Making Sense of the Unemployment Numbers - Transcript

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Tom Mullooly: Welcome back to the podcast. This is episode number 308. We are cruising into Nebraska. Moving along on our area code podcasts. Joining me for the ride today is Tim Mullooly and Brendan Mullooly.

Tim Mullooly: How's it going?

Brendan M: Got all good things to talk about, right?

Tom Mullooly: Yeah, why don't we start off by talking about what's going on with interest rates and the bond market. There's plenty to talk about with this.

Tim Mullooly: Yeah, there was an article in the Wall Street Journal; the headline was "Behind Bond Market Stall, Investors See Hard Times Ahead". And it was talking about the yield on U.S. Government bonds, I think specifically, the 10 year and how it's stalled out near all-time lows. And the author of the article was saying how that's a sign investors and people in the U.S. anticipate a painful economic recovery over the next couple years. And Bren what are your thoughts on that?

Brendan M: I'm not sure I totally agree, because I think they're assuming that the marketplace is setting the interest rates where it is, when that's not necessarily the case. It's been dragged down by what the federal reserve is doing with interest rates, and their intention of doing it is actually the exact opposite of what they're talking about. So instead of rates being low because people expect bad economic growth over the next 10 years, I think it's more that the fed is trying to make economic growth good over the next 10 years.

Tom Mullooly: I agree. In a weird way, there's infinite demand for these treasury securities, because not only is the federal reserve in the market every day, looking to buy treasury bills, notes, and bonds from banks. There's also plenty of places around the globe that just want to have the safety and a positive yield. The yield on a 10 year treasury as we're recording, this is 0.68% for 10 years. So when you think about that, what's a one year going to be? What's a CD at a bank going to be? I mean, these rates are going to be near zero, but it's that demand that the federal reserve has created that I think has helped keeping yields where they are.

Brendan M: Right, and you see that too, with a lot of companies offering out debt too at low interest rates. So what the fed's action has done is it encourages companies to offer bonds, which means they're receiving loans from people who are buying their bonds to get cash today and do stuff in their businesses. And right now that might mean just keeping the lights on and keeping the employees paid, but I mean-

Tom Mullooly: Or retiring older debt with higher rates.

Brendan M: Right, meaning their cashflow improves, and maybe they can do other stuff with the money, but I mean, they're issuing debt. And these are... They mentioned a couple of really big company. You can buy 10 year Costco debt for, you get an extra percent over the 10 year treasury note these days, but it's still super cheap. I don't think that means that things are looking bad for the economy moving forward, I just think it means that there's some interesting engineering going on behind the scenes.

Tom Mullooly: And it-

Tim Mullooly: I also think it might be a misinterpretation or a bad expectation setting in terms of what good economic growth is over the next 10 years. Because I mean, you look back at the last 10 years, rates have still been historically pretty low and the economy wasn't, I guess, meeting the expectations of four, 5% GDP growth. But I wouldn't say the economy was in bad shape for the last 10 years. I mean, everything was doing just fine.

Brendan M: And 10 years brings us back to 2010.

Tim Mullooly: Yeah, exactly.

Brendan M: I mean, it wasn't the hottest or fastest, highest growth GDP positive stretch in history, but it was one of the longest economic expansions in history, and it's only been interrupted now by freak of nature event. It wasn't necessarily even that things in the economy had overheated or gone wrong, it's kind of just like a natural disaster.

Tim Mullooly: I think people get kind of held up on the nominal numbers for GDP, and they don't really think about what it means in real terms.

Brendan M: Yeah.

Tom Mullooly: I think that there's some folks that might be at the fed and certainly fed watchers who say, all this quantitative easing that they did in 2009, 10, 11, and going forward, they were still hoping for, with each blast that there was going to be that 4% annualized GDP number, whether it was just for a quarter or two or for an entire year. And they never got it. But-

Brendan M: I think the interesting thing, and maybe you were getting to this point, is if we were hoping for 4% GDP growth, where are we hoping for 4% GDP growth with zero inflation? Or were we hoping for 4% GDP growth with 2% inflation, meaning nominal GDP of 2%, which is basically-

Tim Mullooly: Because we got that.

