



Sunwest Bank Economic Outlook

■ November 2, 2023

Last Year's Predictions That Hit the Bullseye

- Federal Reserve Prediction: The Fed would have to halt Quantitative Tightening in the first half of 2023.
 - Outcome: The Fed halted QT in late March, pumping \$391B of liquidity into the economy.
- Monetary Policy Prediction: The Fed would break something.
 - Outcome: Silicon Valley, First Republic, and Signature Bank broke.
- CRE Prediction: CRE cap rates would continue to rise, and CRE property values would fall by 15-30%.
 - Outcome: Cap rates continued to rise, and most CRE values fell by over 15%.
- Residential Real Estate Prediction: Residential real estate transaction volumes would stay depressed because many homeowners would be locked into their homes due to low fixed-rate mortgages.
 - Outcome: Residential sales activity continued to decline and are at lows not seen since 2010.
- Political Prediction: The Republicans would begin a series of investigations focusing on Hunter Biden, COVID lockdowns, and Anthony Fauci's funding of gain-of-function research of COVID.
 - Outcome: The Republicans began a series of investigations on these issues.
- Presidential Election Prediction: Democrats would start pressuring Biden to step aside and find a new presidential candidate for 2024. The Republicans would have at least 3 candidates to challenge former President Trump if he runs.
 - Outcome: Pressure is building for Biden to step aside, and multiple candidates are running against Trump.

Last Year's Predictions That Were on the Board

- Interest Rate Prediction: After the 75-basis point rate move in November 2022, the Fed would increase short-term rates by another 50-100 basis points and then pause.
 - Outcome: The Fed has increased rates by another 150 basis points, more than the market predicted.
- Equity Markets Prediction: There would be at least a few bear market rallies during 2023, and if the Fed pivots, there could be a larger rally to bring the markets back to last November's levels.
 - Outcome: The markets experienced volatility but rallied beyond last November's levels.
- Fixed Income Prediction: Corporate credit spreads, particularly high-yield, would blowout as defaults and credit losses materialize. The CMBS and CLO markets would seize up.
 - Outcome: Spreads widened, and the CMBS and CLO markets froze up for periods of time but now remain open at much reduced volumes.
- U.S. Housing Prediction: Prices would fall 10% in 2022 and would decline by another 10-15% in 2023.
 - Outcome: After a modest pull back in 2022, median home prices have fallen by 13.2%.

Last Year's Predictions That Were on the Board

- Europe Prediction: It would fall into a severe recession with the risk of one of the PIGS (Portugal, Italy, Greece, Spain) having a funding crisis.
 - Outcome: Europe has now entered a mild recession, but it is too early to tell the severity of the recession.
- China Prediction: Once China rescinds lockdowns, it would cause a temporary economic boom but also an inflationary spike. The boom would fade within a few quarters, and China's property markets would collapse.
 - Outcome: China did not receive much of a boom, and its property markets have continued to collapse.
- Congressional Prediction: The Republicans would take back control of the House and win 25 or more seats. The Republicans would pick up 2 Senate seats and regain control of the Senate.
 - Outcome: Republicans took control of the House but only gained 9 seats and lost 1 seat in the Senate.

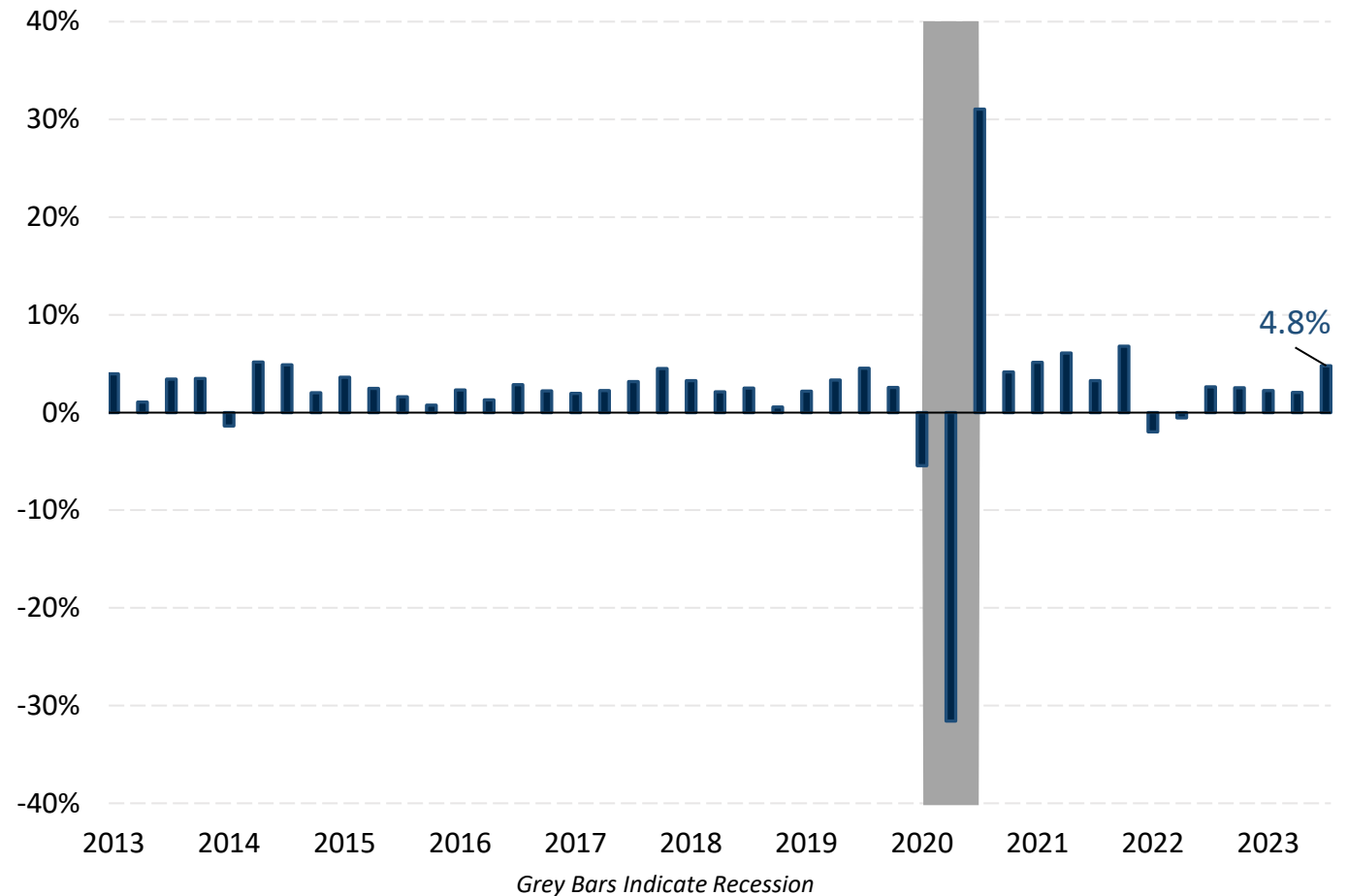
Last Year's Predictions That Missed the Board

- U.S. Economy Prediction: We would be in recession for most of 2023. There could be a quarter of positive growth during the year, but the U.S. would largely be in contraction.
 - Outcome: The economy remained more resilient and grew 3.0% on average per quarter.
- Unemployment Rate Prediction: It would rise and reach at least 5% by the end of the year. Job losses would impact the white-collar worker more than the blue-collar.
 - Outcome: There has not been any deterioration in employment with the unemployment rate remaining at 3.8%.
- U.S. Equity Markets Prediction: Major indices would contract by at least another 20% over the next 6 months due to downward earnings revisions and liquidity being drained from the markets.
 - Outcome: This did not occur due to a massive liquidity injection by the Fed.
- Interest Rate Prediction: Once a crisis occurs, the Fed would start to cut rates, but it would be too hard to determine the size of rate cuts, which would depend on the severity of the crisis.
 - Outcome: A crisis occurred, but the Fed stabilized it through other means and continued to raise rates.

The Economy Remained Unusually Resilient

- The most recent Q3 GDP annualized growth rate was 4.8%.
- The year began with positive annualized growth rates of 2.2% in Q1 and 2.0% in Q2.
- These succeeded two negative prints last year of -2.0% and -0.6% in Q1 and Q2, respectively. But 2022 ended stronger with prints of 2.6% in Q3 and 2.5% in Q4.

U.S. Real Gross Domestic Product QoQ Change (%)

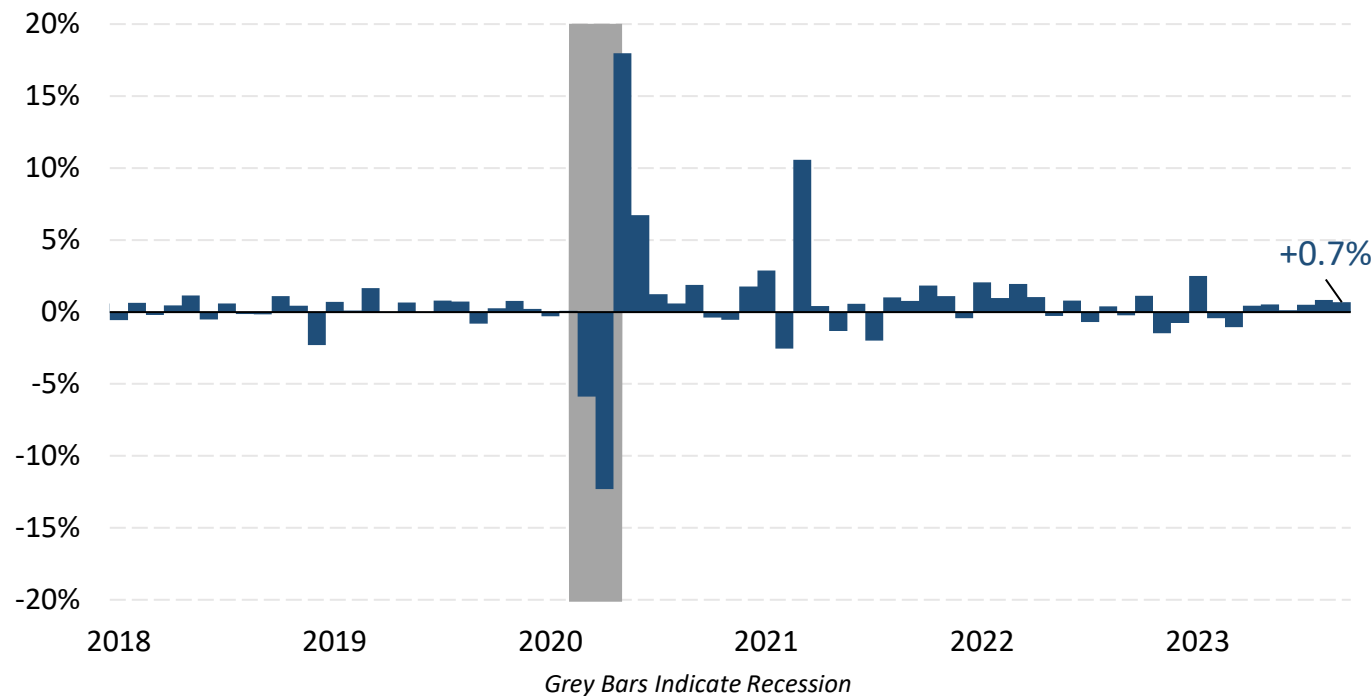


Source: Bureau of Economic Analysis

Consumer Spending on Services Persisted Unabated

- After a strong start to the Christmas season negative growth rates in February and March soon followed, however retail sales have now risen for 6 straight months, printing a much stronger-than-estimated 0.7% MoM in September.

U.S. Retail Sales MoM Change (%)



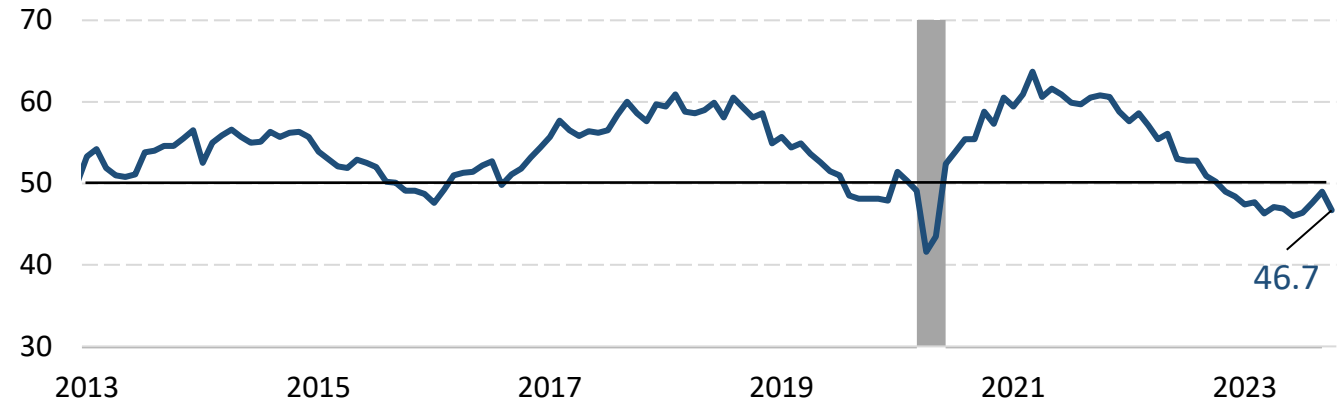
Kind of Business	Adjusted YoY
Food Services Places	9.2%
Health & Personal Care Stores	8.3%
Retail & Food Services	3.8%
General Merchandise Stores	2.0%
Food & Beverage Stores	1.6%
Electronics & Appliances Stores	1.0%
Motor Vehicle Dealers	1.0%
Non-Store Retailers	0.6%
Clothing & Accessories Stores	0.1%
Miscellaneous Retailers	-0.2%
Sporting Goods & Other Hobby Stores	-2.1%
Gas Stations	-3.5%
Building Material & Suppliers Dealers	-4.0%
Furniture Stores	-5.9%

Source: United State Census Bureau

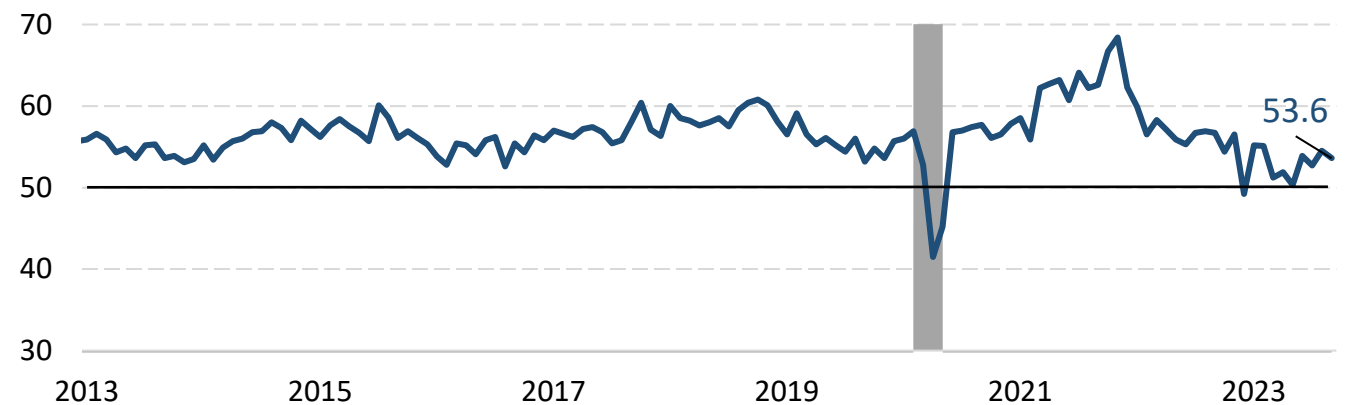
A Tale of Two Economies

- Manufacturing has remained in contraction for the past 10 months and contracted again to 46.7 in October.
- Services has continued to expand, albeit at gradually lower rates since its peak of 68.4 in November 2021, now standing at 53.6 in September.
- For PMI, a measurement above 50 represents expansion, while a measurement below 50 represents contraction.

U.S. ISM Manufacturing PMI



U.S. ISM Services PMI

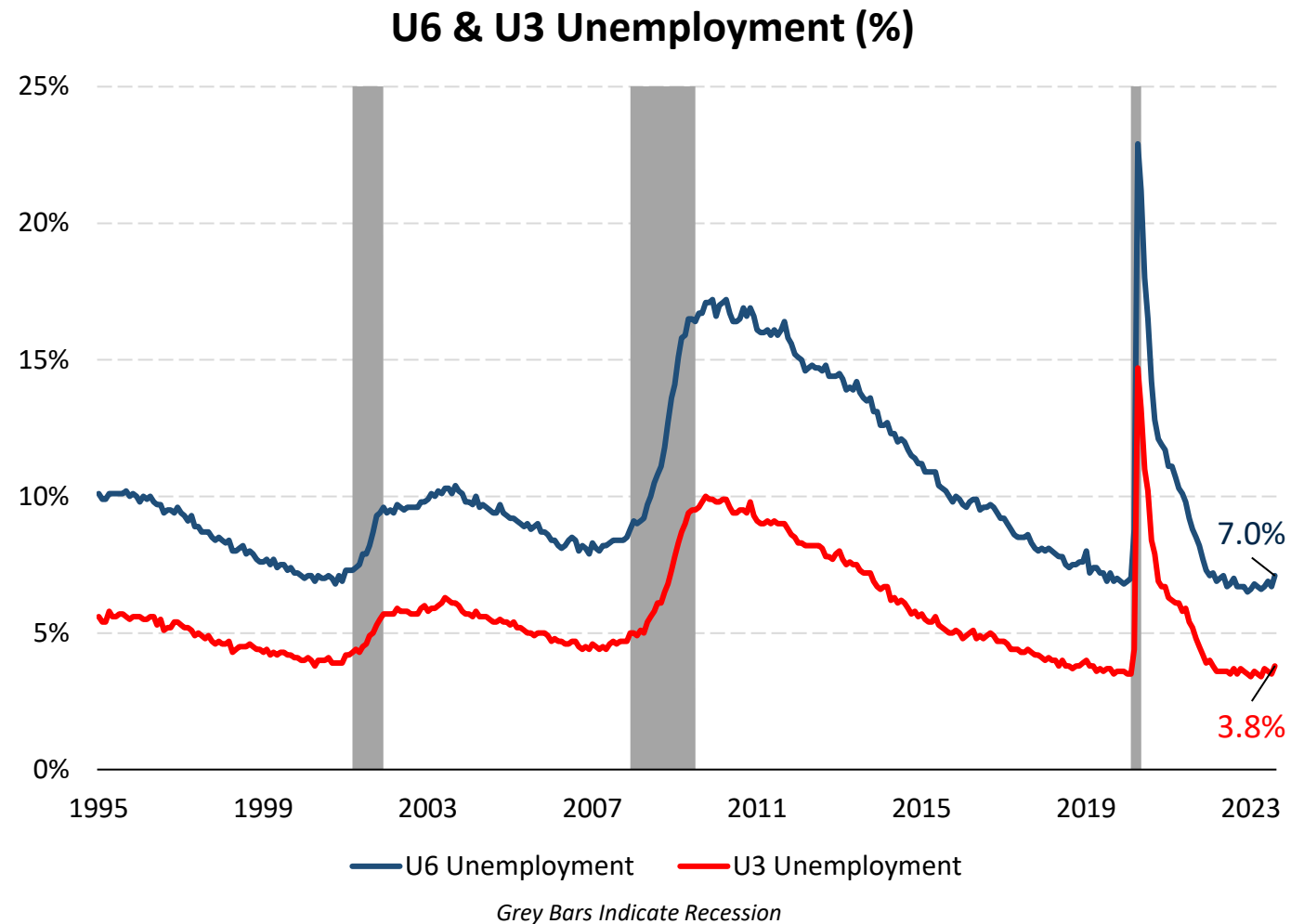


Grey Bars Indicate Recession

Source: Institute for Supply Management

Employment Withstood Numerous Headwinds

- Employment has defied contractionary pressures with the latest September U3 and U6 unemployment rates at 3.8% and 7.0%, respectively.
- The establishment survey reported that 336K jobs were created in September, and the household survey showed 86K, primarily in hospitality, construction, and healthcare.
- Headline gains have been driven by part-time workers. Since June, full-time workers decreased 692K while part-time workers rose 1.2M.



