Dear Client:

Seven months into the COVID-19 era... Just how are small businesses recovering from the deep economic decline the virus caused?

For smalls, the recovery looks like a K... One line pointing up sharply, for firms that are seeing their business bounce back swiftly. And one line pointing down sharply, representing the industries and businesses where business is bad and threatening to worsen.

Anything travel-related is still struggling, given the continuing slump in tourism and flying. Hotels, restaurants and other hospitality businesses are in for further pain before things get better.

A fifth of small firms are mulling layoffs in the next six months if Congress doesn't deliver on further financial assistance, per one survey.

Most smalls are holding off on expanding as they wait to see when a vaccine may be available, and whether states impose more restrictions this winter if and when virus case counts mount.

But for some small firms, business is good. In construction, for instance, employment is almost back to its level of last winter, before the pandemic up-ended the economy. Many manufacturers are doing well as consumers spend less on services and more on manufactured goods.

Interestingly, the smallest of smalls have been holding up better than rivals with larger head counts. Two-thirds of companies with fewer than five employees reported not laying off any workers this year, whereas more than half of companies with 20 or more workers had to let someone go. Yet employers with four workers or fewer received less help from the feds' Paycheck Protection Program loans.

Also surprising: Small-business formation has jumped during the crisis, up 18% annually during the pandemic months, based on applications for new tax IDs. Prior to COVID-19, those applications had been growing at only 2% per year.

Looming over all small businesses, whether they’re doing well or not now: The risk of renewed government lockdown orders to limit a second wave of COVID-19 infections. Most northern states are already seeing rising case counts as colder weather sets in and people spend more time indoors, in closer proximity.

How much small businesses are hurt will depend on how their states react to potential outbreaks. One lesson from the summer is that states face a trade-off between economic activity and infection rates. Opting for more business activity generally means having to tolerate more cases. Trying to hold down the case count causes business to suffer. Every state will be seeking some balance of the two.

The next few months are going to be tough. Vaccines and other treatments are in the works, but none are yet proven and ready to get the virus under control.
World trade has clawed back about 75% of the losses caused by COVID-19. Robust monetary and fiscal policies have been key, propping up incomes across the globe, allowing consumption and imports to rebound once lockdowns were eased. Every region of the world saw an increase in exports this summer. China’s massive export sector has already returned to prepandemic levels. Meanwhile, exports from the U.S. are still down about 18%. Strong demand for COVID-related products has partially offset weakness in other areas, one reason that world trade has held up better than global GDP. Trade will continue to recover in the fourth quarter. The latest data from Asia, excluding China, show trade volumes just a tad below prepandemic levels. For the full year, global trade in goods will fall around 9%. By comparison, global merchandise trade fell 12% in 2009 during the height of the financial crisis. Next year, world trade will bounce back 7.2%, as long as borders stay open.

The next potential target of the Trump administration’s trade retaliation: Vietnam. The U.S. Trade Representative has opened an investigation into Vietnam’s trade practices under Section 301 of the Trade Act of 1974, the same law used to justify the administration’s retaliatory tariffs against China. U.S. trade with Vietnam has grown rapidly over the past two decades, from $1.5 billion in 2001 to $77.6 billion in 2019. So too has the U.S. trade deficit with Vietnam, now America’s fifth-largest (after China, Mexico, Japan and Germany). Note how supply chains have shifted in response to the U.S.-China trade war, with Vietnam a popular destination for manufacturers of apparel, appliances, furniture and other goods trying to avoid U.S. tariffs, as well as the rising cost of doing business in China. From 2018 to 2019, the U.S. trade deficit with Vietnam increased by 40%, from $39 billion to nearly $56 billion, versus a 1% increase from 2017 to 2018.

The European Central Bank has started experimenting with a digital euro and the ECB will decide around mid-2021 whether or not to move forward. Cryptocurrencies are regularly criticized by central banks as speculative assets, but they’ve prompted many nations to look at their payments and currency systems. A digital euro would have several benefits for its users. Eurozone residents could place deposits with the ECB directly...potentially safer than commercial banks, which can go bust. And like cash, money could also be stored outside of banks in a “digital wallet.” Cash is still the most common way of making small payments at retailers, accounting for about 73% of payments in the eurozone in 2019. A virtual euro would also allow the ECB to fend off other digital currencies, such as bitcoin or versions from large private companies, like Facebook’s Libra.

One lagging sign of a deep recession: An uptick in prepaid wireless plans. Expect subscribers to the lower-cost plans to increase next year and beyond as cellular providers end their COVID grace periods, when they didn’t cut off service, and millions of unemployed or underemployed consumers seek cheaper options. Verizon’s planned $7 billion purchase of Tracfone is a big bet on the trend. Tracfone has 21 million subscribers, the most in the market. Other prepaid sellers include Dish, Consumer Cellular, Comcast and Charter. During the Great Recession, the market saw significant growth for four years as traditional subscribers dipped.

Protecting against ransomware attacks doesn’t have to break the bank. Best practices include backing up data, encrypting files, using spam filters, setting up multifactor authentication and disabling USB storage access. Executives should get special training, since they’re higher-risk. A free tool, No More Ransom, provides decryption software to use if hit by an attack at www.nomoreransom.org. Many firms have retainers with third-party security experts, just in case. Companies need a clear plan and a phone number ready to call if hit with an attack.
Democratic Senate candidates in tough races are raking in the cash. The latest political rainmaker: Kansas Democrat Barbara Bollier, who pulled in a state record of $13.5 million in the third quarter of this year. Polls show a tightening race between Bollier and Roger Marshall, her Republican opponent for the open Senate seat now held by Pat Roberts (R), thanks in part to growing support for Democrats in the Kansas City suburbs. But a Democratic win in the Sunflower State would be a shocker.