Tom Mullooly: That's exactly what we got.

Brendan M: But we got 2% GDP growth with no inflation instead, and so the headline number sounds like it's-

Tom Mullooly: Lackluster, right.

Brendan M: ...slow economic growth, kind of a malaise. And, I'm not sure that was the case. I mean-

Tom Mullooly: It actually worked out pretty much the way it should have in the sense that, remember one of the fed targets during QE, when they were talking about, we're not going to raise rates until we get inflation at 2% and it just never got there. And so their goal for inflation was 2% year over year. We've had these periods now where we've had low growth and little to no inflation. And I was told back in the early eighties, when I got into this business, that if we ever went into a period where we had steady low growth and no inflation, that's going to be Nirvana, that's going to be heaven for stock prices. And that's exactly what we got. But everybody was scared as hell on the way up.

Tim Mullooly: It was Nirvana for the stock prices, but everyone was complaining about it the whole time, so.

Brendan M: Yeah, I think like another piggyback topic off of this is just kind of with, with rates being so low, you kind of get into conversations, and they pertain to both bonds and stocks. So when the market goes on a good run, people will say, "Well, the market's so high, it can only go down from here, right?" And so people kind of have the same expectation of bonds and it's rates are so low, they've got nowhere to go but up, with the 10 year, at 0.7%. I've been hearing that for eight years now, since I started at the company here. And I know that at some point there's a limit to this, and I don't know where it is, but for people who in 2012 were beating the drum of don't put your money in bonds rates have nowhere to go but up, meaning if rates are going up, you're going to lose money in principle on your bonds, that was a really bad bet.

Because if you put money into... Here at our company, we use short and intermediate term high quality, treasuries and corporate investment grade debt to invest for clients, but the ones that are most sensitive to interest rates are the long-term bonds. So in 2012, if you put money into the 30 year T-bonds and looked at performance now, I mean, I'd venture to say, you made pretty good money. You might've made almost as good of money as you might've made in stocks over that time.

Tom Mullooly: I was just about to interrupt you and say that. I think if you had bought 30 year zeros, you probably would have done... You would have had stock like returns.

Brendan M: Yeah, right. Easy in hindsight, and also along with the stock like returns is near stock like volatility, which is why we don't necessarily use a long-term bonds in our portfolios here because we use them to tamp down volatility. So, I mean, you don't totally get that with us. But just point being that if you've got feelings about the direction of interest rates and you think it can only go in one direction, I would caution you against that because very smart people in 2012 were beating that drum, and they've been really wrong for eight years now. And it's not because they don't know what they're talking about is just because predicting the path that interest rates are going to go on is feudal and you don't need to do it.

Tim Mullooly: They could eventually end up being right, but being wrong for eight years is a really long time to be wrong. It's eventually it could happen, but-

Tom Mullooly: You'll be out of business.

Tim Mullooly: Right.

Brendan M: I don't think you get to take credit if your position takes that long.

Tim Mullooly: Yeah, true.

Brendan M: If you're... Yeah, if it takes that long, you-

Tim Mullooly: You were wrong.

Brendan M: Yeah.

Tom Mullooly: It's okay, you were wrong. It's alright. Don't stay wrong.

So this also propels the discussion when the fed is buying bonds in the open market like this, and they're keeping rates low, the discussion of the TINA market, there is no alternative. And so it pushes people into riskier investments.

Brendan M: Yeah, I mean, that's the option these days. I mean, you can't just retire and stick your money into treasuries and get four or 5% on it and live off the interest. I'm not sure that world ever existed anyway, as an aside, because inflation. Yeah, I mean, you have to come up with an appropriate mix because I think what you get with the bond side of your portfolio these days with rates as they are, one of the qualities of bonds that you would want is the interest, which is basically a throwaway at this point in time, but you still want to bake it in there into a portfolio meeting, because it's still there to be the ballast. It's still there to provide stability when the stocks are going down, assuming that you're using high quality bonds.

And I still think there's a value to it, but maybe the mix of a retiree's portfolio needs to be a little more reflective of reality these days. Meaning that the growth that you're going to need to stay ahead of inflation over time is coming entirely from stocks. So the bond piece is probably going to have negative real returns from where we're starting today, and that's okay.