Best Way to Avoid a Hangover Is to Keep Drinking



Three Main Reasons the Economy Remained Resilient



Federal, State, and Municipal Government Spending

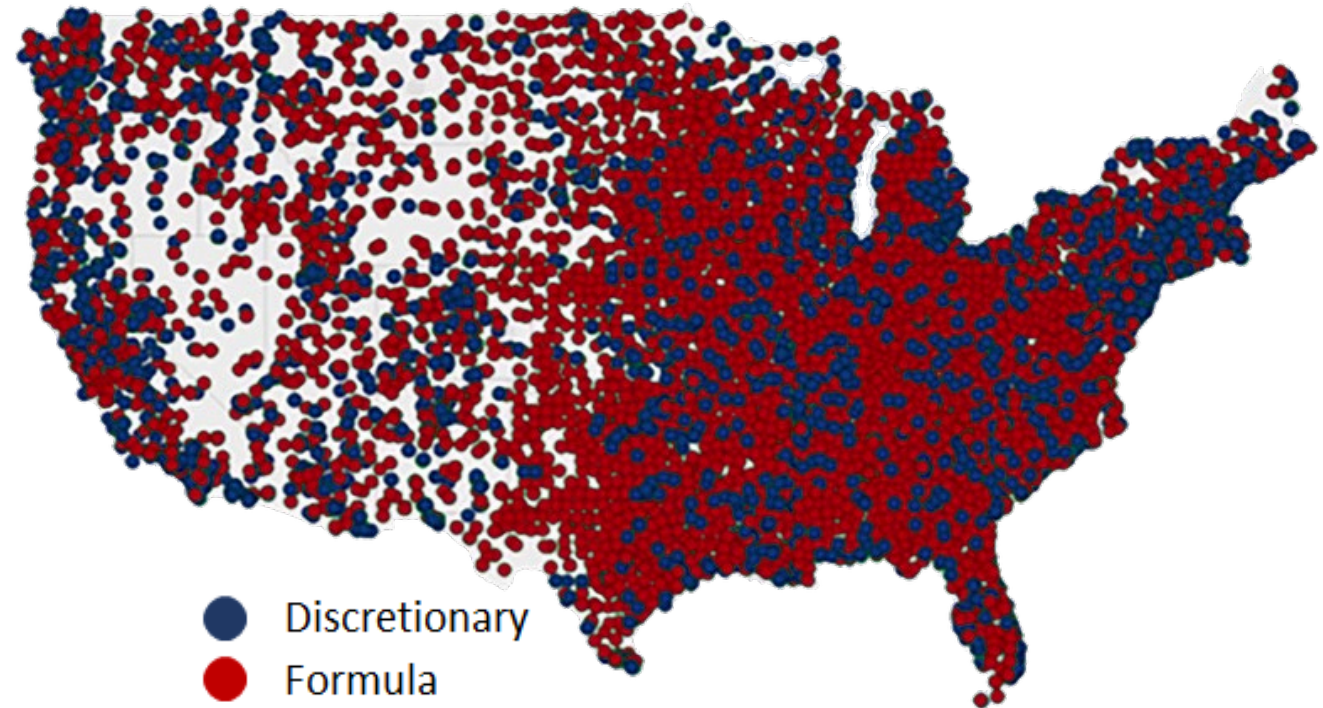
A Resilient Consumer

Failure of Silicon Valley, Signature, and First Republic
Banks Triggered the Fed to Restart QE Briefly

Unprecedented Public Spending – COVID Money Unleashed



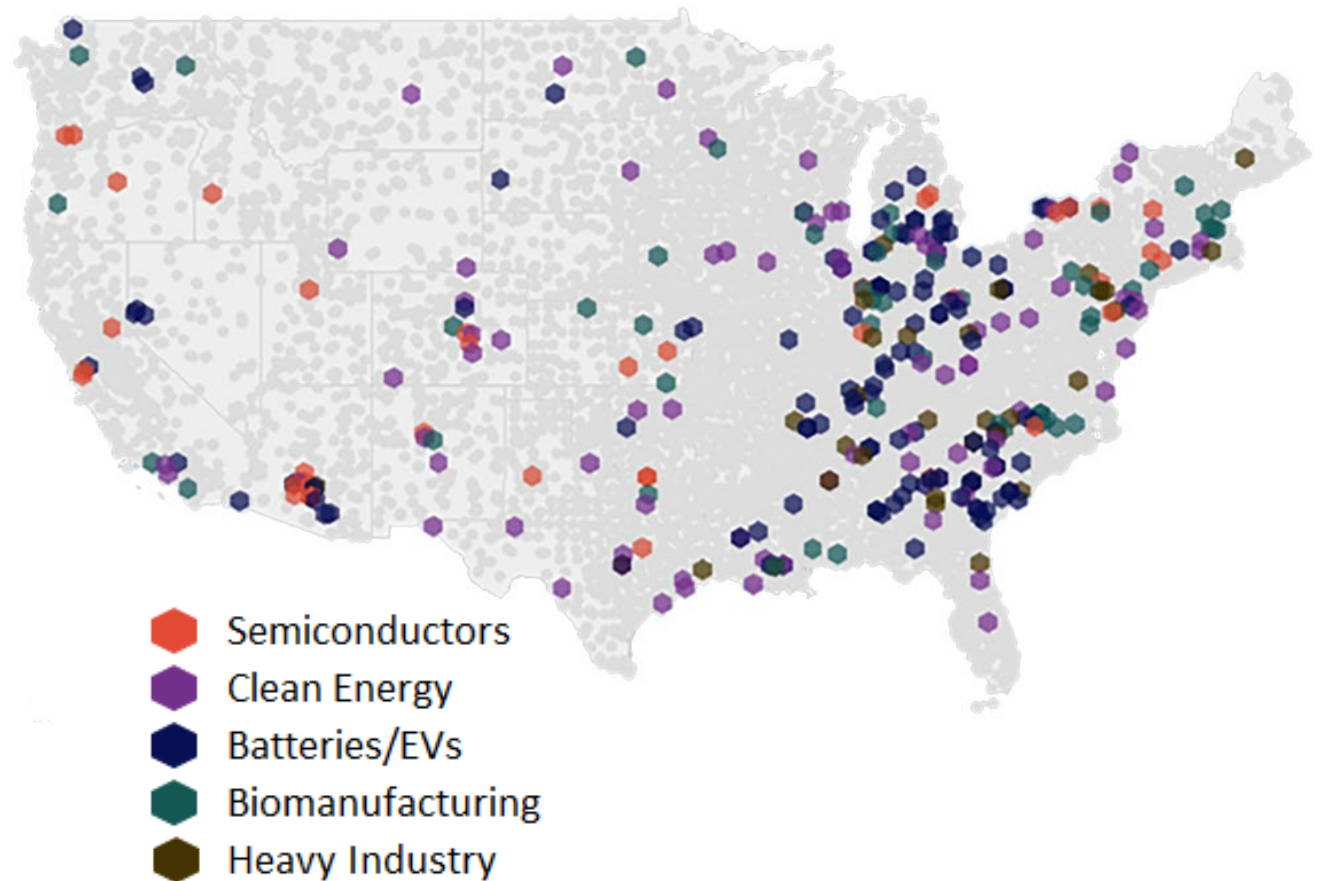
CARES Act March 2020	\$2.2 TRILLION
Consolidated Appropriations Act December 2020	\$900 BILLION
Other Related 2020 Spending	\$400 BILLION
American Rescue Plan Act March 2021	\$1.9 TRILLION
Infrastructure Investment and Jobs Act November 2021	\$1.2 TRILLION
The CHIPS and Science Act August 2022	\$280 BILLION
Inflation Reduction Act August 2022	\$437 BILLION
Total as of November 2023	\$7.32 TRILLION



Source: WhiteHouse.gov

Corporate Welfare for R&D

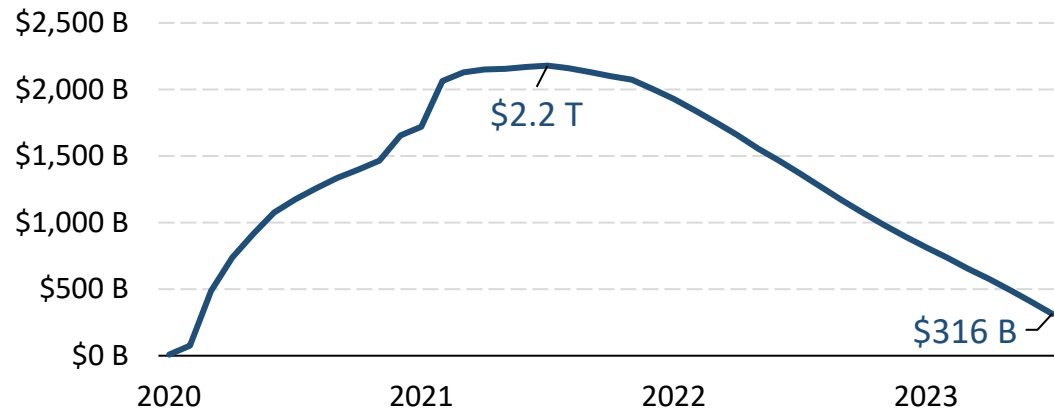
- The Infrastructure deal directs \$1.2T into re-building physical infrastructure, such as roads, bridges, airports, and EV charging stations.
- The CHIPS Act spends \$280B on STEM workforce development and R&D.
- The Inflation Reduction Act disburses \$500B for green energy initiatives.



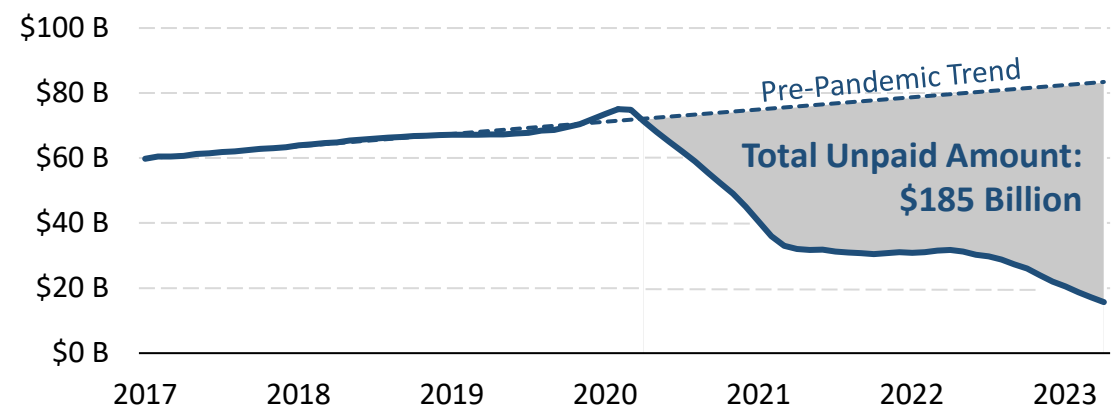
Forces That Lifted Consumers – Biggest Part of GDP



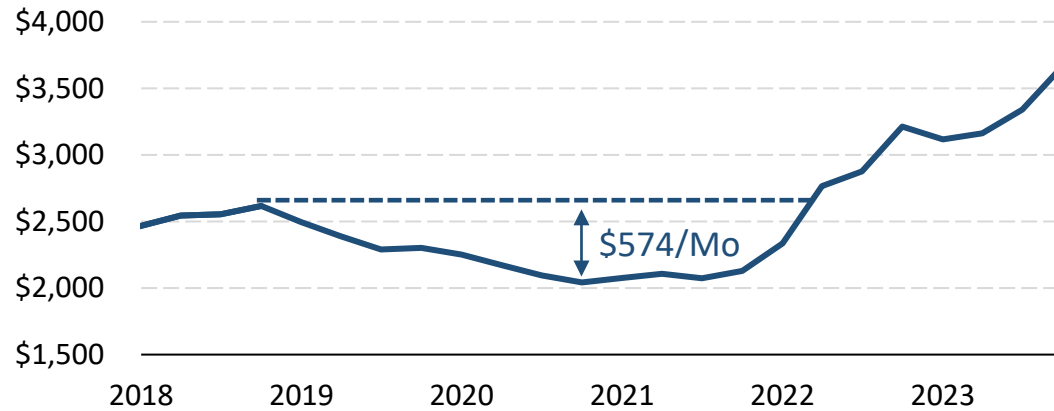
Excess Savings (in \$ billions)



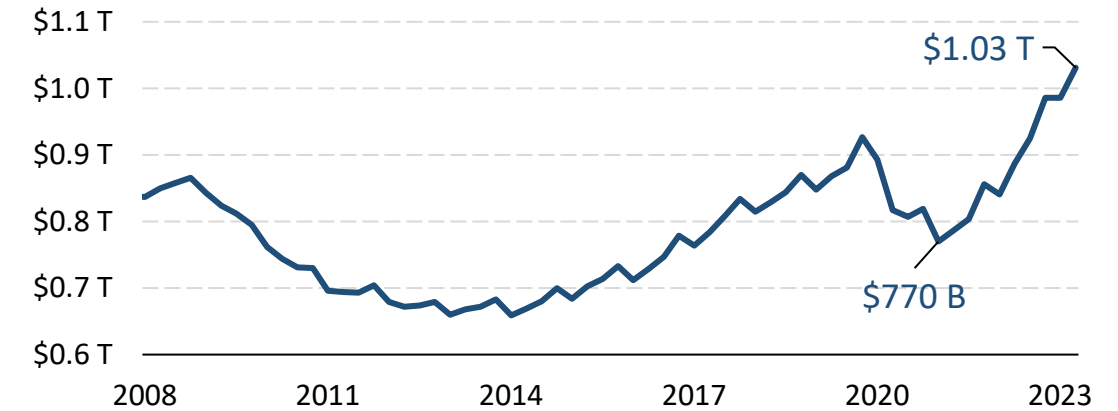
Student Loan Repayments (in \$ billions)



Monthly Payment on \$500K Mortgage



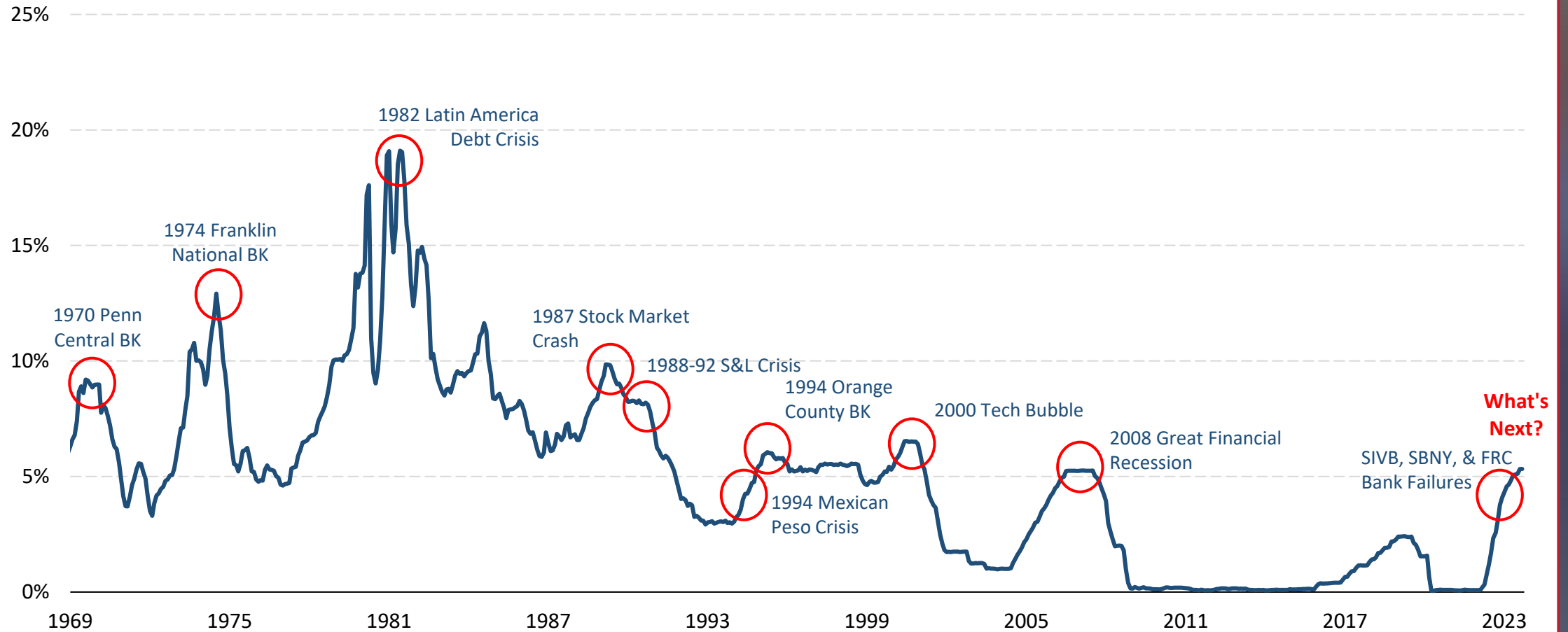
Credit Card Balances (in \$ trillions)



Source: Bureau of Economic Analysis, Treasury Department, Author's Calculations, Bloomberg

The First Thing to Break... Three Regional Banks

U.S. Federal Funds Target Rate (%)



What's Next?

The Overnight Response

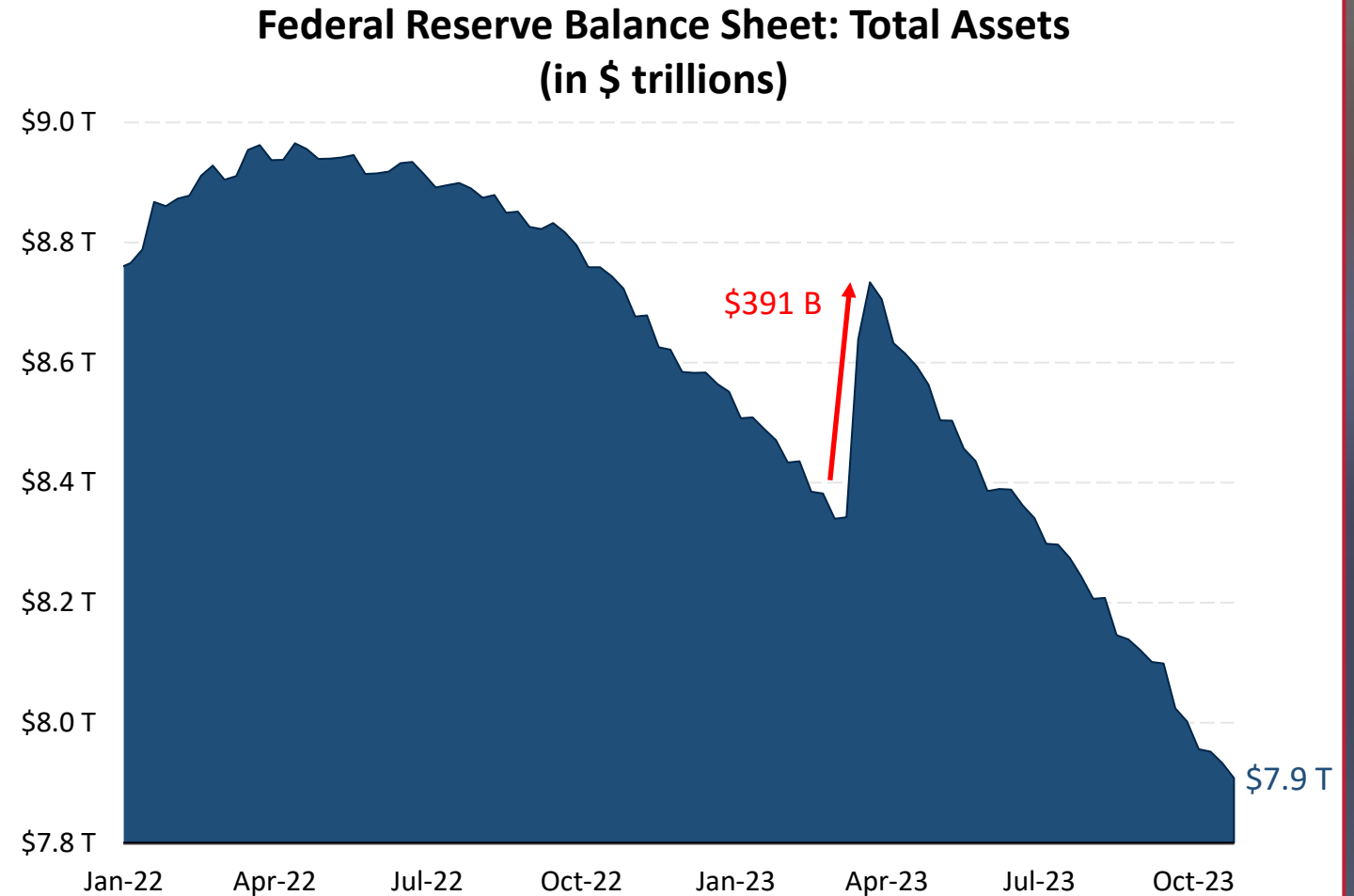


US politics & policy

The weekend US officials hatched a plan to
stave off a banking crisis

Fed and Treasury Took Emergency Actions

- Following the bank failures, the Fed injected \$391B into the economy, taking its balance sheet back to October 2022 levels.
- The Bank Term Funding Program (BTFP) has grown to over \$107B since its inception in March 2023.
- The Treasury insured all deposits at SIVB, FRC, and SBNY and used other tools to provide liquidity.



