PALLAS CAPITAL ADVISORS

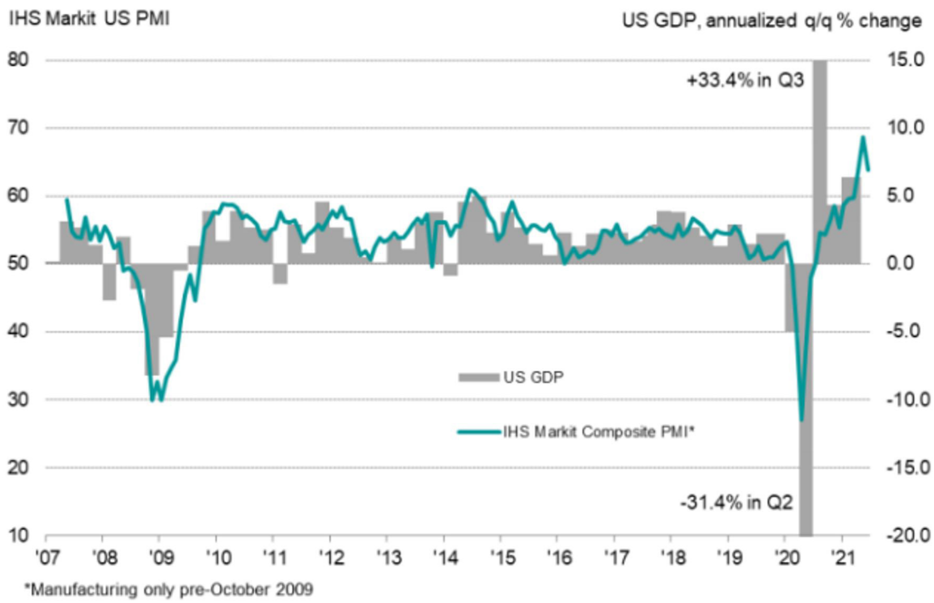
Week in Review

Friday, June 25th 2021

1. ECONOMIC ACTIVITY CONTINUES TO GROW AT RECORD HISTORICAL LEVELS BUT SLOWER THAN THE PAST TWO MONTHS

U.S. private sector businesses continued to register further marked expansion in activity during June, according to IHS Markit's survey of manufacturing and service companies. However, the survey also showed a reversion in the index, albeit still at record historical levels, from the highs reached in the previous 2-months. Moderations were seen in both the manufacturing and service sectors, with goods producers hampered in particular by significant supplier delays and both sectors reporting difficulties finding staff.

IHS Markit Composite PMI and U.S. GDP



Sources: IHS Markit, U.S. Bureau of Economic Analysis

New business growth was noted as continuing to be strong in June, concurrent with the relaxation of COVID-19 restrictions driven by both domestic demand and an upturn in export orders amid looser containment measures in key export markets.

Price pressures remained elevated in June, but it was noted that the rate of input inflation softened. Manufacturers noted ongoing increases in raw material and fuel costs, while service providers highlighted higher wages required to attract workers, and greater transportation and fuel costs. Labor constraints were a theme in the survey, touching on the difficulty to find suitably trained candidates for current vacancies.

Overall, while the absolute level of activity measured by HIS remains historically strong, the second quarter may represent the peak in growth.

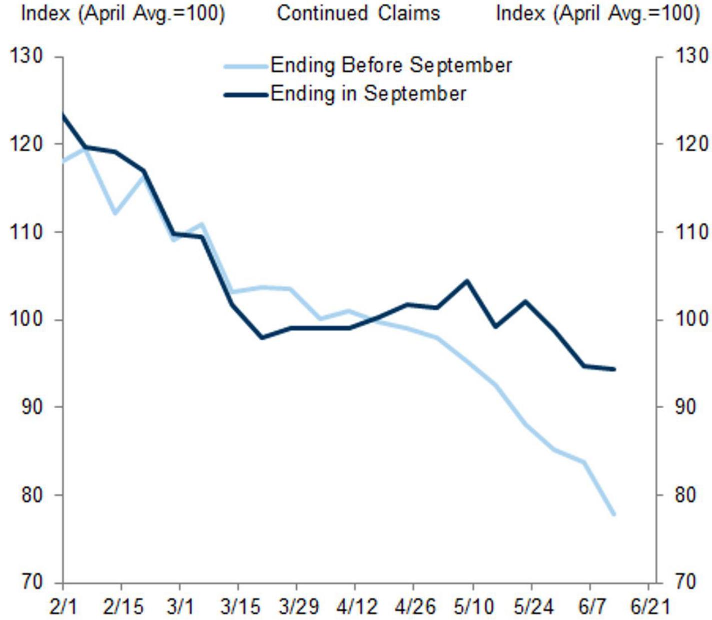
2. INITIAL CLAIMS FOR UNEMPLOYMENT LEVELING OUT FOR THE TIME BEING

Initial claims for unemployment came in at 411,000 this past week, above the expectation for 380,000, but slightly below the previous weekly level of 418,000. This level remains above the norm prior to the pandemic, which averaged around 200,000 to 250,000. This pre-pandemic level is being targeted by the Federal Reserve as a data point for assessing the full recovery of the economy.

Source: fred.stlouisfed.org

Nationwide continuing claims, the number of persons receiving benefits through standard programs, decreased by 144,000 to 3.390 million. However, the continuing claims number understates the number of workers receiving unemployment insurance benefits. Combining regular state continuing, extended benefits, and the Pandemic Emergency Unemployment Compensation programs suggest the total number of persons receiving benefits is approximately 9 million. The non-standard benefits do seem to be affecting employment, as states that have phased out enhanced benefits have seen a more rapid drop in continued claims.

Continued Claims in States by Duration of Enhanced Benefits



Source: Department of Labor, Goldman Sachs Investment Research

The phase-out of enhanced benefits by all states prospectively is consistent with Fed Chair Powel's belief that employment constraints will improve markedly from today in the second half of the year. The Federal Reserve has retained its stance that achievement of full employment remains a key pillar in measuring the economic recovery in the U.S.

3. INFRASTRUCTURE DEAL MOVES FORWARD

A $1.2 trillion, eight-year infrastructure deal was put forward with a bipartisan group of senators and accepted by President Biden. The deal includes $579 billion in new spending over 5-years with over half of that amount targeted at roads, bridges, public transport, airports, rail, electric buses, and electric vehicle infrastructure.

Passage of the deal hinges on negotiations over further spending and funding. These other areas for spending include education, healthcare, clean energy, caregiving, anti-poverty, and worker training. There is lack of bipartisan support on funding these additional measures and the process of reconciliation could delay or even derail the forward movement of the proposed infrastructure deal.

The market's reaction was positive to the progress with the stock prices of companies seen as direct beneficiaries moving up and overall the programs should be positive for economic growth more broadly.

4. DIVIDEND AND SHARE BUYBACK RESTRICTION LIFTED ON BIG BANKS

The Federal Reserve completed its stress tests, designed to measure the ability of a bank to withstand a severe recession, and declared that the nation's largest banks have strong capital levels. The Fed had been imposing additional restrictions on the amount that large banks could payout to shareholders in dividends and share repurchases, but those restrictions would be lifted if the banks met regulatory minimums in their stress tests. It is expected that banks will be aggressive in paying out capital for the rest of 2021.

Thinking Ahead

Forces driving economic growth continue to be in place, and hurdles to growth such as employment are likely to be overcome as the year progresses. Government policy continues to be supportive of economic growth and provides support for the financial markets. Pallas Capital Advisors will continue to monitor economic, political, and corporate data for implications to the markets.

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