Tom Mullooly: So when we talk about bonds and the bond market, it naturally kind of spills over into talking about mortgage backed securities, which the fed is also buying, and talking about the mortgage market. And there was some headlines that came out in the last few days about mortgages.

Tim Mullooly: Yeah, so there was an article in MarketWatch talking about how mortgage loans backed by Fannie Mae and Freddie Mac, they're making it easier to refinance for people that are in forbearance, but are still current on their payments. Or they're shortening the amount of time that you need to have been current before you can refinance after being in forbearance. Because I think originally it was 12 months. If you were in forbearance, you needed to be current for 12 months after that, before you can refinance, and now they're shifting it to three months to make it a little easier for people.

Brendan M: It seems like there are more people in this situation with everything going on right now and interest rates are really low, and I think the hope still from everybody is that this is going to be a short term blip for the economy and something that can help to stimulate the economy is people doing refinances or getting lines of credit from their properties or getting new mortgages. And I think they want to do everything they can to not prohibit people who want to do that from doing it.

Tim Mullooly: They were talking about just making sure that the mortgage industry continues to run efficiently. So if people want to refinance, they can.

Tom Mullooly: And it didn't run efficiently in 2009, 10, 11. There was actually a really good example, believe it or not in the New York Post, the bastion of business news. But they had one of these letters that they from a reader who wrote in and said, "Hey, I contacted Chase Bank about getting forbearance because I heard that everybody can..." With forbearance, you basically hit the pause button, in this case for three months. This guy had a $2,000 a month mortgage payment, and Chase said, "Sure, we'll put you on forbearance for 90 days. That's three months, three payments. But at the end of the forbearance period, you need to get current on your mortgage. So you're going to need to cough up $6,000 in 90 days." And he's like, "Why in the world would I get into a forbearance program when I have to come up with all of this money, a lump sum in 90 days? That doesn't help me at all."

And so there were discussions about, hey, maybe we should just tack those three months to the end of the mortgage, or maybe they can be a little flexible on this, but I don't think a lot of people understand what forbearance actually means. It's not that you're allowed to just skip a mortgage payment. We're just hitting the pause button here for a while.

Eventually those payments are going to resume. So the problem that Tim alluded to was that a lot of people wanted to refinance in 2009, 10, 11 to get out of some of the overwhelming debt that they had. In addition to their homes being upside down, they then found out from mortgage lenders that they couldn't refinance because they were in forbearance. And like you said, Tim, they found out the hard way that they had to be not only current, but they had to be 12 months past the end of the forbearance period. And people are like, "What the hell?"

Brendan M: Yeah, these could have been people who theoretically were down on their luck and then had turned things around, and then we're looking to further that by maybe refinancing and getting their mortgage payments to a more feasible level as they continue to get employment back and really get back on the right track. And then they were told, because of this thing that happened a year ago, you're still in trouble and you can't refinance. And that would have only helped them to... Theoretically it could have helped people to continue to recover quicker from a bad stretch, and so I think that's... They're trying to make that not happen this time, because I think that was probably a ripple effect that they did not intend to have coming out of a crisis, and maybe it prolonged some of the pain in housing, I mean-

Tom Mullooly: Absolutely, in my opinion it absolutely did.

Brendan M: Housing suffered until 2012, and the economy was getting better in 10 and 11.

Tom Mullooly: Yeah, this was not just a ripple, I mean, it was like a white cap, kind of a ripple. We didn't even hear these stories until 2010, 2011, where people had been... They've gone through forbearance, now they're trying to piece their life back together, and now they're finding out that they're stuck in a six or 7% interest rate mortgage because they can't refinance because of this forbearance thing.

Brendan M: I think that something that's come out of this whole pandemic situation has just been these... We're rolling out programs and trying to help people, and I think, in my opinion, we're doing a pretty good job of realizing quickly what unintended consequences we're creating and then reacting and updating rules or changing rules because ultimately the programs, a lot of these things were just rolled out as quickly as possible to help people. And then if we're discovering after the fact that there were some kind of unintended consequence that didn't help people as much or was a negative unintended consequence, we're fixing it. Which is, I think what this is. So I think it's good for everybody and I think it's just a sign that we're all trying the best we can.