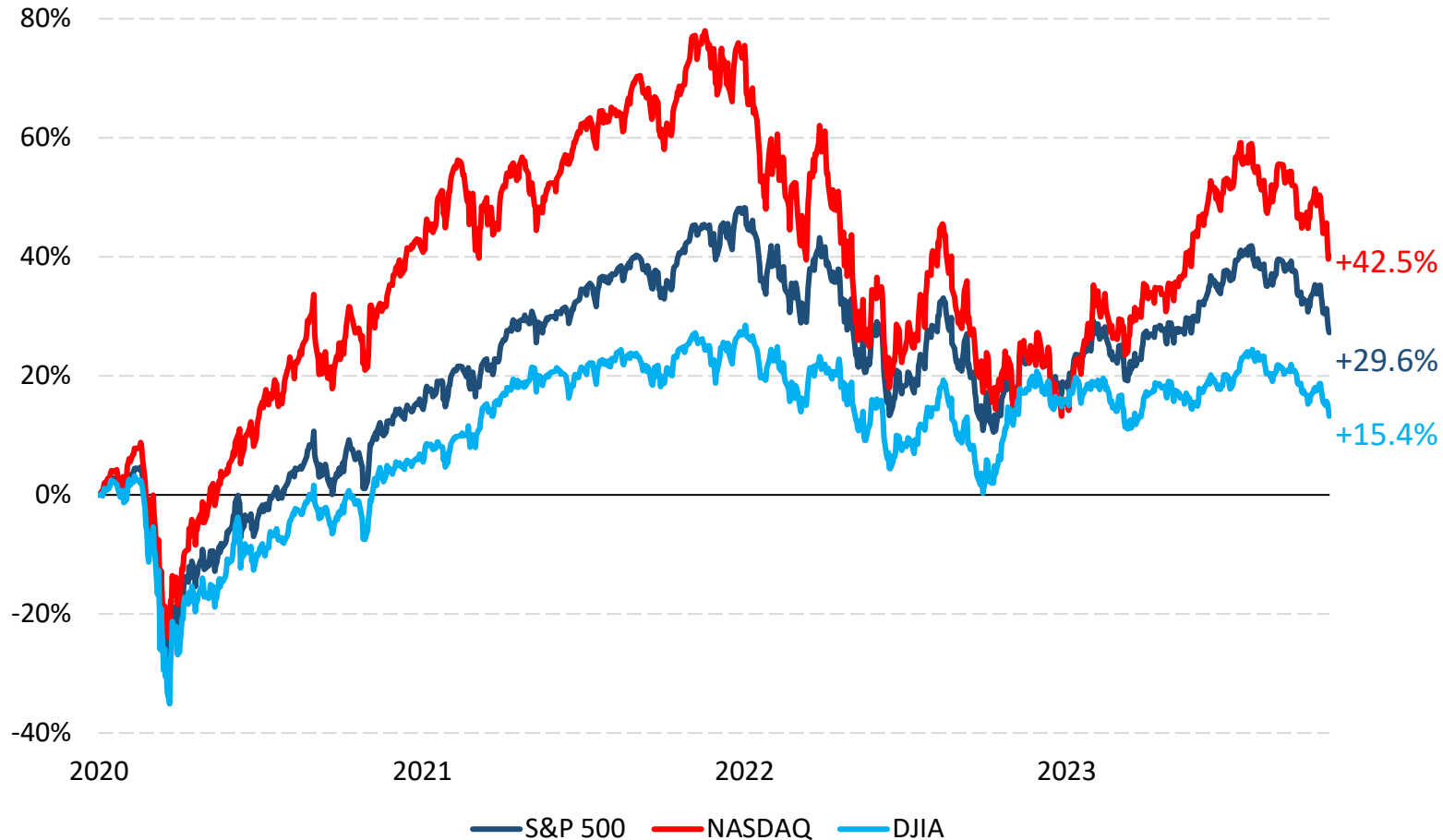
An After Party Commenced



Equities Tumbled Then Rallied Post Liquidity Injection



U.S. Equity Returns Indexed to 2020 (%)



S&P 500 Sector Performance: YTD

Communication Services	+33.6%
Information Technology	+31.4%
Consumer Discretionary	+17.7%
Industrials	-1.8%
Energy	-3.5%
Materials	-3.6%
Financials	-8.2%
Health Care	-9.5%
Consumer Staples	-9.7%
Real Estate	-12.7%
Utilities	-16.8%

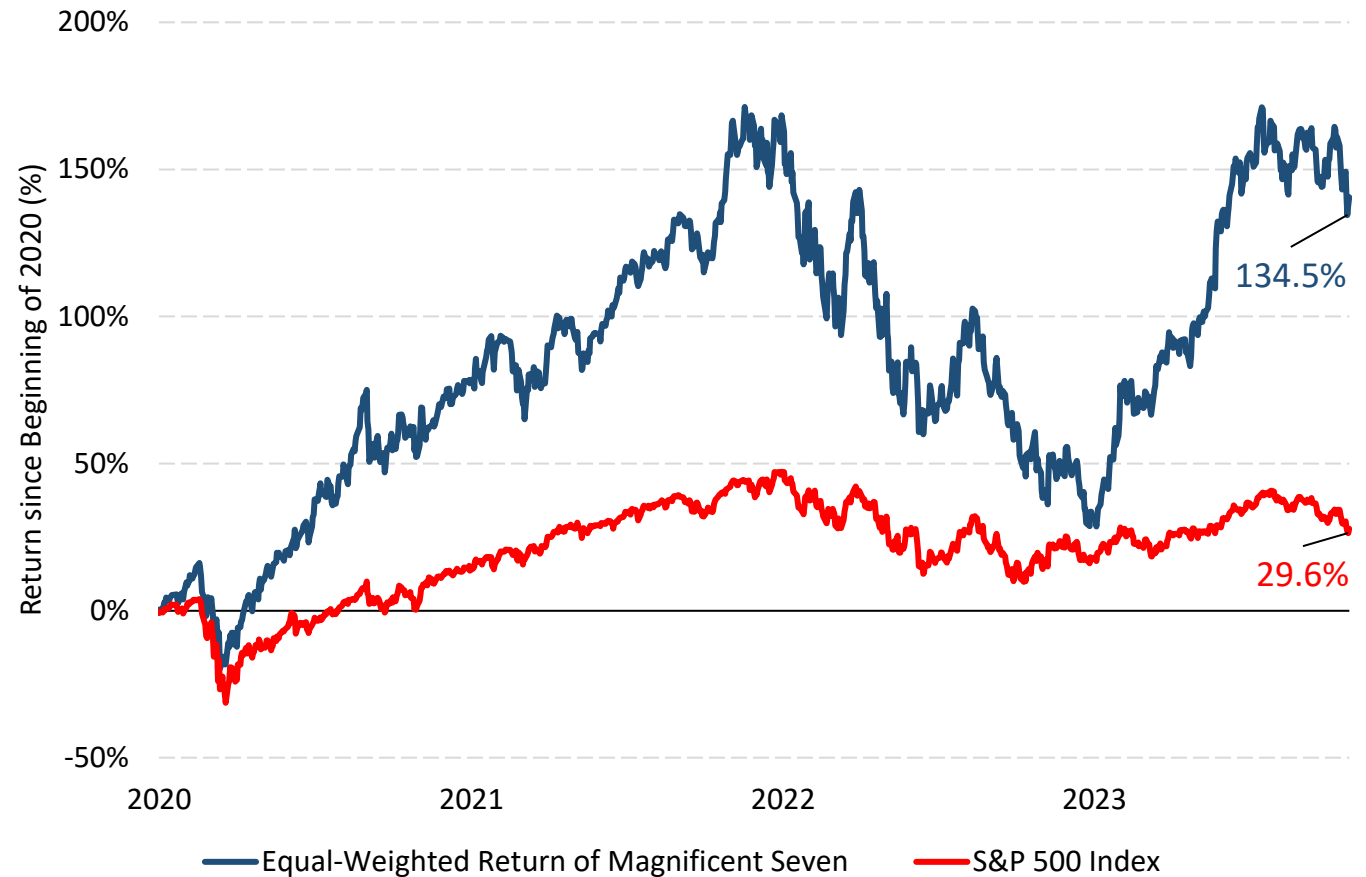
Source: Yahoo Finance, Fidelity

Magnificent-7 Drives Market Returns

Company	Market Cap	P/E LTM
Apple	\$2.7 T	28.9x
Microsoft	\$2.6 T	33.4x
Alphabet	\$1.6 T	23.9x
Amazon	\$1.4 T	70.5x
Nvidia	\$1.0 T	101.0x
Meta	\$788 B	27.1x
Tesla	\$638 B	64.7x

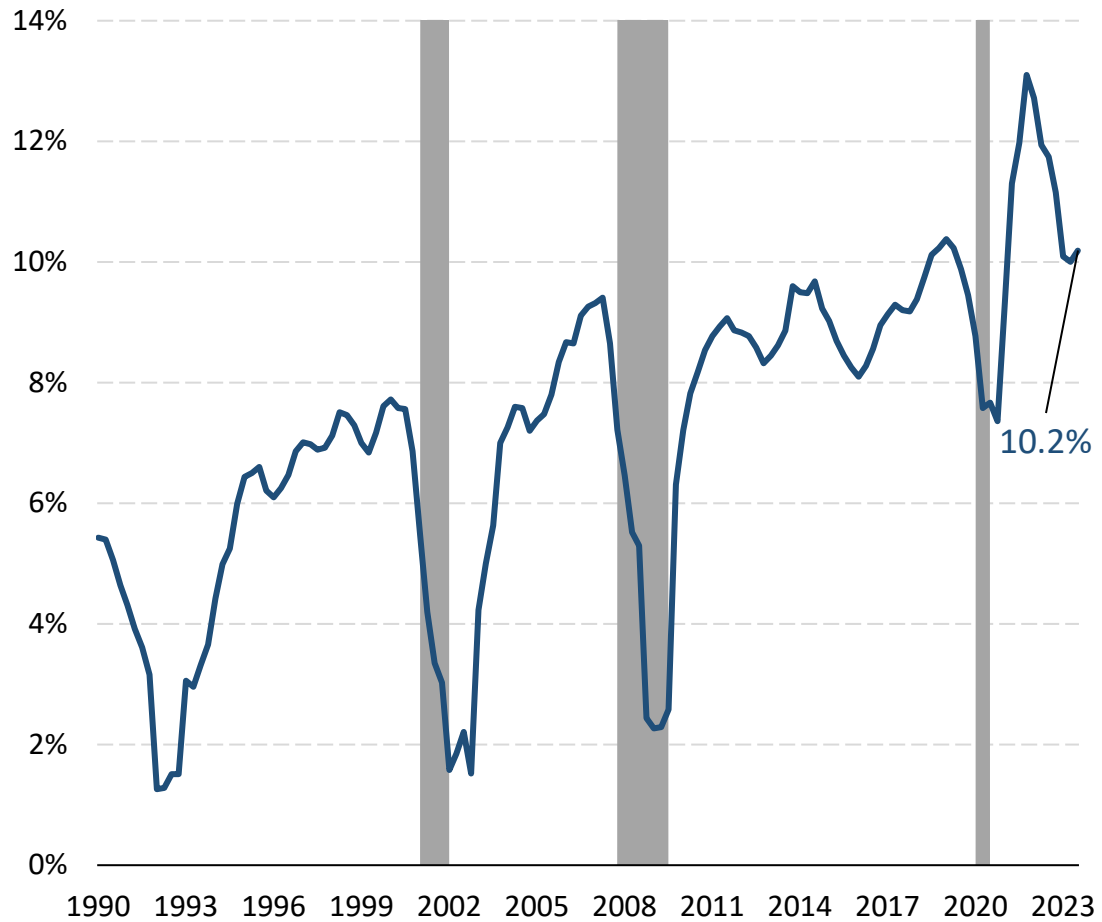
- Just 7 companies account for 29.4% of the S&P 500 market capitalization.
- Last 12 months price-to-earnings ratio of the Magnificent-7 is 43.7x.
- Last 12 months price-to-earnings ratio of S&P 500 ex-Magnificent-7 is 14.9x.

Return from Magnificent Seven Stocks vs. S&P 500

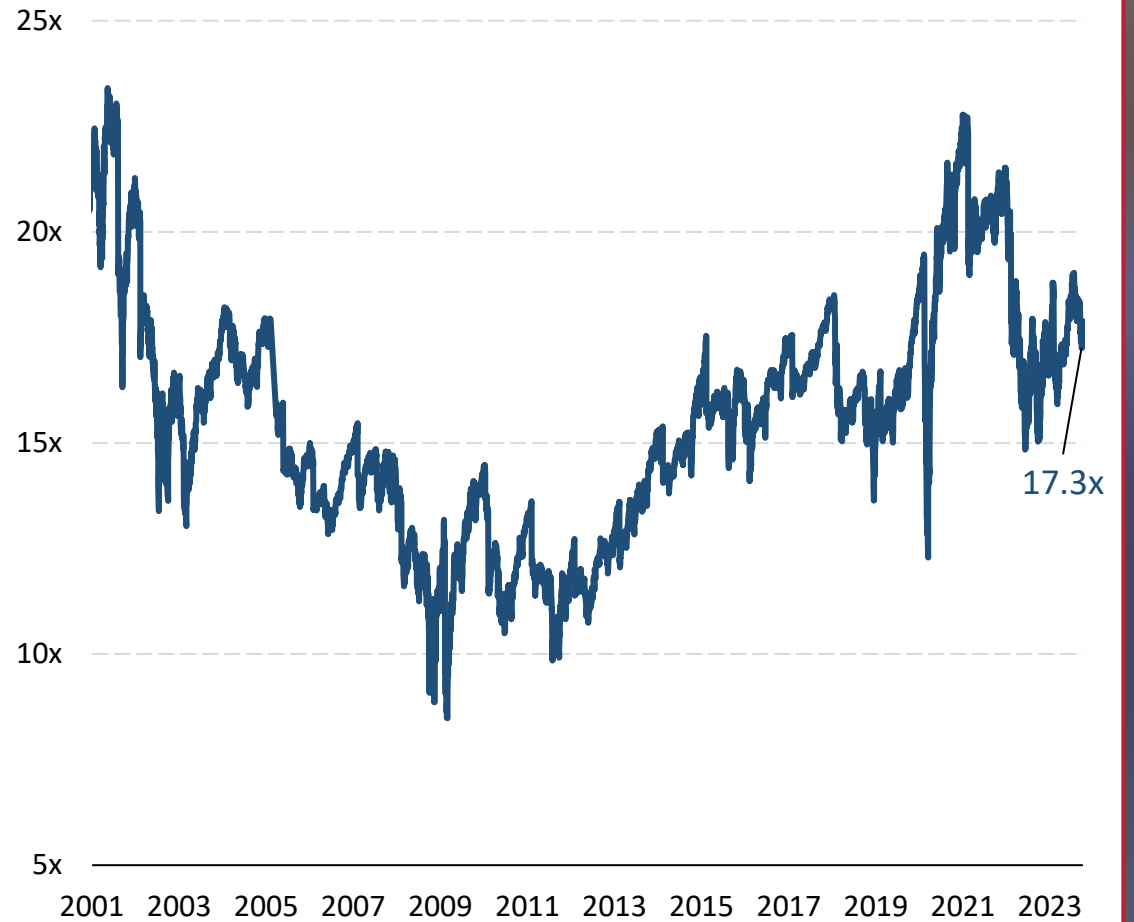


Profit Margins Decline and PE Ratios Rise

S&P 500 Profit Margins (%)



S&P 500 Forward P/E Ratio (x)



Grey Bars Indicate Recession

Source: Bloomberg

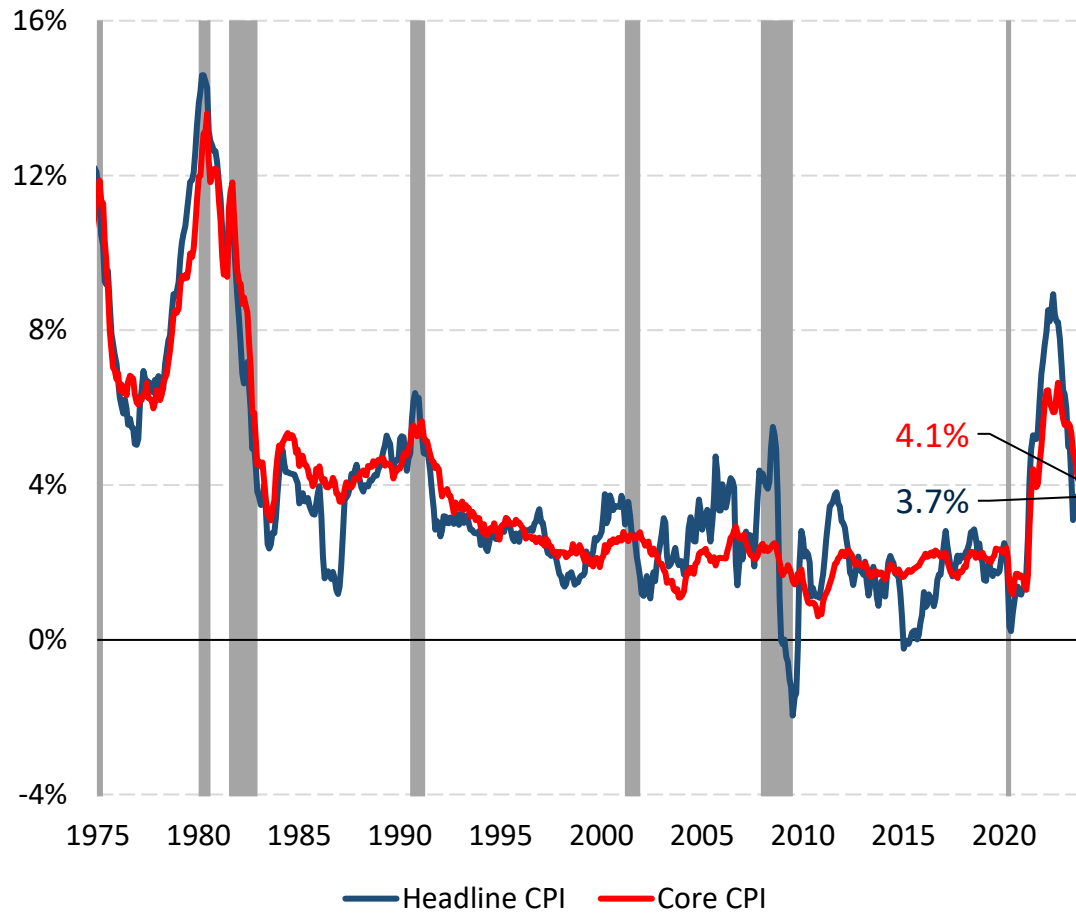
Inflation Has Remained Sticky



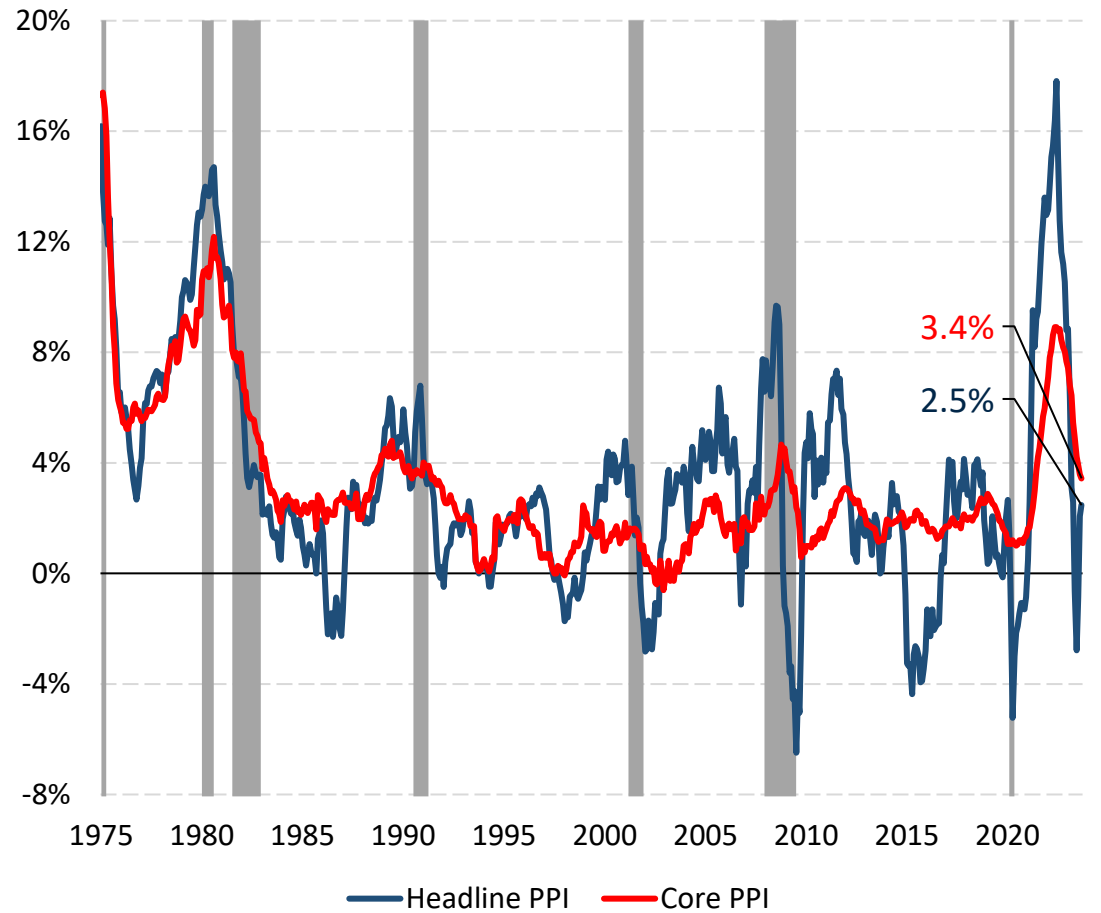
CPI and PPI Remain Well Above the Fed's 2% Target



Headline vs. Core CPI YoY Change (%)



Headline vs. Core PPI YoY Change (%)



