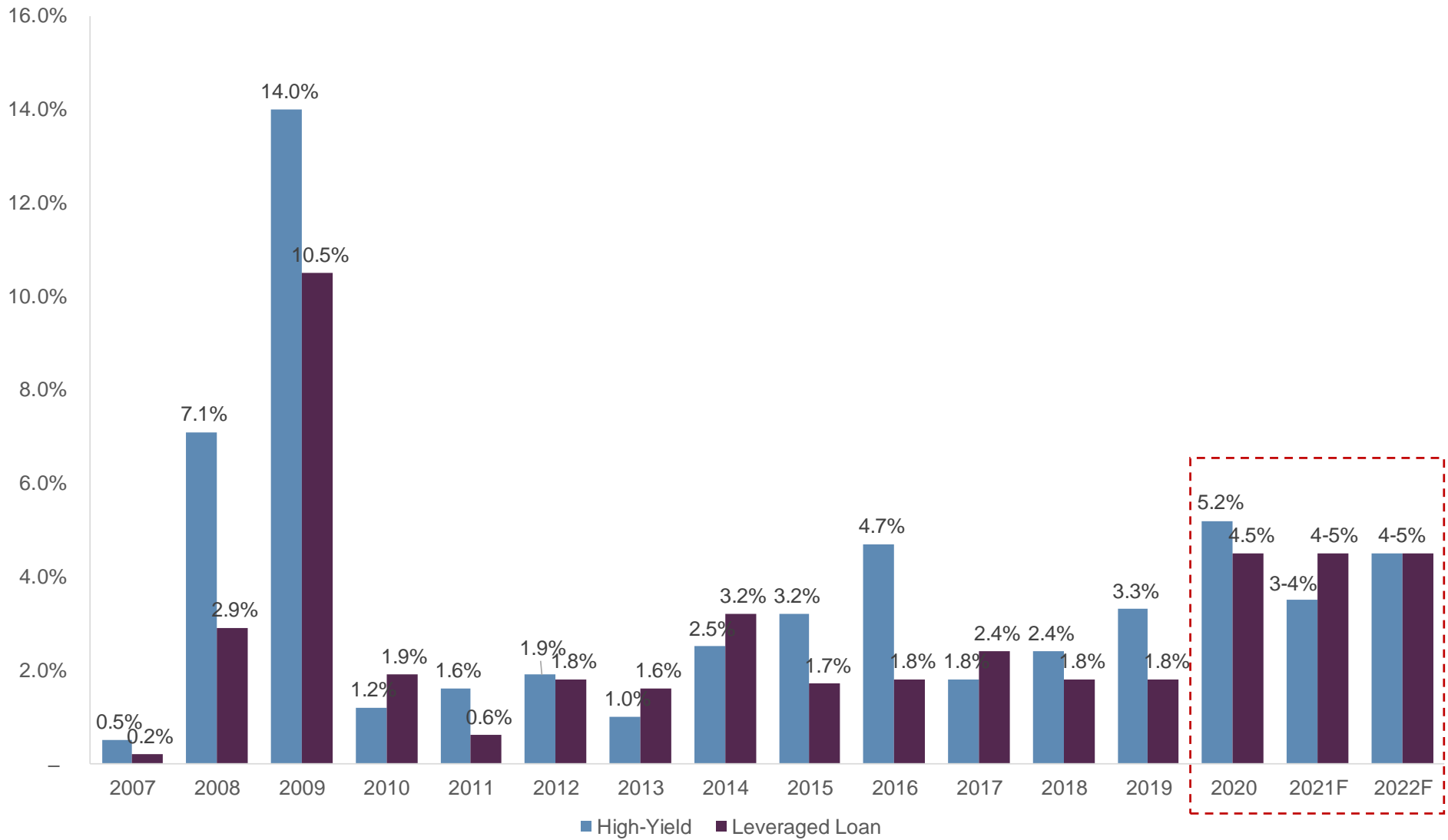
(1) Per S&P LCD Comps.

(2) Represents composition of ICE BofA US High Yield Index, which tracks the performance of US dollar denominated below investment grade rated corporate debt publicly issued in the US domestic market. To qualify for inclusion in the index, securities must have a below investment grade rating (based on an average of Moody's, S&P, and Fitch) and an investment grade rated country of risk (based on an average of Moody's, S&P, and Fitch foreign currency long term sovereign debt ratings). Each security must have greater than 1 year of remaining maturity, a fixed coupon schedule, and a minimum amount outstanding of \$100 million.



# While Default Rates Have Not Reached Financial Crisis Levels, the Sustained Elevated Forecast Combined With Record Speculative Debt Issuance Is Not Promising for the Health of US Corporate Sector

Fitch Default Forecast



Source: Fitch.