Tim Mullooly: I think there was a stat in this article on MarketWatch though, that was saying that like 70% of the people who are in forbearance, ended up not needing it. I get when all of this started, there was even more uncertainty than there is now and people didn't really know what was going to happen, so maybe they kind of jumped the gun in terms of raising their hand for forbearance. But I think, think things through a little more. And also, if you voluntarily put your mortgage into forbearance and then you want to refinance, it's like, well, if you have the money to refinance your mortgage, you could have just not put your-

Tom Mullooly: Gone into forbearance to begin with.

Tim Mullooly: Gone into forbearance in the first place, but it's... I don't know-

Brendan M: I think they're trying to make it easy on those people.

Tim Mullooly: I have some empathy for people-

Brendan M: Right, because people didn't know.

Tim Mullooly: Yeah, there was a lot going on.

Brendan M: And so now to allow them to do something that, I said before, it's helpful to the economy that people are refinancing. It's good for the mortgage industry and it keeps them on their feet and maybe keeps the housing market from tanking-

Tim Mullooly: Stalling out, yeah.

Brendan M: ... like some people have expected or anticipated. We'll see what happens there. It could be helpful that this sort of activity can still occur and that we're not putting up barriers that don't necessarily need to be there for people to do it.

Tom Mullooly: I will say, I think that the whole financial industry has learned a lot and, and the government too, has learned a lot from the last time that they had to do this in 2008 and 2009. And the speed and the size and the velocity of these programs is, it's a huge difference from 2008 and nine. When the mortgage market basically seized up in 2008, you could forget about refinancing. You just couldn't get a loan.

Brendan M: Yeah, rates were super low, it did nobody any good.

Tom Mullooly: It didn't matter. Right, and so you wound up getting these zombie neighborhoods where people were well underwater on their mortgage, and they didn't want to pay because they knew that there was already a list 10 miles long of people who were ahead of them in the foreclosure line. And so there were, unfortunately for a lot of people, people were living in houses that they were underwater on, they were not making payments, the banks weren't getting money, the mortgages weren't getting paid, bond holders were suffering. I mean, it was a bad situation for everybody. I think a lot of these things like the forbearance period being 90 days, you know what, that's actually pretty good. And not having to wait 12 months to be eligible to refinance, that's good. These are things that are really going to, like you said, Brendan, this is going to really help keep the market moving.

Brendan M: which is, I mean, and that's what we've seen in this stock market too. With, with the fed stepping in to buy not only treasuries, but corporates too, and some municipal bonds. I mean, it's not just for fun, it's to help make these markets liquid, which is what we're talking about with the real estate market too. They want transactions to occur; they want business to be happening because it's ultimately in everybody's best interest.

Tom Mullooly: So it's Thursday morning, we're recording this. And Thursday mornings, the last few weeks has meant initial jobless claims. Let's spend a minute or two, just kind of talking through what these numbers mean.

Tim Mullooly: Yeah, there was an article outlined in the Wall Street Journal that talked about kind of making sense of jobless and unemployment numbers. Taking a look at are these jobless claims the same thing as layoffs. And in a sense they are, but we've also seen with the amount of people applying for unemployment at one time, not everyone is able to submit their claim at the same time. So we've seen states get overwhelmed with claims and have it carry over to a week or two weeks or three weeks. So there could potentially be people that got laid off five or six weeks ago that just got their claim submitted last week, so they show up in this week's initial jobless claims. So it's-

Tom Mullooly: I personally know someone who's been trying to get through to the New Jersey Unemployment Office since March 20th.

Tim Mullooly: So I think the overall number, it could still potentially be understated, but it's also potentially being stretched over a longer week period than it needed to be just because the system got overwhelmed and they couldn't report it all at once.

Tom Mullooly: It kind of put it-

Brendan M: Yeah, so we ultimately get to the-

Tim Mullooly: Well yeah, we'll get there.

Brendan M: The number will be the number the number eventually, but it may not be telling us in real time what's actually happening on a week to week. And we use this as a proxy for people losing their jobs, but it may not be updating us that-

Tim Mullooly: When are they losing it.