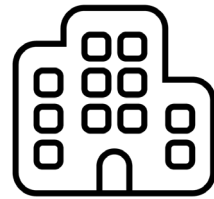
Grey Bars Indicate Recession

Source: Federal Reserve Bank of Atlanta

Refresher on the Stages of Inflation

The Order in Which Inflation Flows Through an Economy

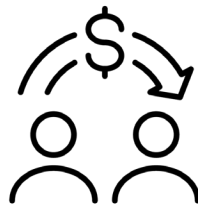
1. Asset Values



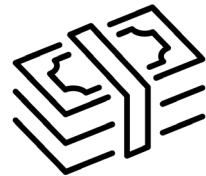
2. Price of Goods



3. Price of Services

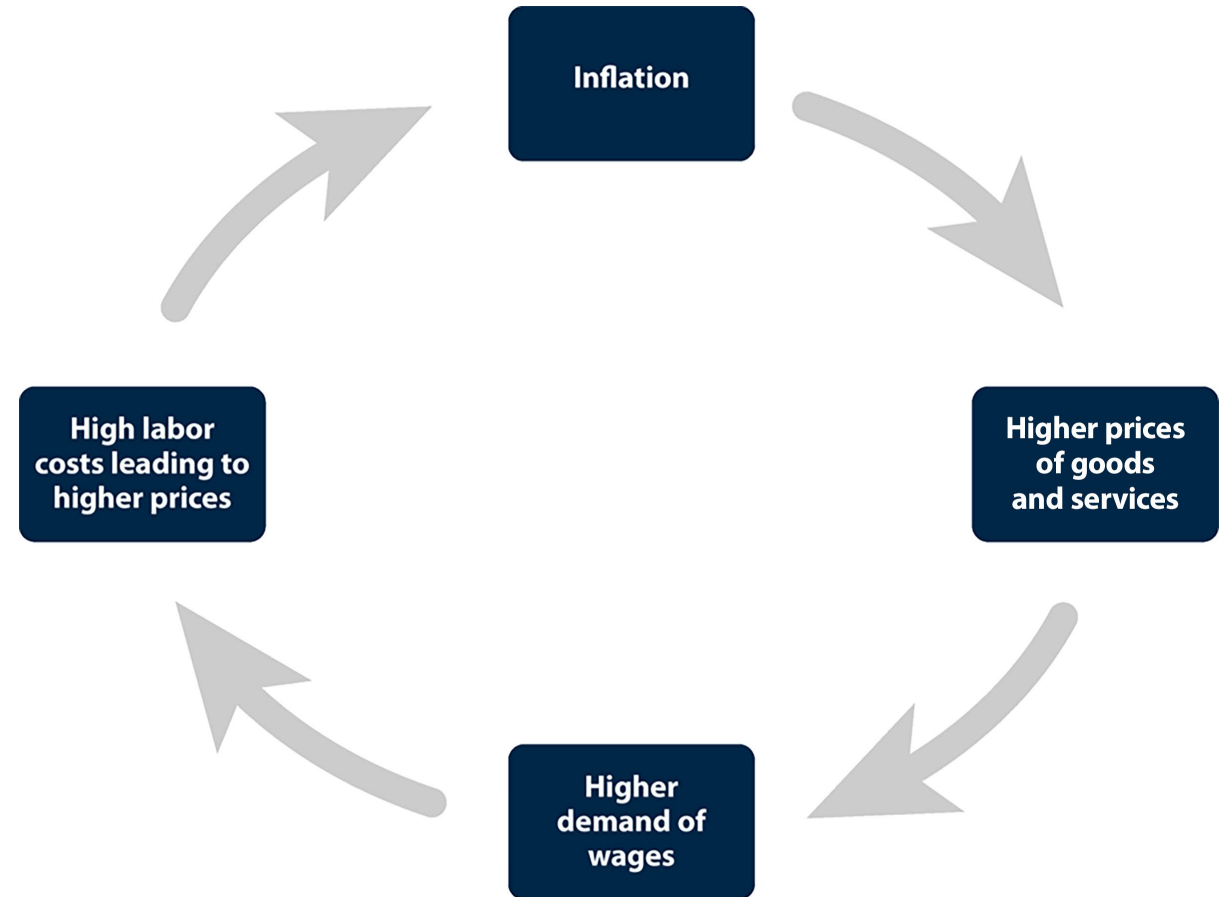


4. Wages



Wage-Price Spiral: Fear of Entrenched Inflation

- Wage inflation becoming entrenched poses the greatest danger to the economy, at which point it could accelerate inflationary pressures of all goods and services.
- Nominal wages have increased 4.5% YoY. However, adjusted for inflation, real wages have only increased 0.8% YoY.
- Consequently, employees will seek even greater compensation increases.



Unions Demand Higher Wages and Benefits



- **UPS Drivers** – Drivers will earn \$170,000 in annual pay and benefits by the end of the 5-year contract.
- **Healthcare Unions** – Unions representing 85,000 workers at Kaiser Permanente came to a tentative agreement which includes a 21% pay increase over the next 4 years.
- **UAW Workers** – The Big Three Automakers have agreed to a 25%-33% pay increase over 4 years, with 11% of that coming in the first year.
- **Major Airline Pilots** – Various deals have been made, including American Airlines' agreement to increase pay by 46% over the next 4 years.
- **Major Airline Flight Attendants** – Flight attendants at Southwest Airlines agreed to a 36% cumulative pay increase over a 5-year contract.
- **Culinary and Bartenders Unions** – MGM, Caesars, and Wynn Resorts workers are demanding the largest increase in the history of the Union.



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An Expert's Wisdom

Inflation is just like alcoholism; In both cases, when you start drinking or when you start printing too much money, the good effects come first, and the bad effects only come later. That's why in both cases there is a strong temptation to overdo it—to drink too much and to print too much money.”

– Milton Friedman

The Fed Has No Choice but to Bust Up the Afterparty

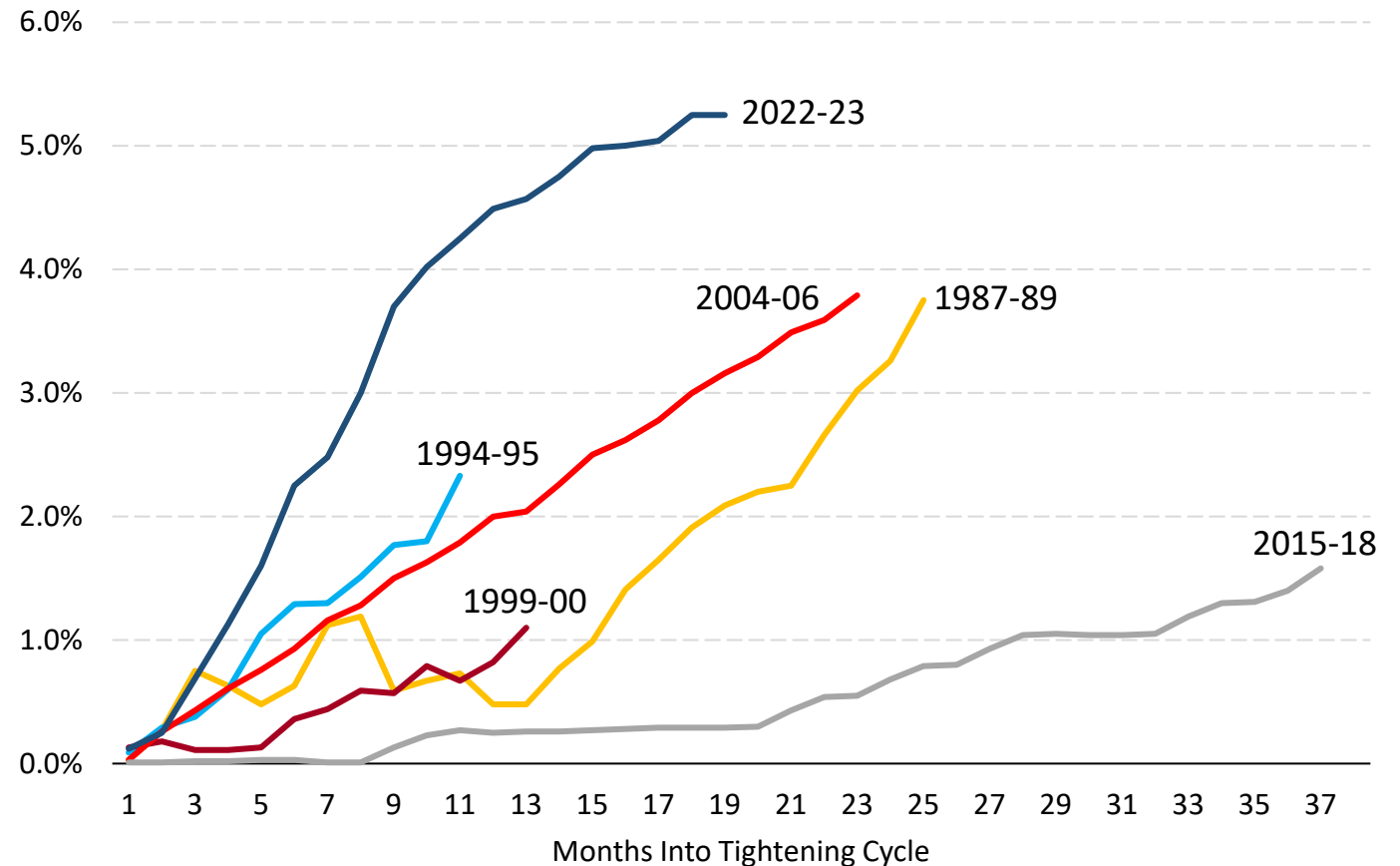
 Sunwest Bank



Fed Funds Rate Has Surged at Historic Pace

- The current effective fed funds rate is 5.3%, rising from 3.8% a year ago and 0.1% when the fed began raising rates in March 2022.
- The 10-year Treasury rate rose from 2.2% when rate hikes began to 4.7% today.
- Movements in interest rates generally have a lagging effect of at least 12 to 18 months before their full impact is felt. The first rate move was 19 months ago.

Fed Funds Rate Hike Cycles Since 1987 (%)



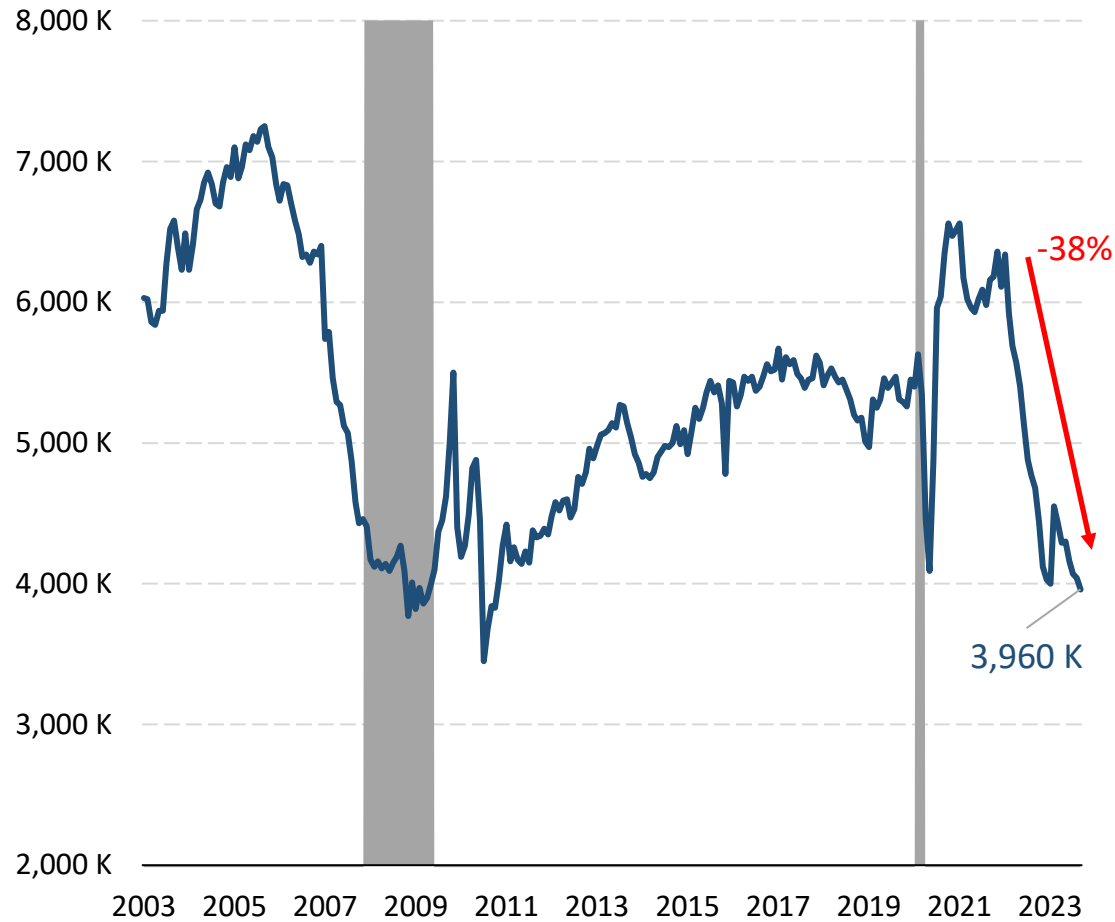
The Housing Anomaly



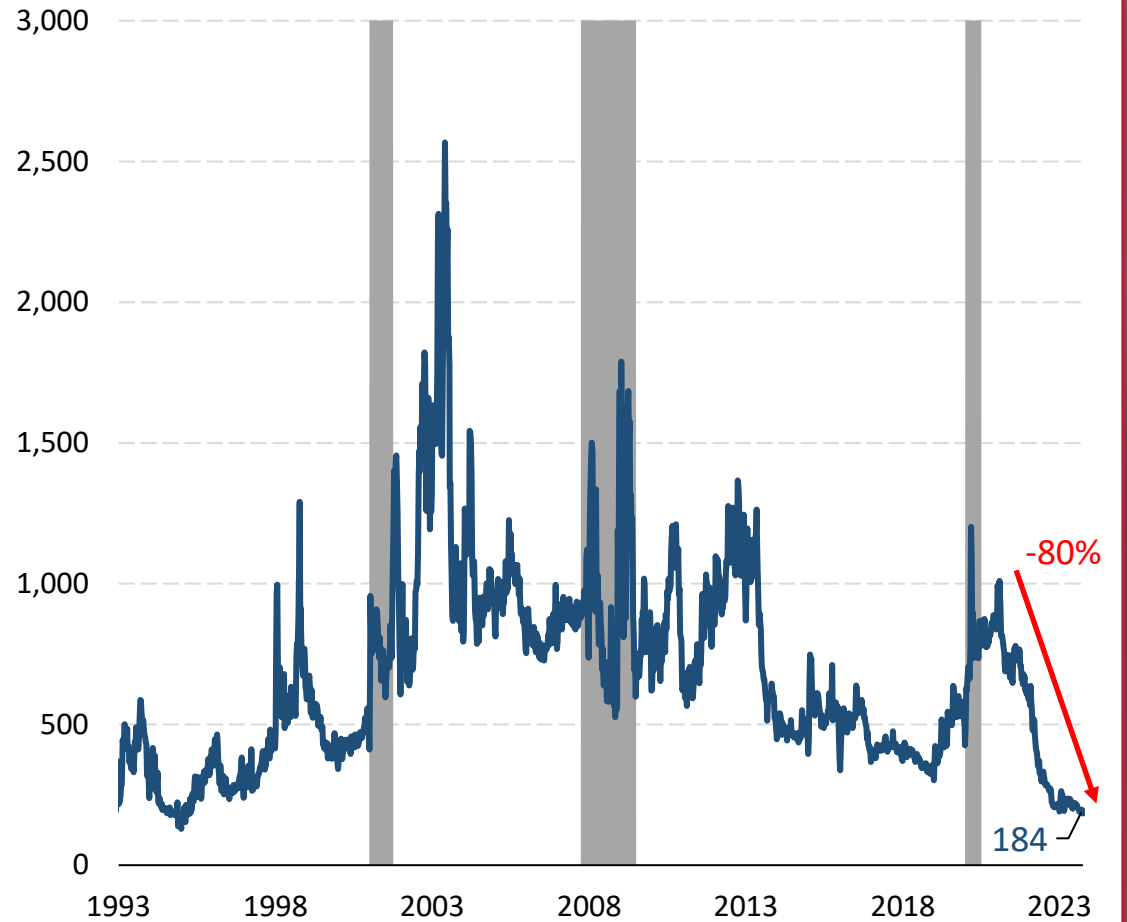
Rates Have Crushed Housing Activity



U.S. Existing Home Sales (in thousands)



Mortgage Application Index

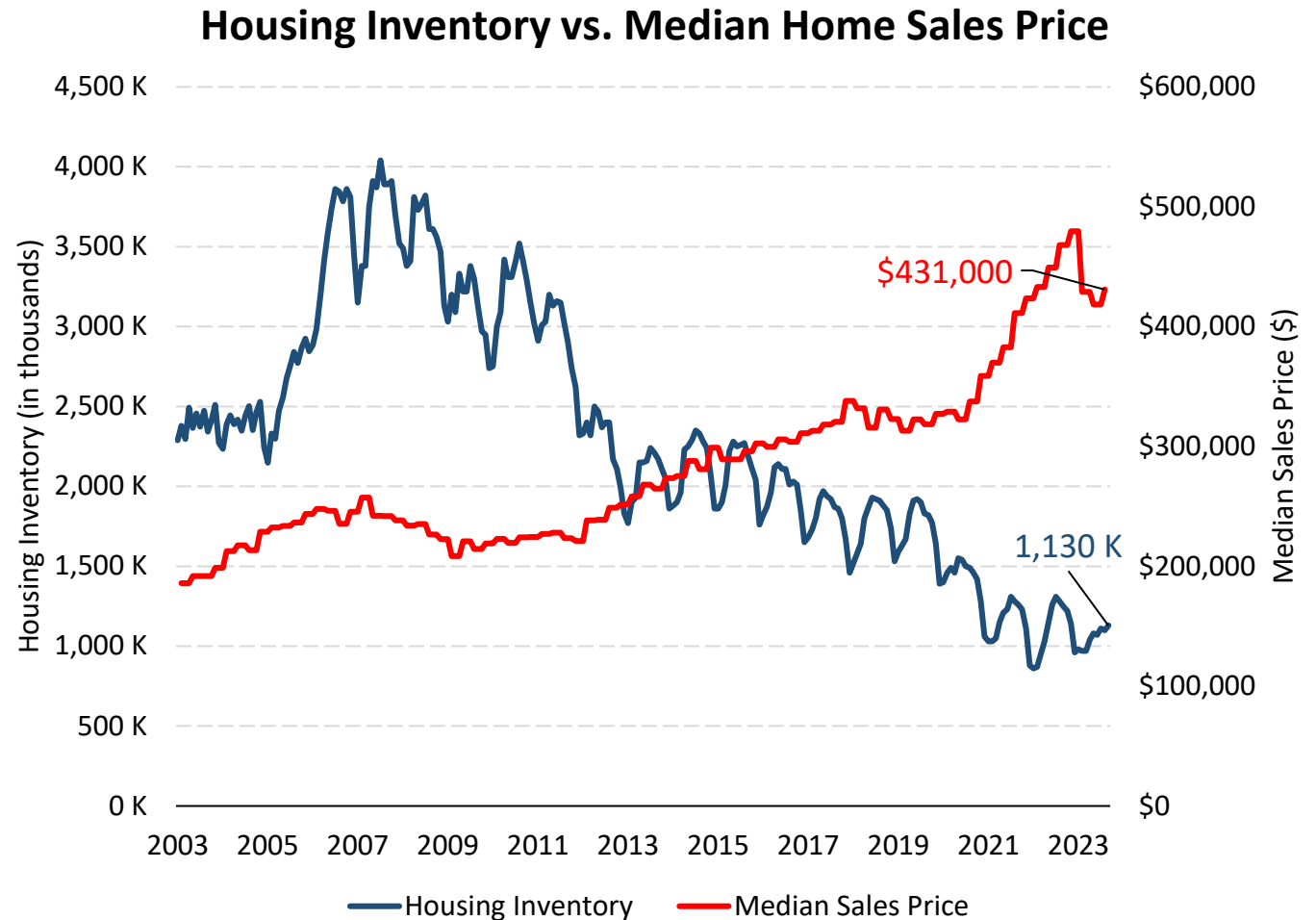


Grey Bars Indicate Recession

Source: National Association of Realtors, Bloomberg

Historically Low Inventory Has Supported Prices

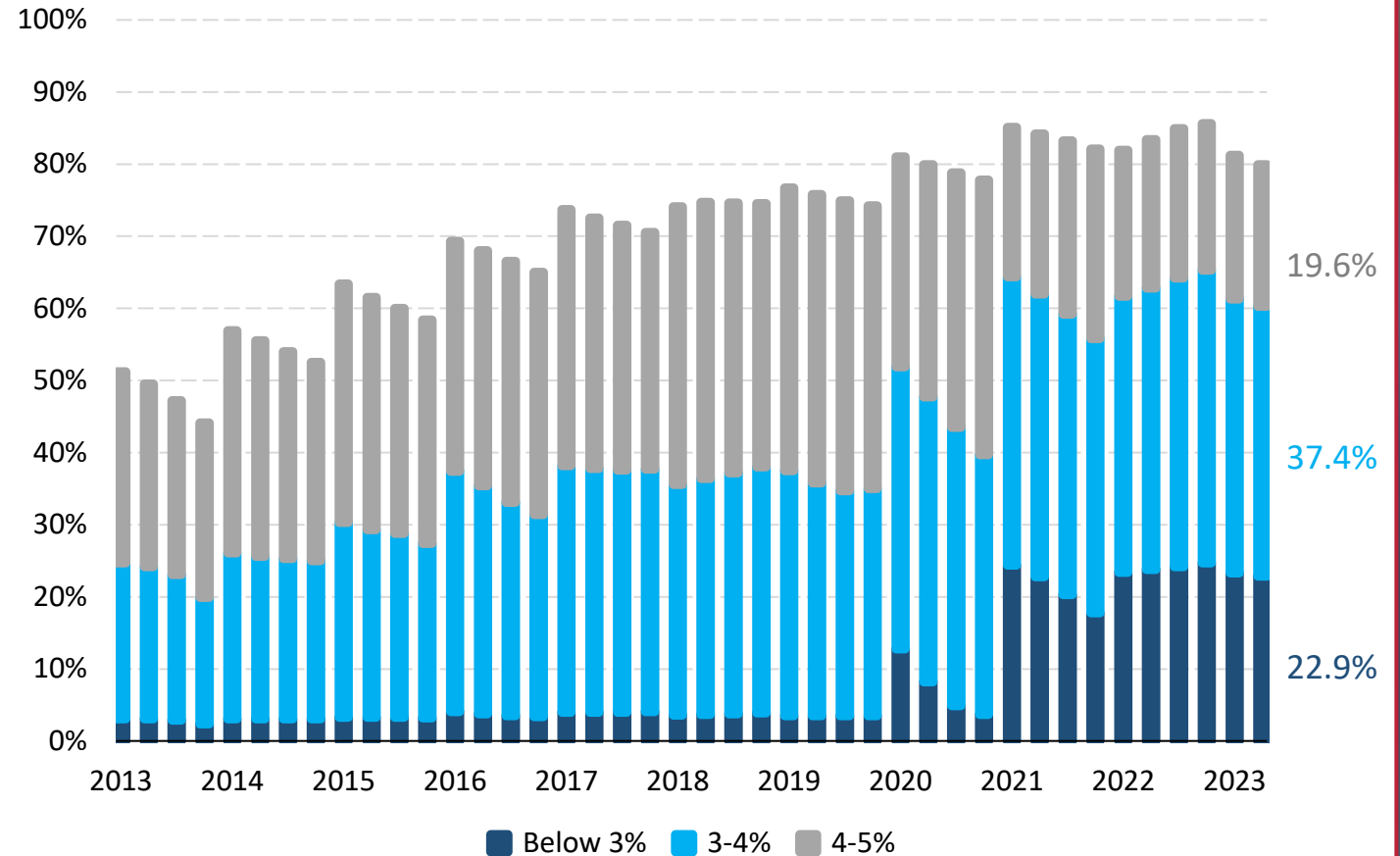
- Median Sales Price peaked at \$480K and fell to \$419K before rising to \$431K for Q3.
- Due to rising rates and extremely low inventory, there has been a 31% YoY decline in overall home sales.
- Investors were a major buyer of homes over the last decade and now own 16% of all homes. Today, investors are buying 45% less homes than this time last year.