The party hasn’t held a Senate seat in Kansas since the Great Depression.

So, too, would a Republican victory in the Mich. Senate contest, which is already the most expensive in the Great Lakes State’s history. Still, polls show incumbent Gary Peters (D) struggling to break away from GOP challenger John James, who is black and an Iraq War veteran. Both candidates recently reported massive third-quarter fund-raising totals. Mich. is the GOP’s next-best hope for a 2020 Senate pickup after Ala., where Democrat Doug Jones trails Republican challenger Tommy Tuberville.

Political sex scandals aren’t what they used to be. Just ask Cal Cunningham. The Democratic Senate candidate in N.C. has actually expanded his lead over incumbent Thom Tillis (R), despite the recent revelation that Cunningham, who is married, exchanged explicit text messages with a woman who is not his wife.

The issue isn’t dead. But most N.C. voters say it won’t change their minds. N.C. is key to Democrats’ hopes of taking control of the Senate this fall. The race is on track to be the most expensive Senate election in history.

Some things we learned traveling and reporting in the Tar Heel State: N.C. remains a land of political extremes, with solidly blue urban areas, such as Raleigh and Charlotte, surrounded by solidly red suburban and rural areas. Even in the state’s handful of swing counties, most voters remain highly polarized along racial lines, with white folks largely Republican, black folks largely Democratic. Even since 2016, the state has experienced high levels of in-migration, lifting the population of urban Wake (Raleigh) and Mecklenburg (Charlotte) counties, and also their surrounding suburbs, where Democrats hope to make inroads in 2020. Brunswick County, a GOP stronghold, has also grown fast as a magnet for retirees.

In short, expect a close election, no matter which candidate prevails. The state is a must-win for President Trump, who is hoping his loyal base of conservative support can blunt Biden’s strength among urbanites and rural blacks. Democrats need strong African-American turnout, which was low in 2016.

Also on our swing state tour: Pa., a state Trump narrowly won in 2016. And Ohio, a state he won by eight points. Both are in play this year, a bad sign for the president as he tries to shore up his coalition before Election Day.

The big challenge for the president in these states: The suburbs, where voters are shifting in the Democrats’ favor...a national trend...from Philadelphia to Cincinnati. But Trump is also losing ground in many blue-collar counties that he won in 2016...think Ohio’s Trumbull County, which used to be a Democratic stronghold. Where the president is popular, he is very popular, especially in western Pa. Outside of Pittsburgh, the landscape is blanketed with Trump signs and flags.

A red flag for Democrats: There is plenty of disenchanted with their party, as well as distrust of prominent lawmakers, such as Calif. Sen. Kamala Harris, Biden’s running mate. This includes voters who are generally OK with Biden himself. We give Biden a slight edge in Pa., while Ohio remains too close to call. No Republican has ever been elected president without winning Ohio.
A sign that a serious effort to take on Big Tech’s dominance is under way: The first major congressional antitrust report in decades, released on Oct. 6. The House Judiciary Com. report called out anticompetitive behavior by Amazon, Apple, Facebook and Google. Democrats want to aggressively beef up antitrust laws, plus add new regs. Republicans don’t fully agree with the report or recommendations, but some see areas of compromise, setting the stage for talks that could lead to action. 

But don’t expect major changes soon. New laws or regs will take a while.

One area of growing agreement: Giving federal regulators more resources, both funding and expertise. Such low-hanging fruit is likely to be one of the first steps.

Facebook and Twitter will continue to ramp up efforts related to the election. Recent actions target premature claims before official election results are in. Both platforms are preparing for delayed results. They will add information labels and take down misleading or false posts on Election Night and in the days after. When in doubt, the companies will try to slow down posts’ viral spread.

Lawmakers are watching closely and new regulations could stem from Nov. 3, related to how sites deal with calls for violence, foreign meddling and other issues.

The Pentagon is working to ensure a steady supply of secure semiconductors for the cutting-edge weaponry the Dept. of Defense needs to keep pace with China, as well as Russia, in a new era of great-power military competition.

One idea: Entice more chipmakers to open up fabrication plants in the U.S. Currently, 75% of semiconductors designed by U.S. firms are produced offshore; 95% are packaged and tested offshore. Congress will soon pass a defense policy bill that features numerous incentives for chipmakers willing to manufacture in the U.S.

Another idea: Design chips with security in mind. DoD’s research arm, DARPA...Defense Advanced Research Projects Agency...is working with both tech firms and major defense contractors on ways to make chips less vulnerable to tampering.

The Dept. of Energy is laying the foundation for a new quantum internet. The idea: An “unbreakable” network of secure, next-generation computers, enabled by quantum mechanics. The agency’s 17 national laboratories will serve as the backbone of the new system, which should be completed within a decade.

Such networks aim to exploit the peculiarities of quantum physics, in which particles can exist in multiple states at the same time and become entangled, sharing information with each other over long distances without a physical connection. In theory, they would be “virtually unhackable,” per Dept. of Energy officials, since the very act of trying to intercept quantum transmissions can also destroy them.

Weed isn’t just for young people. Older folks are increasingly lighting up, too. About 5% of Americans 55 and older reported in a 2016-18 survey that they used cannabis (marijuana or hashish) in the past month. Consumption, which is higher among men than women, has likely risen further since then. Why? New pot education, changing attitudes and the continuing trend of state legalization. Many seniors are using pot for pain relief and other medicinal purposes. But older folks should be careful and consult a physician before partaking.

Yours very truly,

Oct. 16, 2020

THE KIPLINGER WASHINGTON EDITORS

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