Brendan M: ... like so and so lost their job this week and had their claim filled, because like we've said that they could have lost their job several weeks ago and just got their application through this week.

Tim Mullooly: And it's going to be a moving number too, because even as we get... There's going to be numbers every week, but as more and more states start to reopen people are going to be able to submit their claims that got laid off a month ago, so their number is going to show up on the initial jobless claims, but there's also going to be people who maybe lost their job and was able to submit a claim six weeks ago that got rehired or something like that.

Brendan M: Maybe their business got a loan, and they ended up bringing all the employees back, and so they went on and then came off and then we haven't fully updated the numbers there yet either.

Tom Mullooly: Yeah, I've seen some headlines that say there it's possible there may be as many as 5 million people who have regained their jobs since the end of February, beginning of March, when the shelter in place started. I've also read that some people in the market are estimating that 80% of the job losses might be temporary. Now you may be temporarily furloughed, expecting that you'd be out of work for two or three or four weeks, but now that we're going on a much longer period of time, that business may not come back. And so some of these things that we were originally estimating to be temporary job losses may turn into permanent job losses. That's going to be a problem, but again, we're not going to know. We just have to continue to watch the numbers. So initial jobless claims come out every Thursday morning, and that gives us a sneak peek, state by state, of what the numbers are.

But then there's also continuing jobless claims, which are also... They're a week behind. So if you filed your initial jobless claim last week, this week, if you're still out of work, now you are part of the continuing jobless claims. And so right now, the number is that there's 25 million people who are still getting continuing unemployment claims. So the workforce prior to the slowdown was 155 million. So back in the envelope numbers, 25 million on 155 million jobs puts you around a 16% unemployment rate. That's... Like we were saying before we turned the microphone on these numbers are going to be squishy for a while.

Brendan M: A point that I'd like to add, the numbers are always squishy. So if you think you're discerning news about the economy, or especially what that means for stocks moving forward by looking at economic data, it's important to look at it, but I think it's important to remember that these are loose proxies for these things that we want to know about the economy, because you get these numbers, they're always rear looking, but not only are they rear looking, but a lot of them then get revised after the fact, because they're so noisy and they're not perfect ways to measure it, we revise them months later.

Tim Mullooly: They were talking in the article about how they usually, they seasonally adjust the unemployment numbers too, because, and they gave the example, usually around Thanksgiving and Christmas, they would seasonally adjust the unemployment numbers because a lot of temporary jobs pop up around the holidays for stuff like that. So they adjust it. I don't know how they're going to adjust it this year, but...

Brendan M: And so they do these things and we need these measurements in some form. I'm not saying they're not important at all, but I'm just saying that if you take them too literally, I don't think that they're providing you as much valuable information as you think. And I'm not sure how much I would bake them into any investment process.

Tom Mullooly: Right.

Tim Mullooly: You used to use the phrase "interesting, but not actionable."

Brendan M: Yeah, it's... I think-

Tim Mullooly: File it under that category, I think.

Tom Mullooly: That's a good way to-

Brendan M: That file cabinet is very big. Yeah.

Tom Mullooly: That's good. Just to put this in perspective, today's initial jobless claims number was 2.4 million people who filed last in the past week for their initial job was claims. A big number in a recession in the past used to be 210,000 people filed for job loss last week, 220, 230,000. Now we're getting 10 times. The other thing-

Tim Mullooly: But it's relative too, because compared to what it was four or five weeks ago, it's like oh only 2.4 million people. You get-

Tom Mullooly: Sounds like a win.

Tim Mullooly: Yeah. You get accustomed to these things pretty quick.

Tom Mullooly: The last thing I'll just throw in on this, if you're a sole proprietor and you don't have employees, so you don't have a payroll report, you basically what's left in the till at the end of the month is your profit. Those people, like a barber, okay. Those people are not included in jobless claims. So all of these small employers, like the boss, they've been out of work too. They're not even in these numbers. The actual number of people who are not working, it's a lot bigger.

Okay, that's going to wrap up episode number 308. Thanks again for tuning in, and we will catch up with you when we hit Peoria, Illinois, that's area code 309, our next episode.