Most Homeowners Now Locked Into Low Rates

- Roughly 14M homeowners refinanced their mortgage between 2020 and 2021 with rates as low as 2.65%.
- 60% of homeowners now have a mortgage rate below 4%, and 80% have one below 5%.
- In 2022, a buyer with a \$1,500 monthly budget could afford a \$416K home with a 3.5% mortgage rate and 20% down; however, today with an 8.0% mortgage rate, they could only afford a \$256K home, representing a **38% decline**.

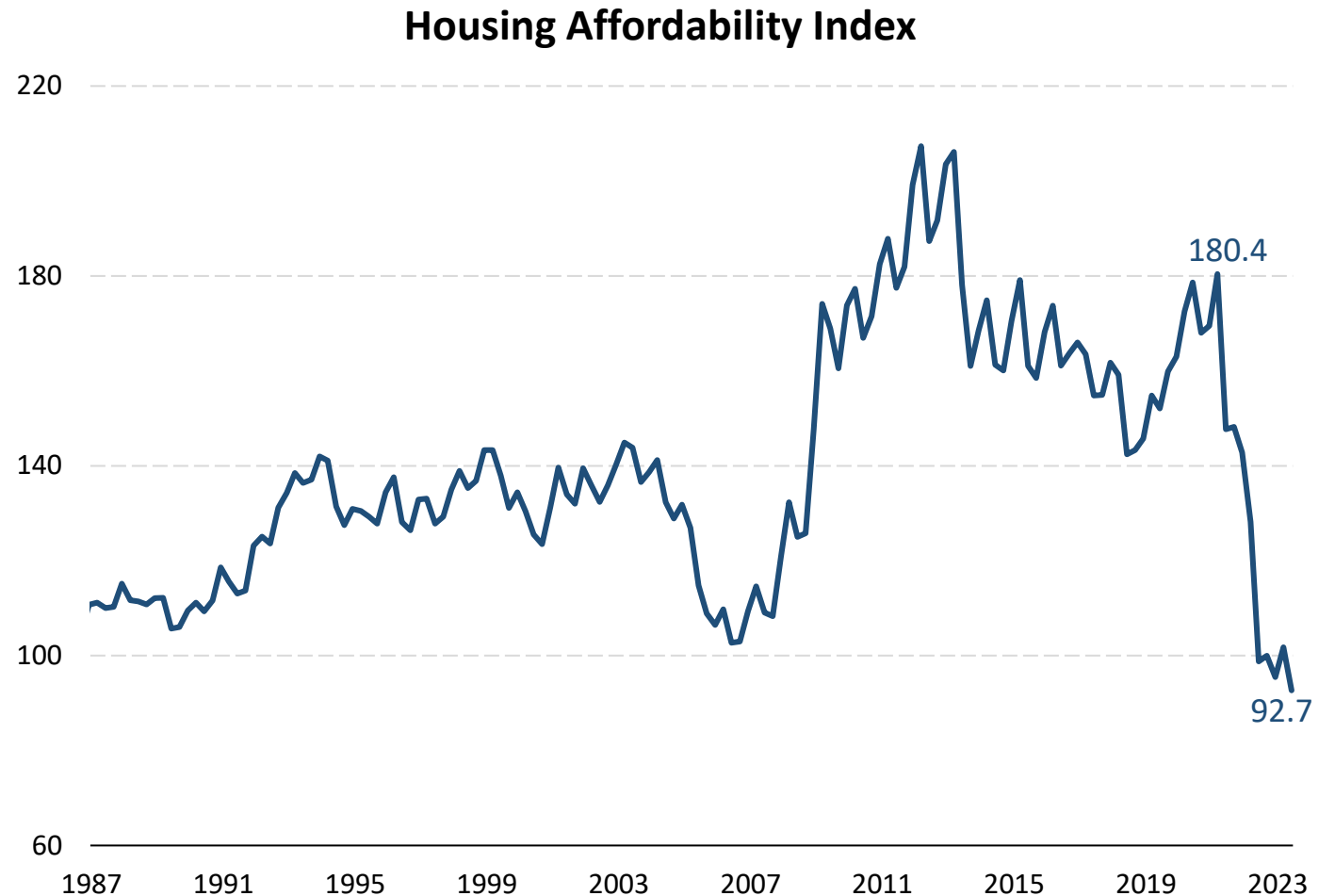
Portion of Mortgage Loans Below 5% (%)



What Did Rates Do to Housing Affordability? Cratered It



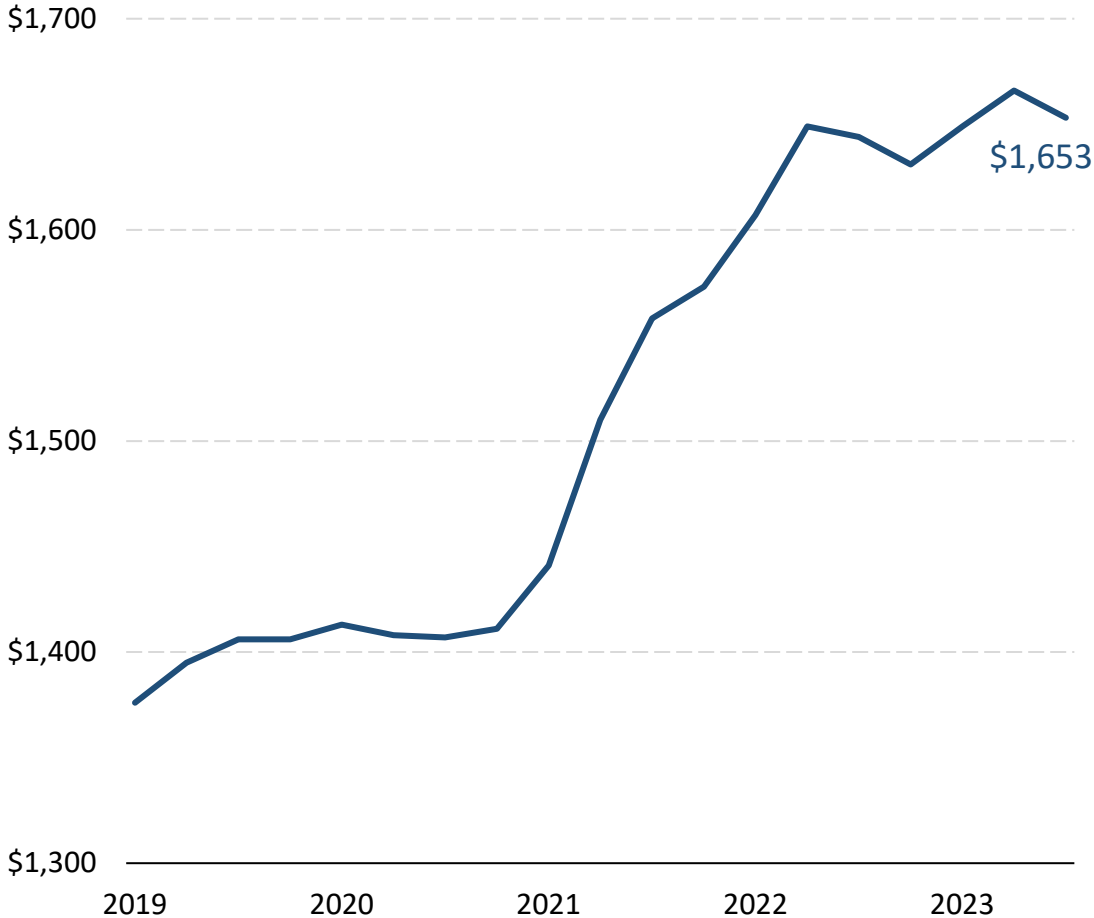
- Housing affordability has collapsed with the index now at 92.7, the lowest level since 1985.
- This will continue to weigh on the housing market and related industries. Moreover, it will have significant social consequences, making it more difficult for: 1) family formation and 2) long-term financial stability.
- The housing affordability index represents median family income divided by qualifying income for a conventional loan.



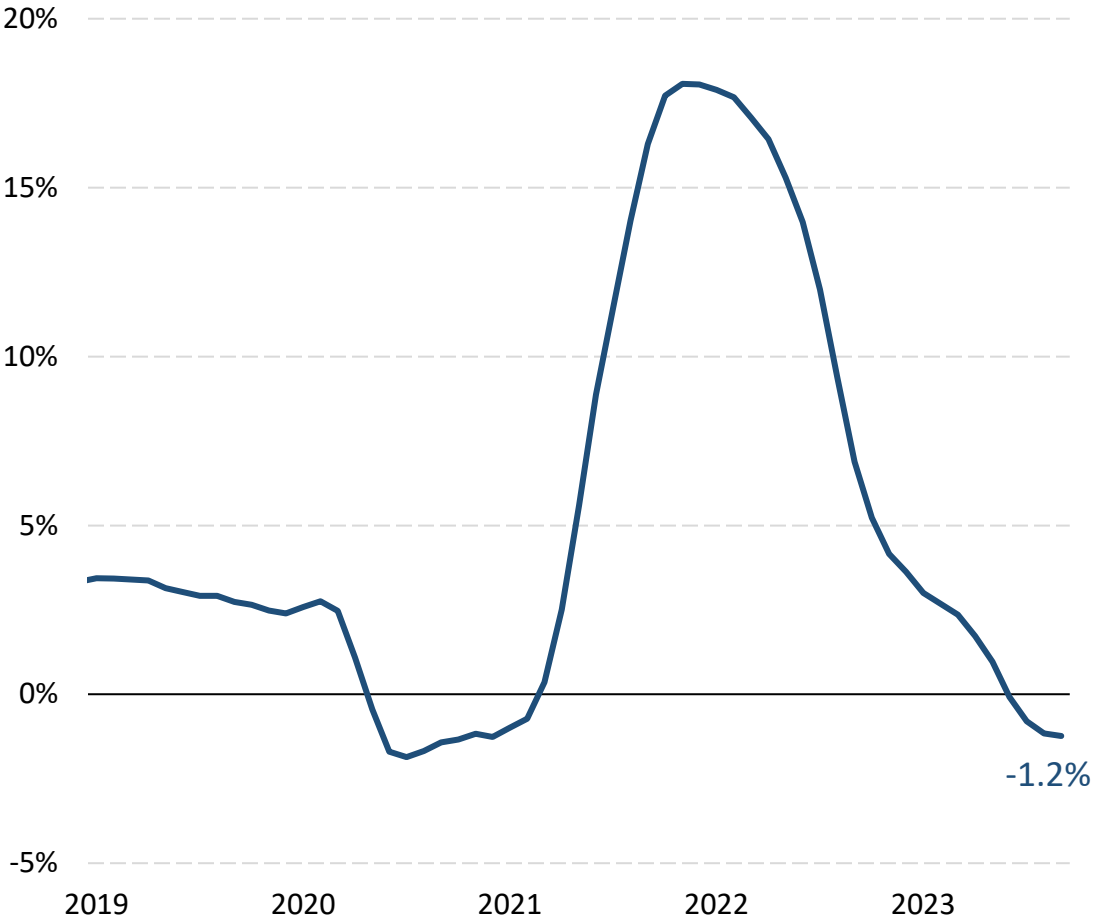
Source: Bloomberg

Multi-family Rents Have Started to Cool

Average Monthly Rent



Apartment List Rent YoY Change (%)



Source: Apartment List

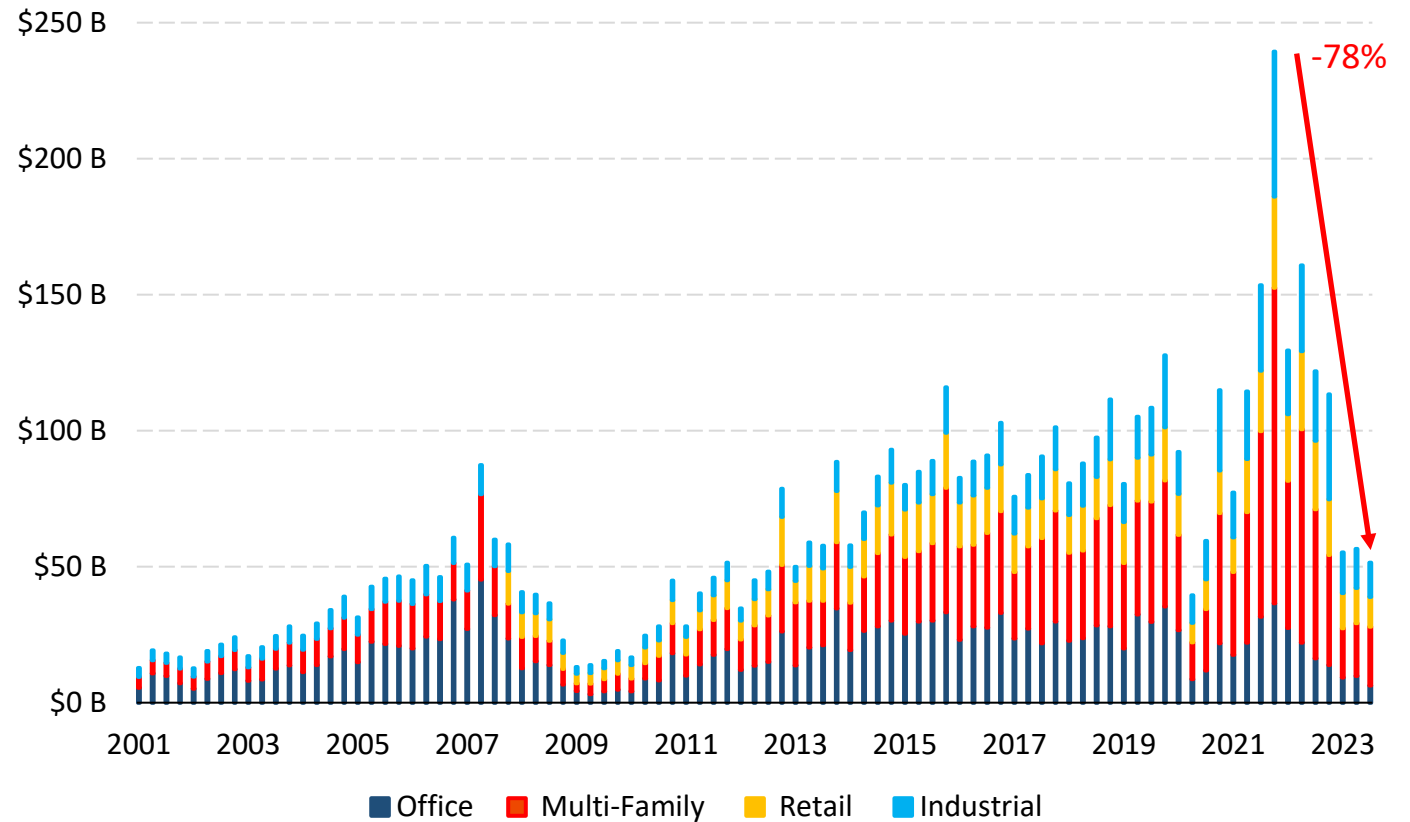
Commercial Real Estate – The Great Re-margin



CRE Transaction Volumes Plummeted

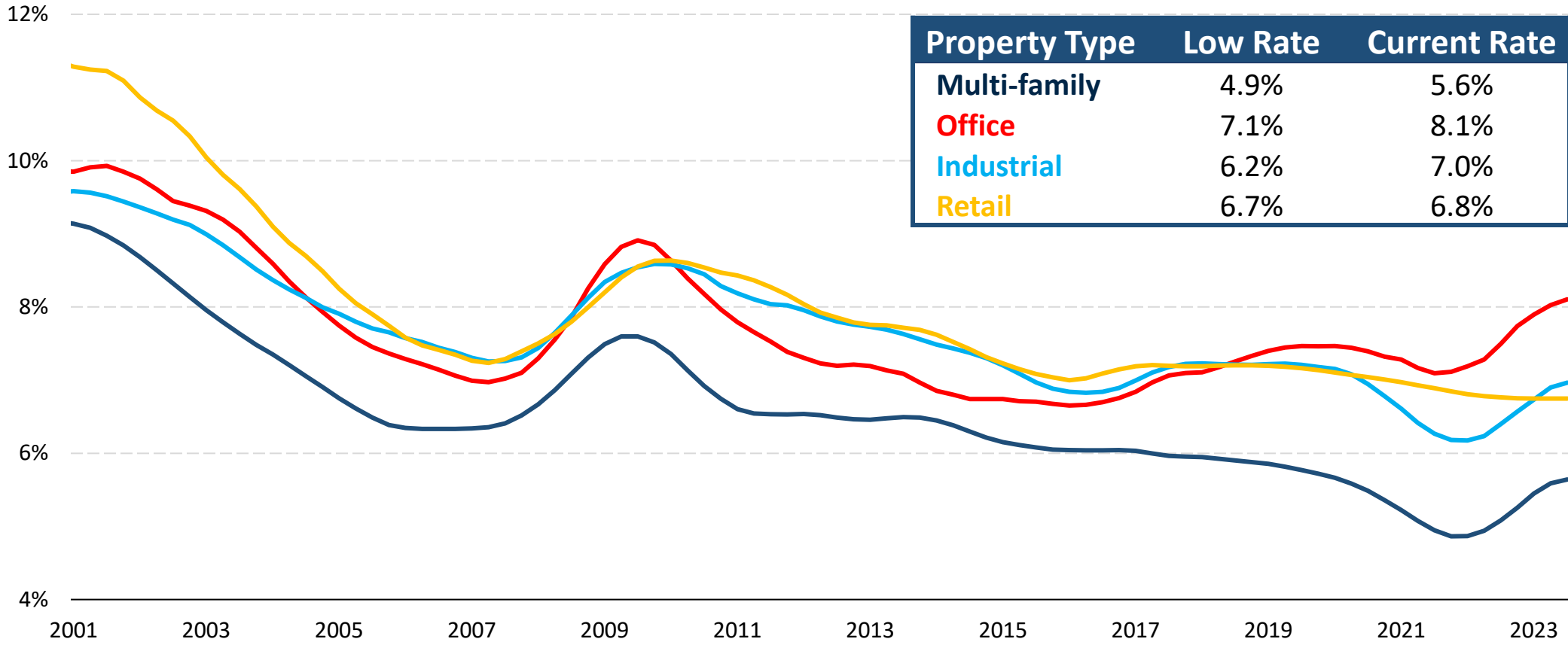
- After peaking at \$239B in Q4 2021, total commercial real estate transaction values have fallen to just \$52B in Q3 2023.
- Transaction values of Office CRE totaled only \$6B in Q3 2023, the lowest since the GFC, driven by multiple factors, including work-from-home and collapsing CRE values in many urban hubs.
- Distressed transactions will become more prominent in the next 2 years as lenders have to repossess properties and sell them to opportunistic buyers.

**Total Quarterly Commercial Real Estate Transaction Values
(in \$ billions)**



CRE Cap Rates March Higher – How Much Higher?

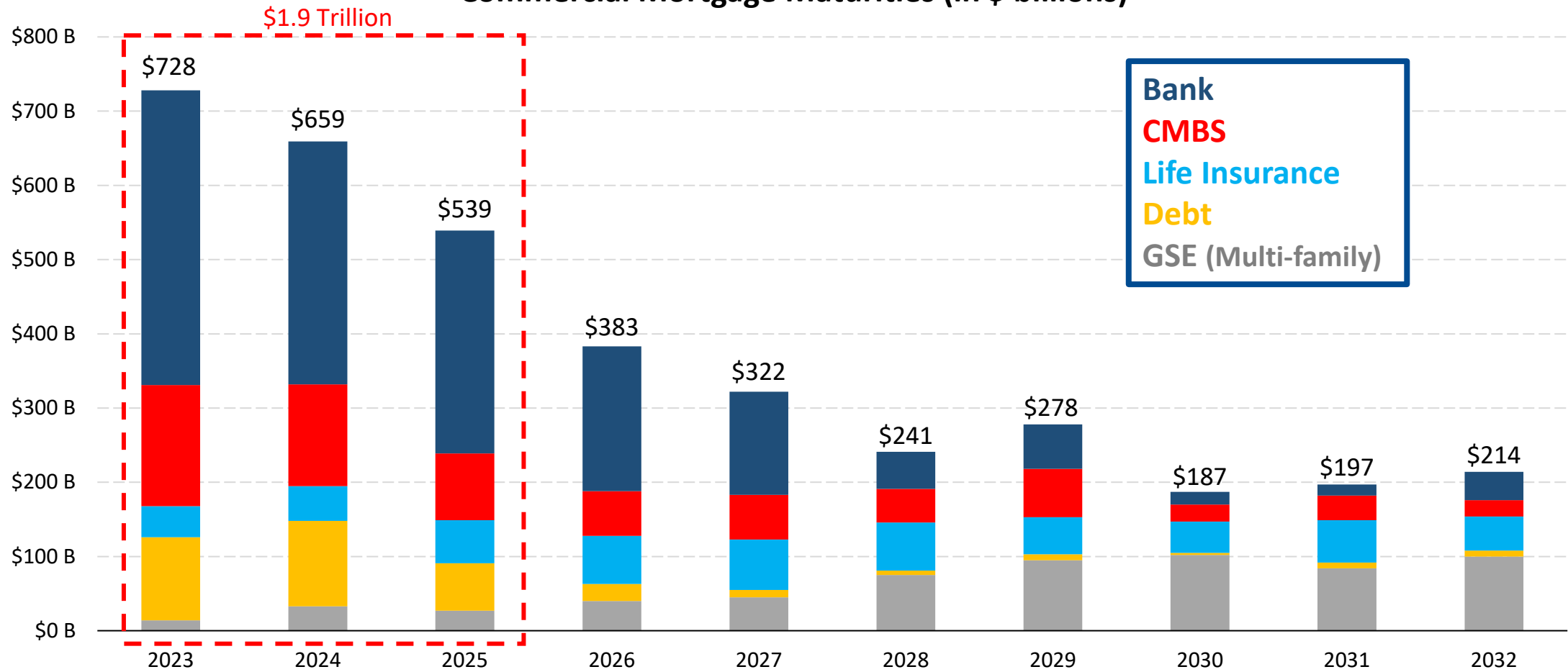
Cap Rates by Property Type (%)



Source: CoStar

Wave of Commercial Maturities Approaching

Commercial Mortgage Maturities (in \$ billions)



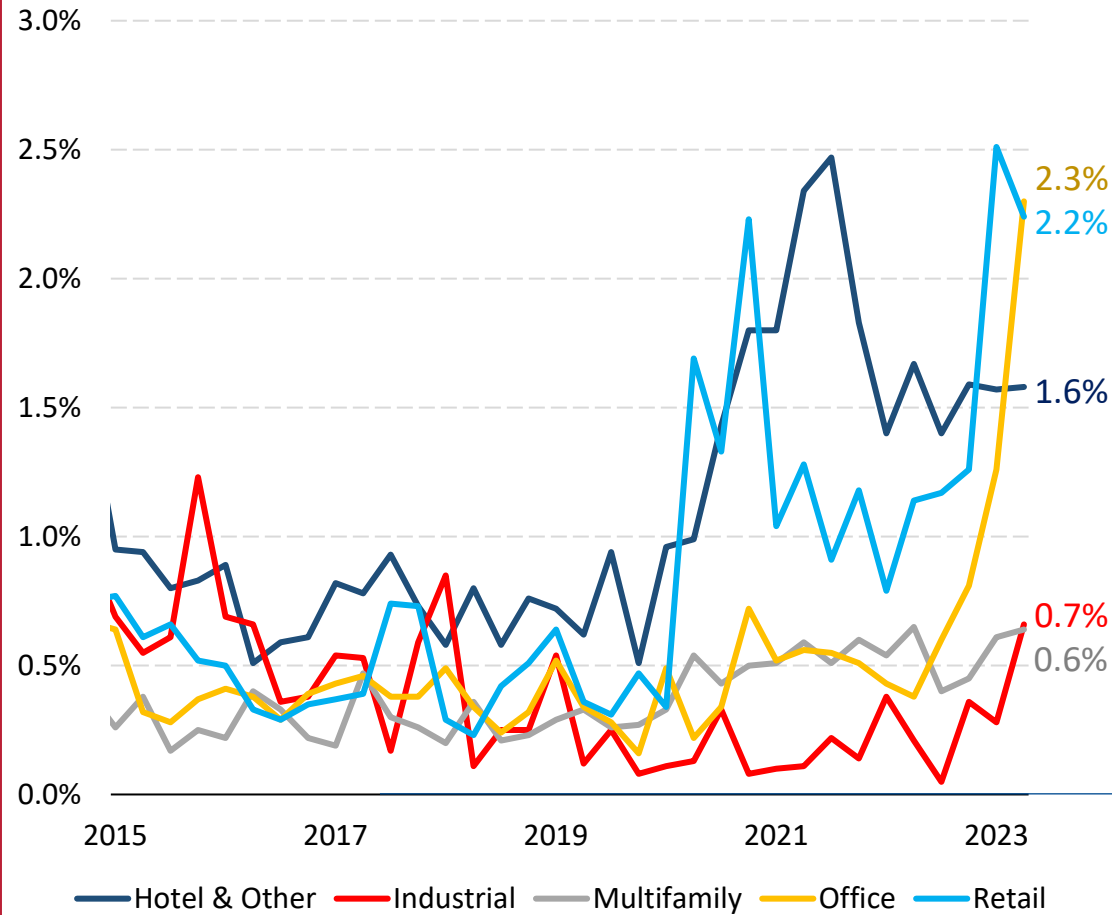
Source: MBA, Newmark Research

The Problem: Re-Margining CRE Loans

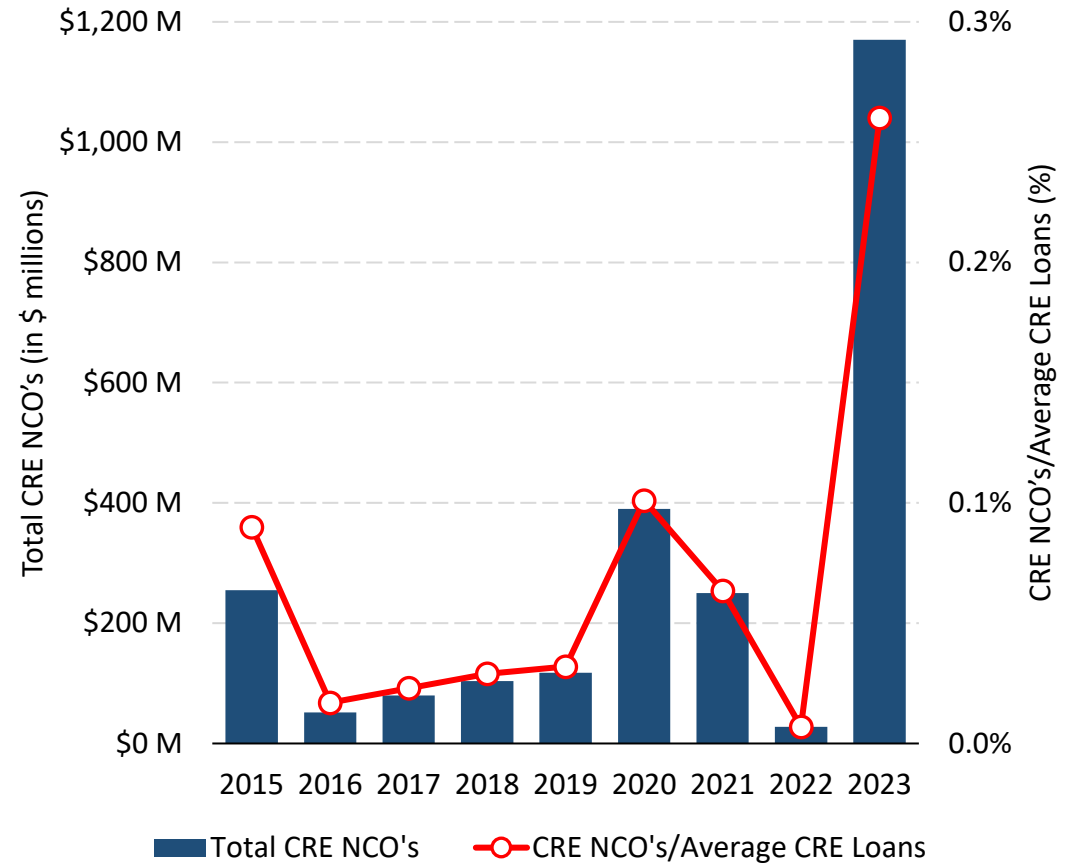
	Loan Amount	Rate	NOI/CF	Interest Payment	CF after Interest	DSC
Original Loan	\$10,000,000	4.00%	\$600,000	\$400,000	\$200,000	1.50x
Original Loan at Current Rates	\$10,000,000	8.00%	\$600,000	\$800,000	-\$200,000	0.75x
New Loan at Current Rates	\$6,000,000	8.00%	\$600,000	\$480,000	\$120,000	1.25x
Financing Gap:	-\$4,000,000					

CRE Net Charge-Off's Accelerating

Delinquency Rates at U.S. Banks (%)



CRE Net-Charge Offs at U.S. Banks (As of second calendar quarter each year)

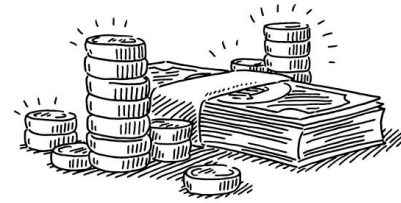


Source: Trepp, S&P Global Market Intelligence

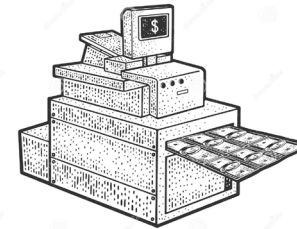
No Landing... Soft Landing... Hard Landing...



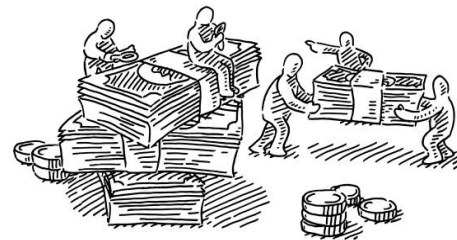
The Cost of Money



The Supply of Money



Credit Creation



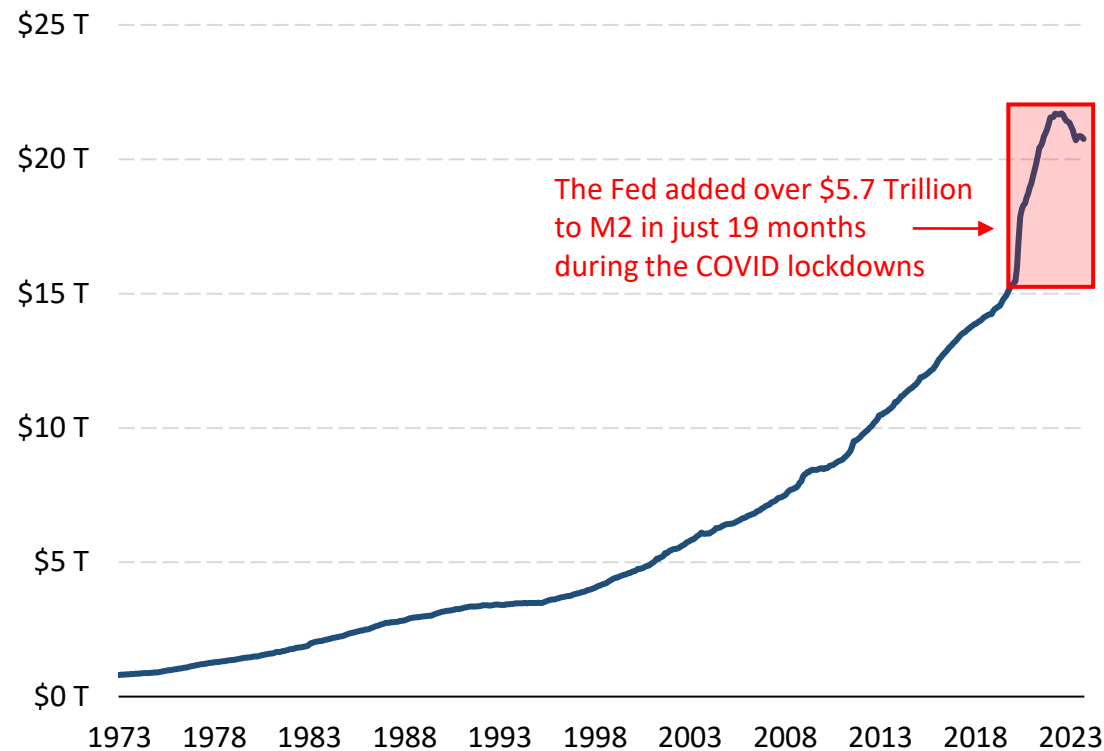
The Fed Dramatically Raised the Cost of Money

Duration	Rate as of Nov. 1, 2021	Rate as of Nov. 1, 2022	Rate as of Nov. 1, 2023
Federal Funds Rate	0.07%	+301bps → 3.08%	+225bps → 5.33%
2-Year Treasury	0.50%	+391bps → 4.41%	+54bps → 4.95%
5-Year Treasury	1.19%	+299bps → 4.18%	+48bps → 4.66%
7-Year Treasury	1.46%	+264bps → 4.10%	+64bps → 4.74%
10-Year Treasury	1.56%	+245bps → 4.01%	+73bps → 4.74%
30-Year Fixed Mortgage	3.09%	+386bps → 6.95%	+74bps → 7.69%

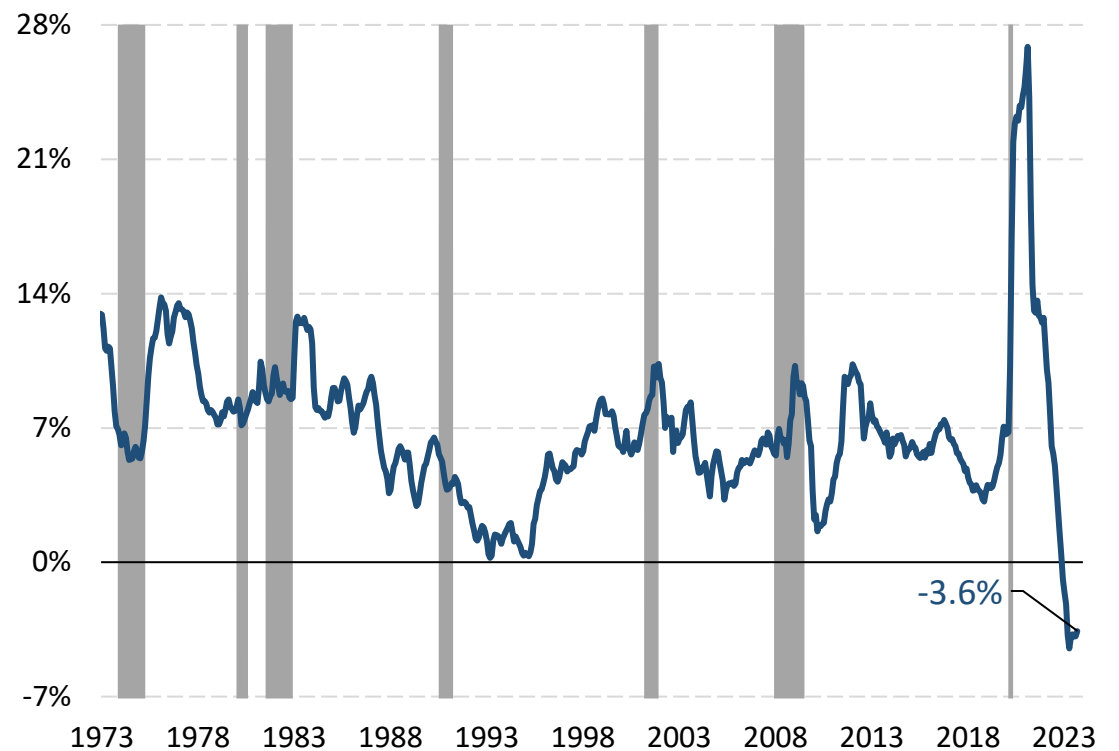
While Shrinking the Supply of Money

- The Fed increased the money supply by 39% during the COVID lockdowns, the highest in our country's history. Money supply is now contracting.

M2 Money Supply (in \$ trillions)



M2 Money Supply YoY Change (%)



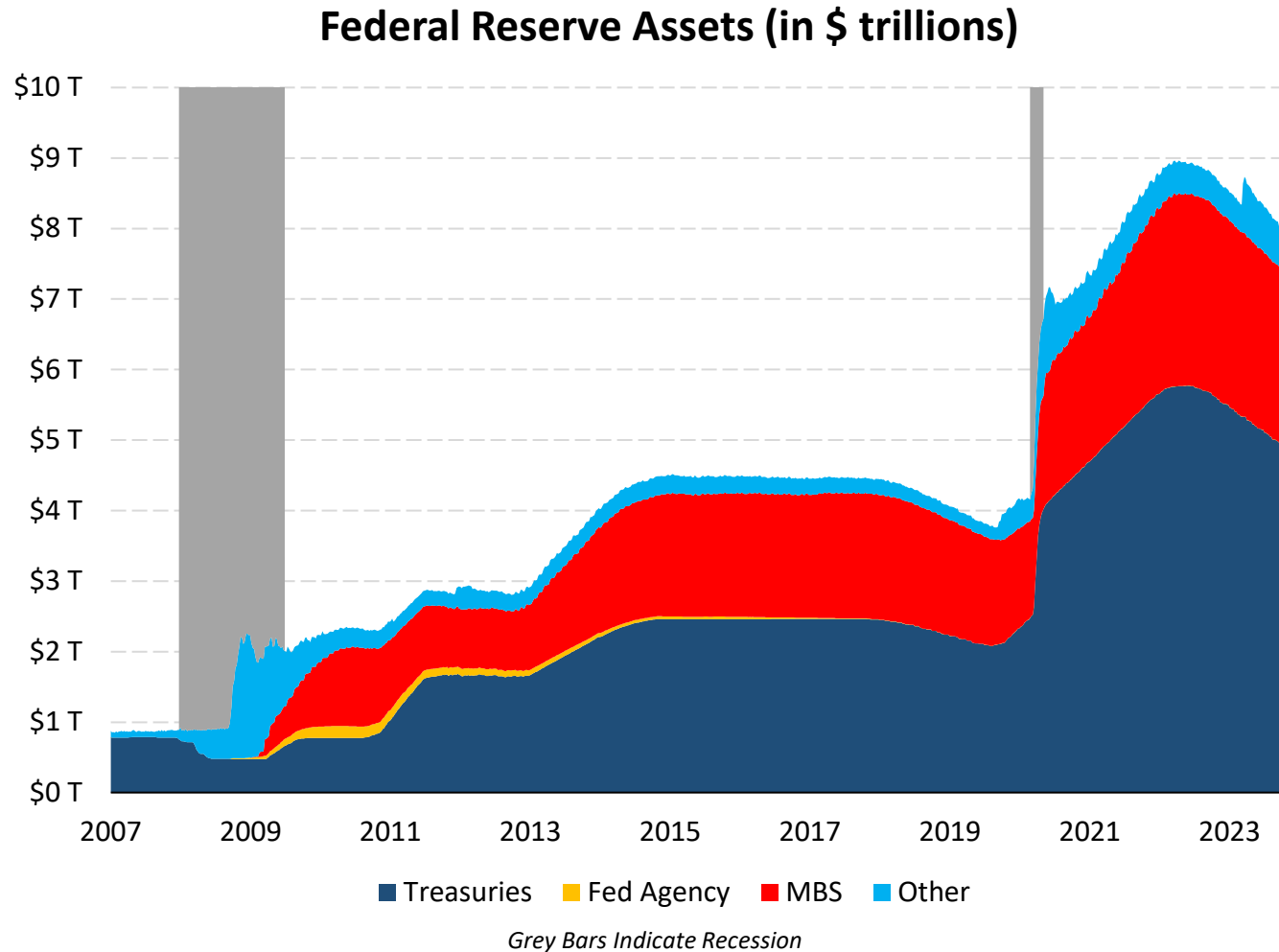
Grey Bars Indicate Recession

Source: St. Louis Federal Reserve

And Is Continuing to Drain Liquidity From the Economy



- The Fed injected over \$5.0T of liquidity since the beginning of the pandemic, peaking at \$9.0T in March 2022.
- The Fed turned from QE to QT in March 2022 and has drained \$1.0T from the economy since, as securities matured without being replaced.
- But the Fed still holds \$7.9T on its balance sheet: \$4.9T in Treasury securities and \$2.5T in mortgage-backed securities.

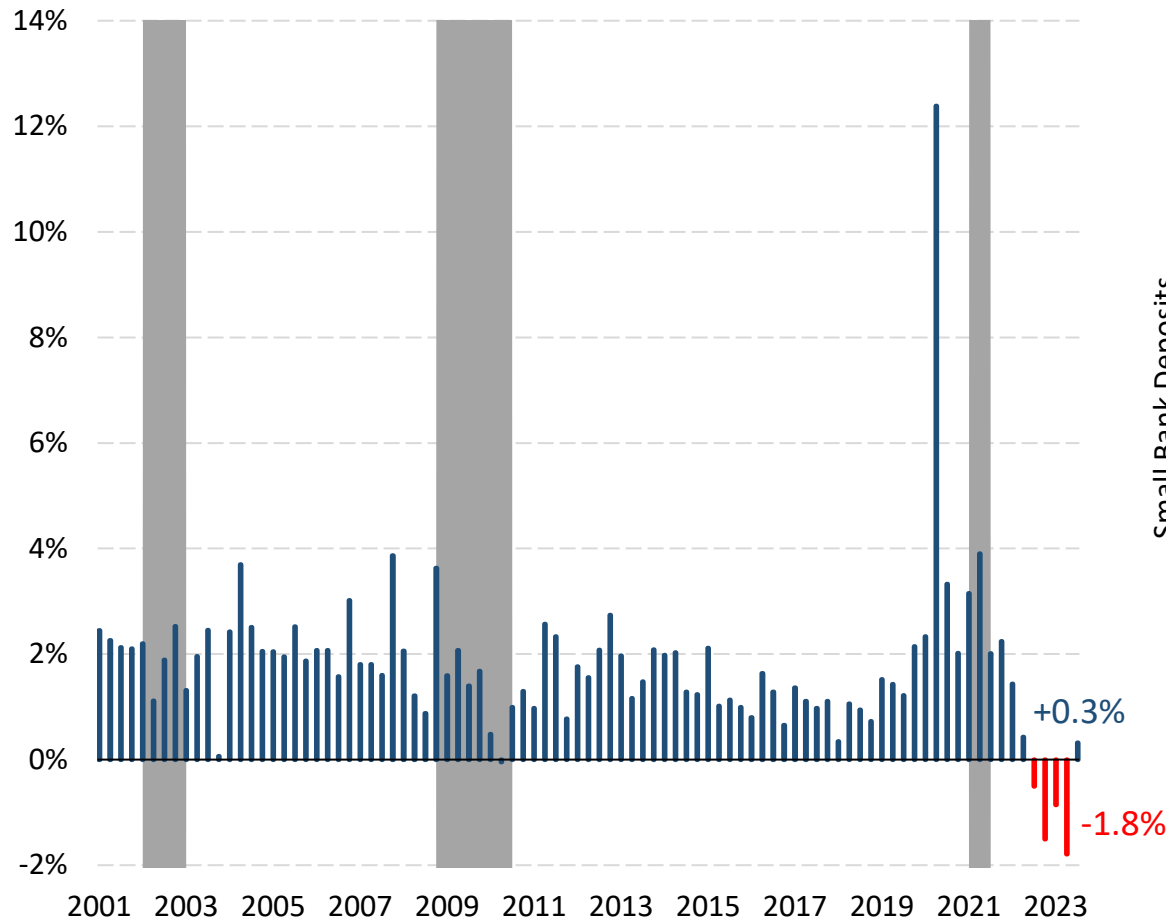


Source: St. Louis Federal Reserve

Core of Credit Creation – Bank Deposits Are Declining

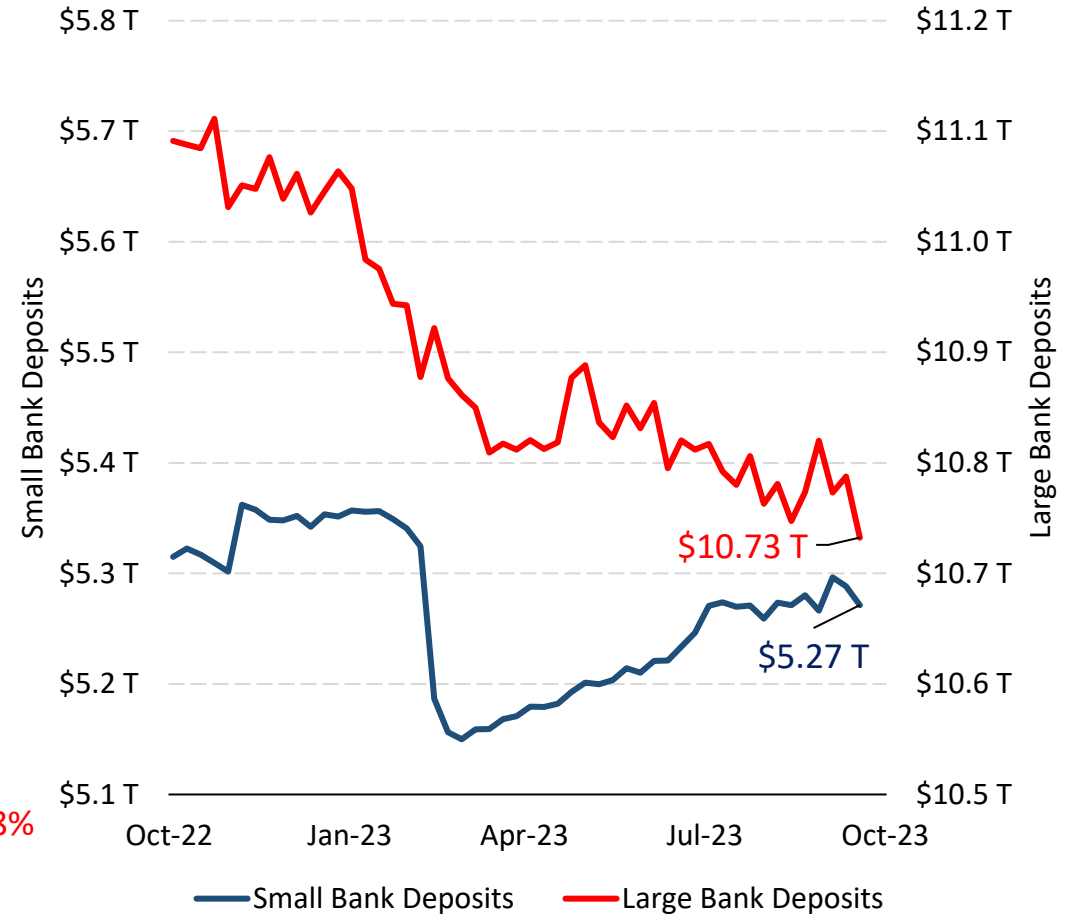


Commercial Bank Deposits QoQ Change (%)



Grey Bars Indicate Recession

Small vs. Large Bank Deposits (in \$ trillions)

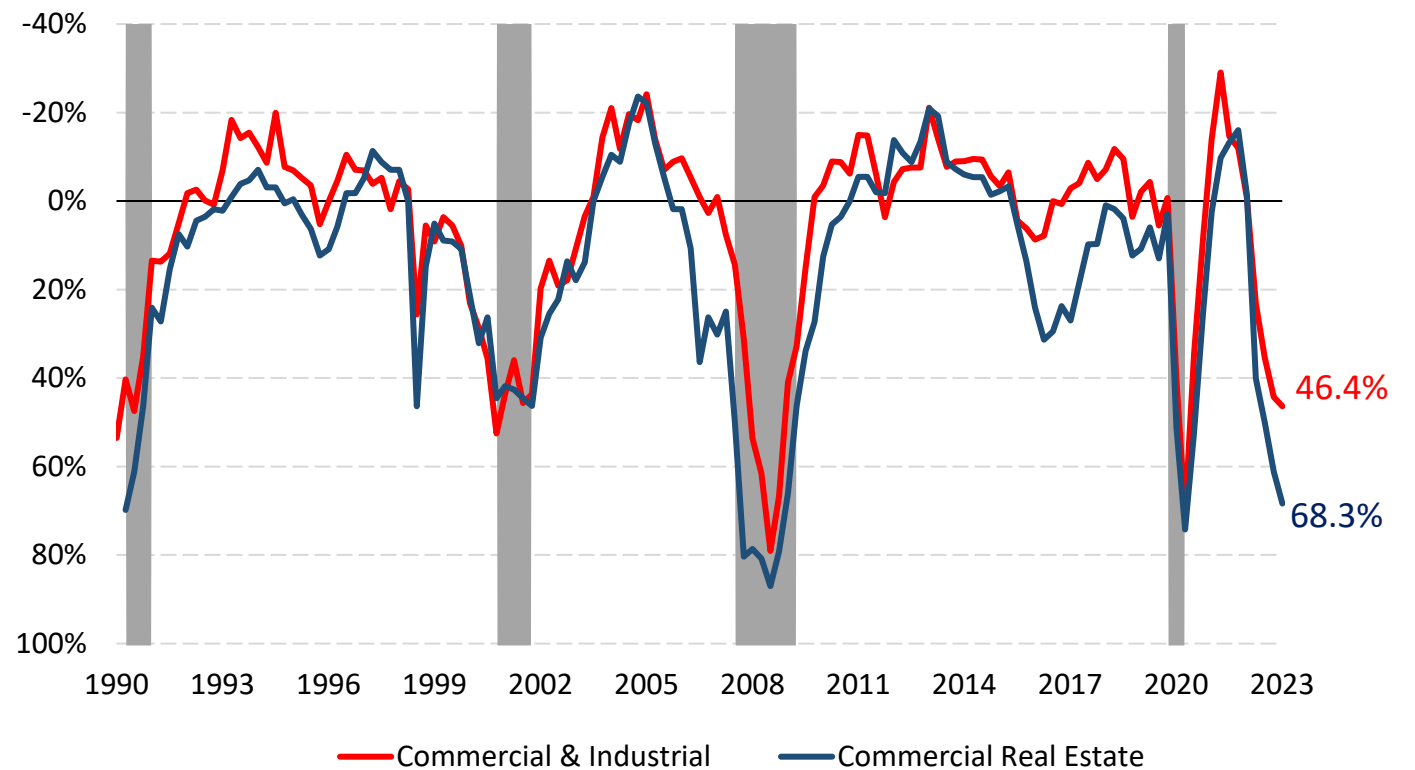


Source: St. Louis Federal Reserve

Banks Continue Tightening the Credit Box

- As of Q2 2023, 46.4% of banks are tightening standards for commercial & industrial loans.
- As of Q2 2023, 68.3% of banks are tightening standards for commercial real estate loans.
- Only during the GFC and temporarily during the COVID lockdowns have banks contracted lending by a greater pace.

Net Percentage of Domestic Respondents Tightening Credit Standards (%)



Grey Bars Indicate Recession

Source: St. Louis Federal Reserve, Author's Calculations

Troubling Trends



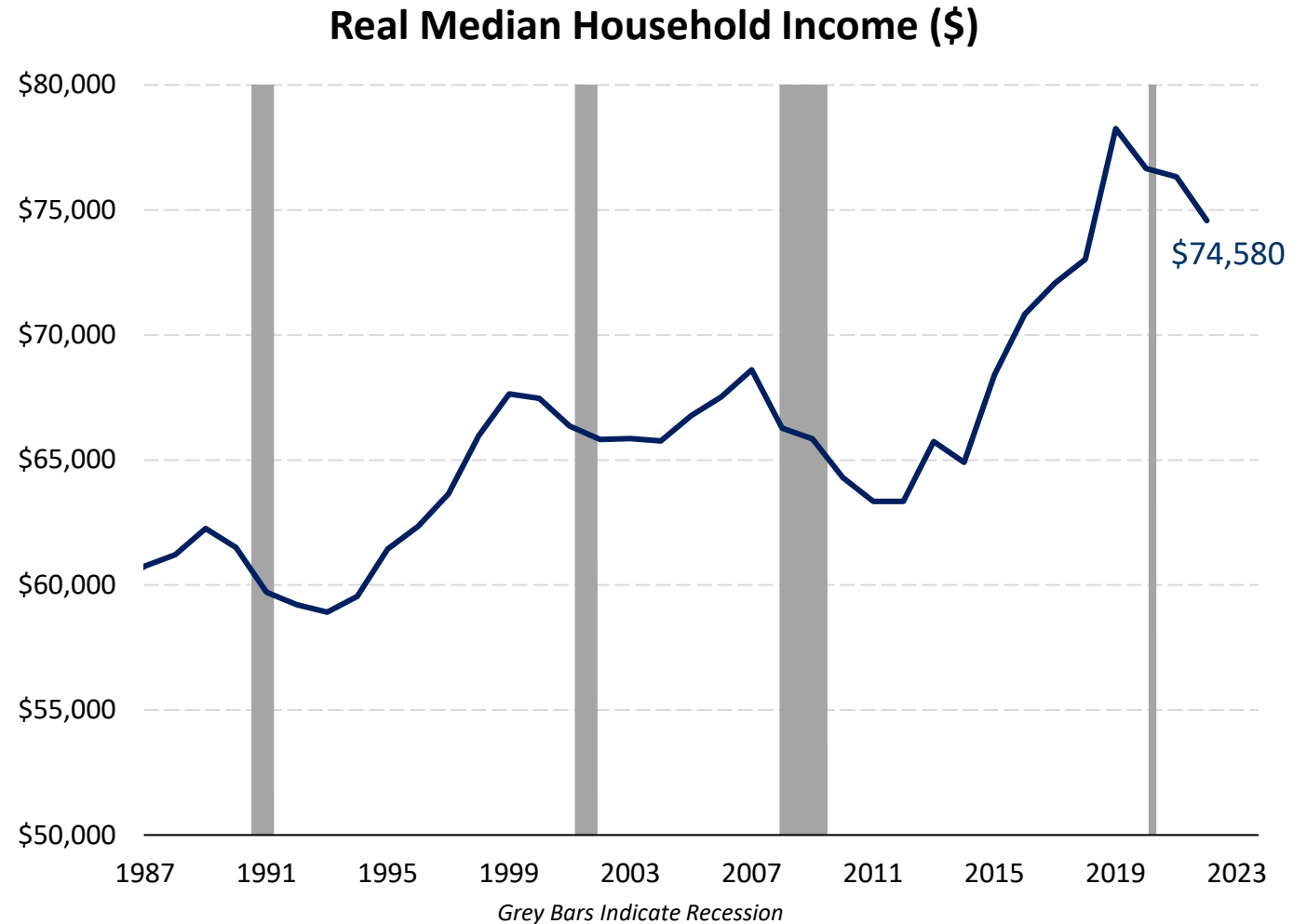
Bond Market Bears Hold Firm in Belief of Recession

- The yield curve remains inverted with the 10-year Treasury at 4.74% and the 2-year at 4.95%. The spread is -0.21% today.
- Once the yield curve inverts, it takes about 15 months for the economy to enter recession. The latest inversion began in July 2022, 15 months ago.
- When the long end of the yield curve rises more than the short end, you have a “Bear Steepener,” which is a signal the recession is soon to start.



Real Wages (Inflation-Adjusted) Are in Decline

- In 2019, real median household income peaked at \$78,250, which represents an increase of 24% since 2012.
- Nominal wages have continued to rise; however, inflation has outpaced the growth in wages. Therefore, real median household income is now \$74,580, down 5% from its peak despite all the government transfer payments.
- Since 1987, every time real median household income has fallen, the country has entered a recession.

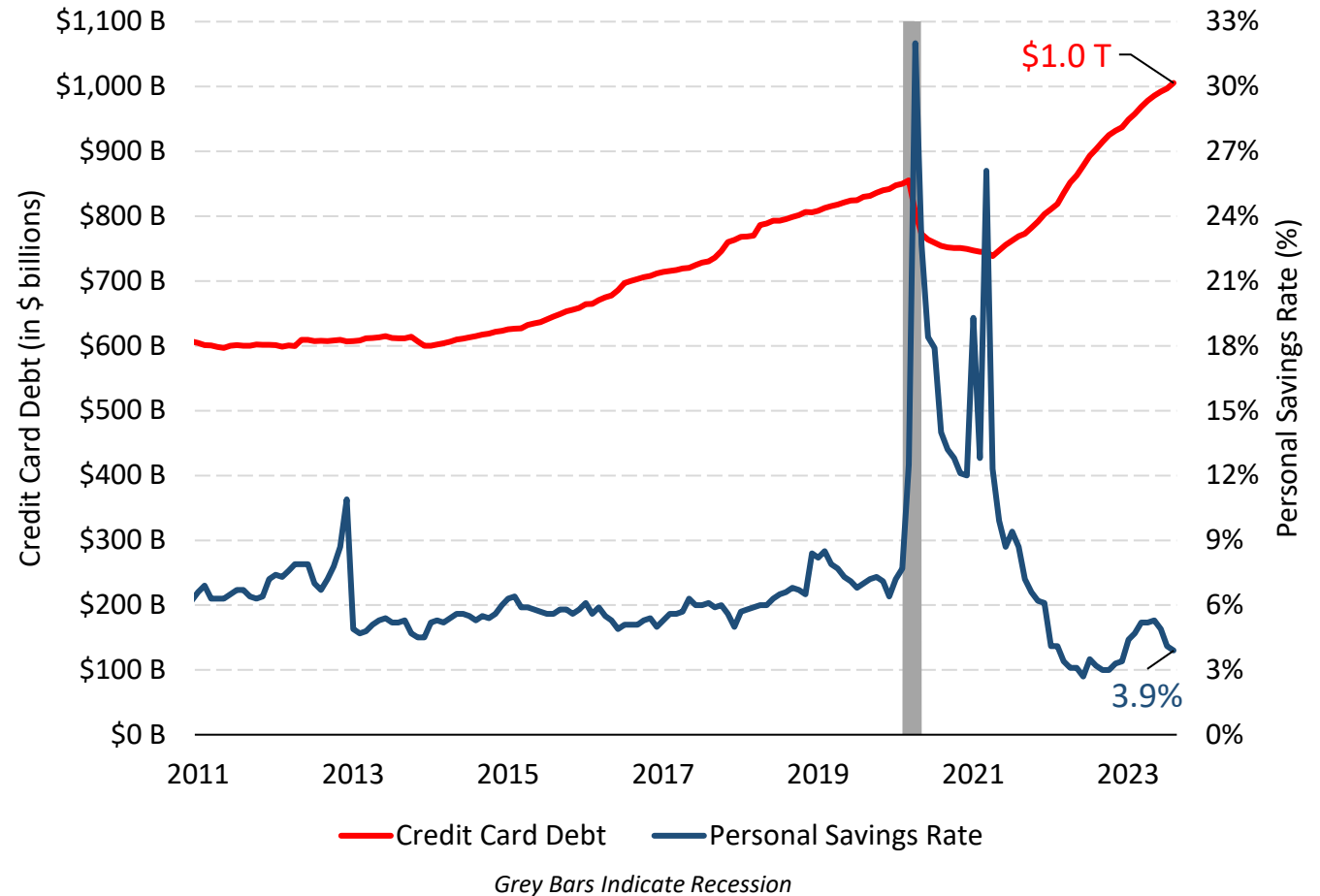


Source: United States Census Bureau

Consumers Cut Savings Rate While Adding Debt

- Credit card debt has rapidly increased and now exceeds \$1T, \$142M higher than at the prior peak of 2020.
- The personal savings rate plunged from its peak during the pandemic and has settled at 3.9%, the lowest since the GFC.
- Credit card interest rates have risen 6.6% since February 2022 to 21.2% today.

Credit Card Debt vs. Personal Savings Rate

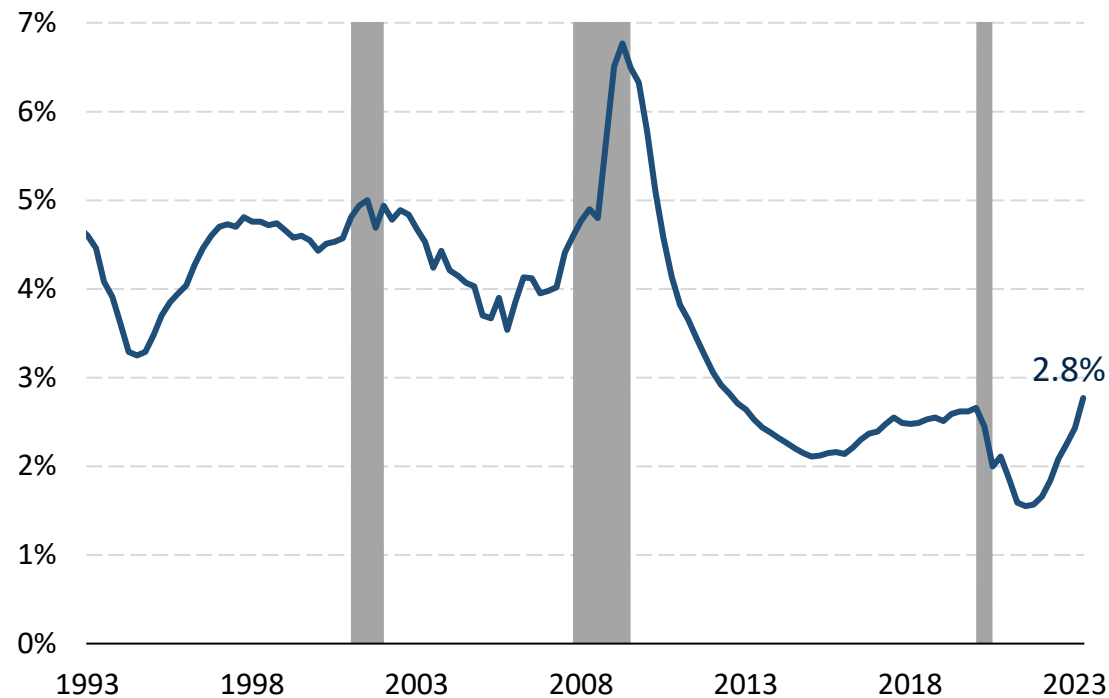


Source: Bureau of Economic Analysis

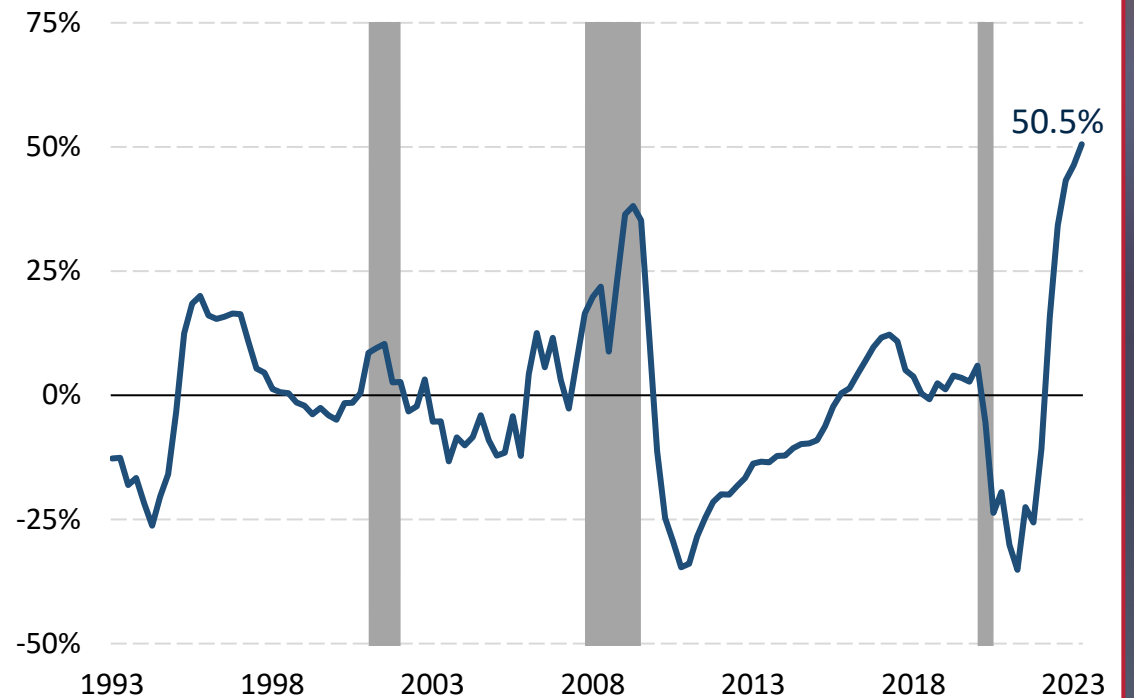
Consumer Delinquencies Are Accelerating

- After a period of significant government transfer payments, reported credit worthiness significantly improved, but credit quality is now deteriorating at a rate surpassing that of the GFC.
- Subprime auto credit 60+ days delinquent is now the highest on record at 6.1%.

Delinquency Rate on Credit Card Loans (%)



Delinquency Rate Change YoY (%)



Grey Bars Indicate Recession

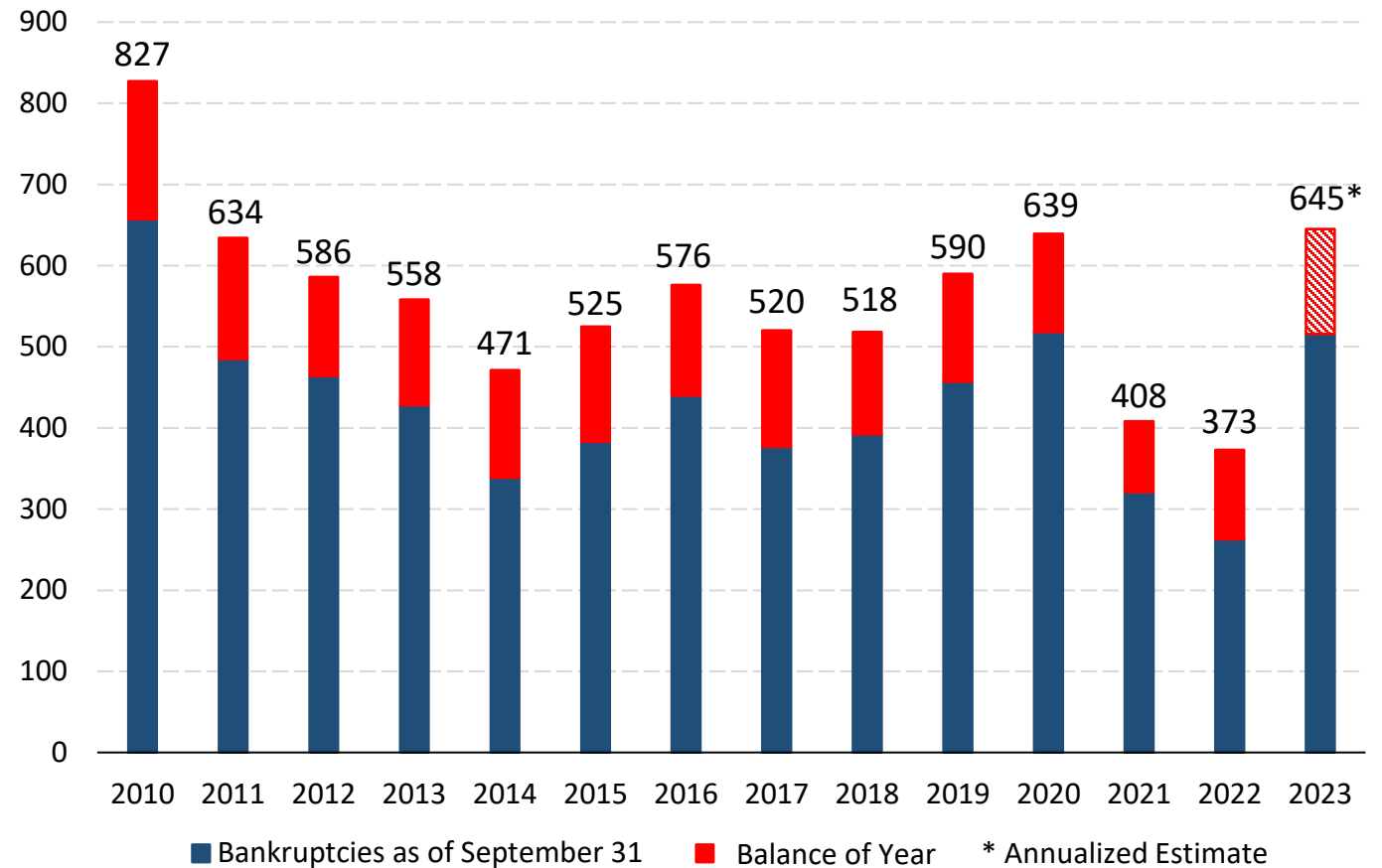
Source: Federal Reserve System

Corporations Across Industries Fold

Bankruptcies in 2023:

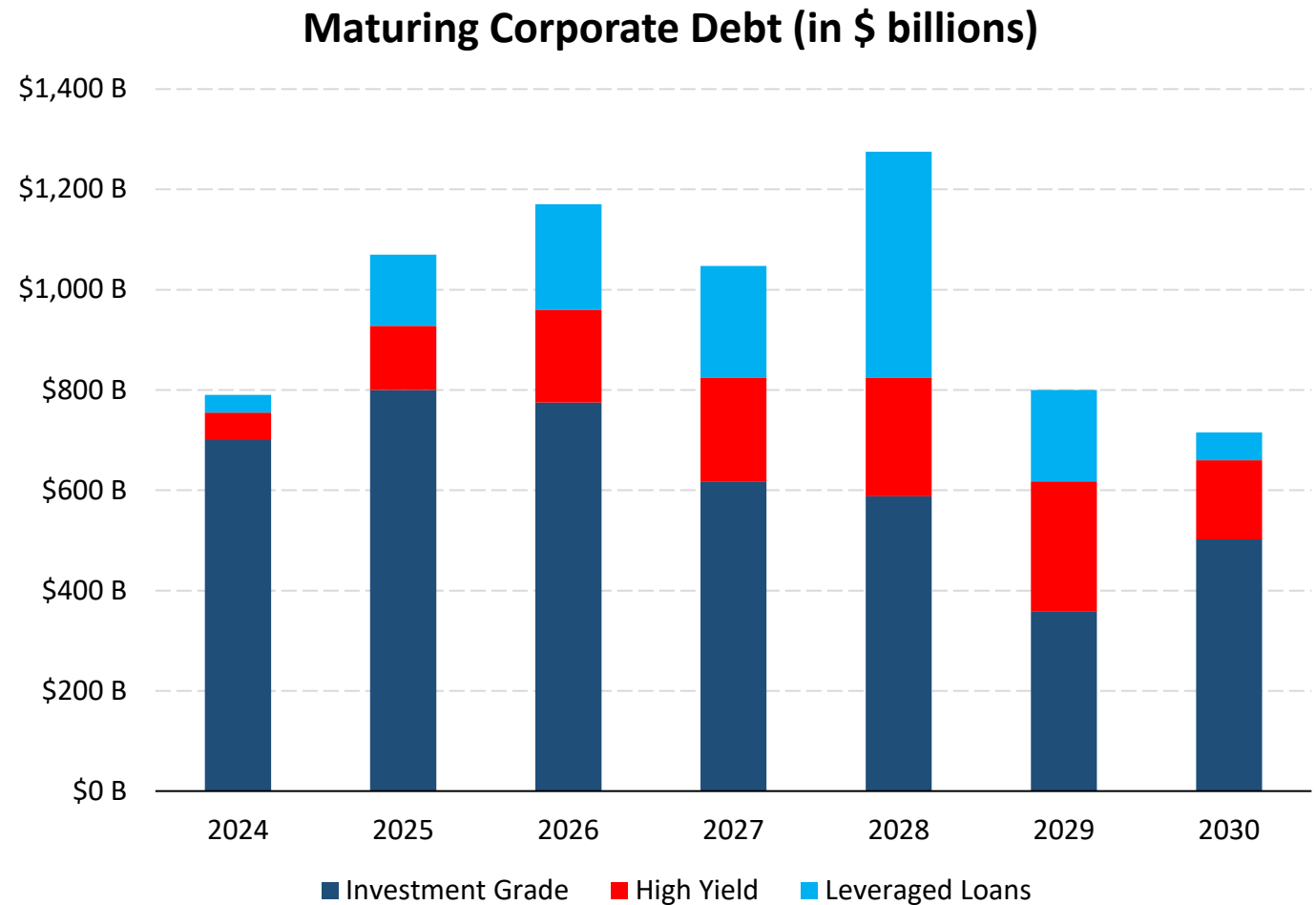
- Silicon Valley Bank
- Bed Bath and Beyond
- Vice Media
- Signature Bank
- First Republic Bank
- FTX
- Virgin Orbit
- Lordstown Motors
- Yellow Trucking
- Celsius Crypto
- Party City
- Smile Direct Club
- Rite Aid
- Serta Bedding
- *+400 Additional*

U.S. Corporate Bankruptcies by Year



Billions of Debt Needs Refinancing at Higher Rates

- Nearly \$800B of corporate debt is set to mature in 2024, followed by \$1.1T and \$1.2T in 2025 and 2026, respectively.
- A total of \$6.9T of corporate debt is set to mature by the end of 2030.
- If all S&P 500 companies' debt refinanced at today's rates, 29% would become unprofitable.

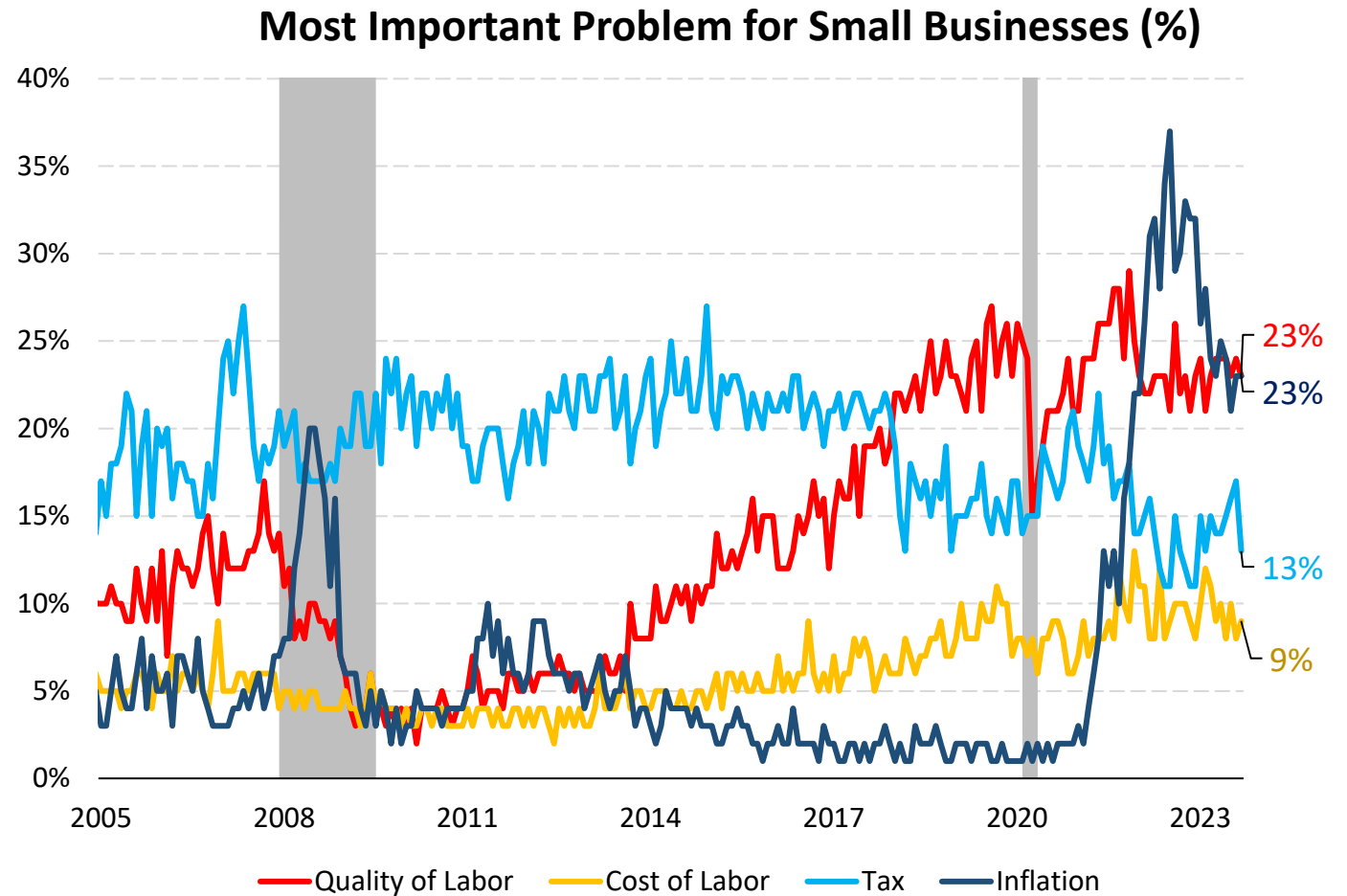


Source: Bloomberg, Goldman Sachs Global Investment Research

Labor Quality Poses a Major Problem for the U.S.



- A 2020 Pentagon study revealed that **77% of young Americans do not qualify for military service** due to drug abuse, mental health, or obesity.
- The more important concerns are the health of our society and our ability to properly operate our education and healthcare systems, as well as the broader society.



Grey Bars Indicate Recession

Source: National Federation of Independent Business

Mismanagement of Energy Resources



U.S. Energy Prices – Forerunner of Inflation Resuming?



WTI Daily Crude Oil Price



Henry Hub Monthly Natural Gas Price



U.S. Weekly Regular Gasoline Price



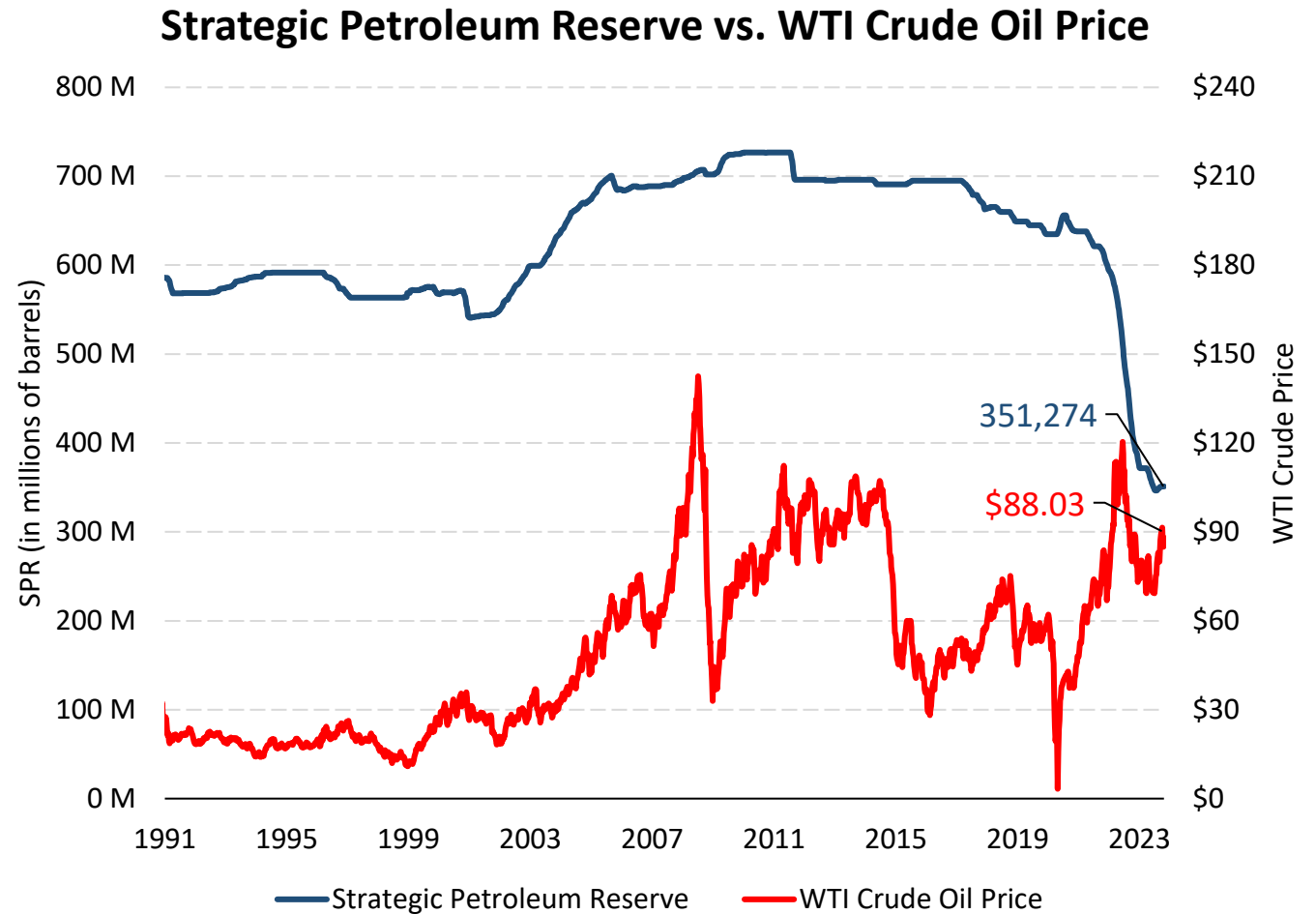
U.S. Weekly Diesel Gasoline Price



Source: CME Group

Strategic Petroleum Depletion Weakens U.S.

- We have now drained 44% of our strategic petroleum reserves.
- SPR depletion has left the United States with **17 days** of supply. Historic average SPR supply is 33 days.
- Biden originally announced that the refill price was \$70, then raised the price to \$79 on Oct 19th.



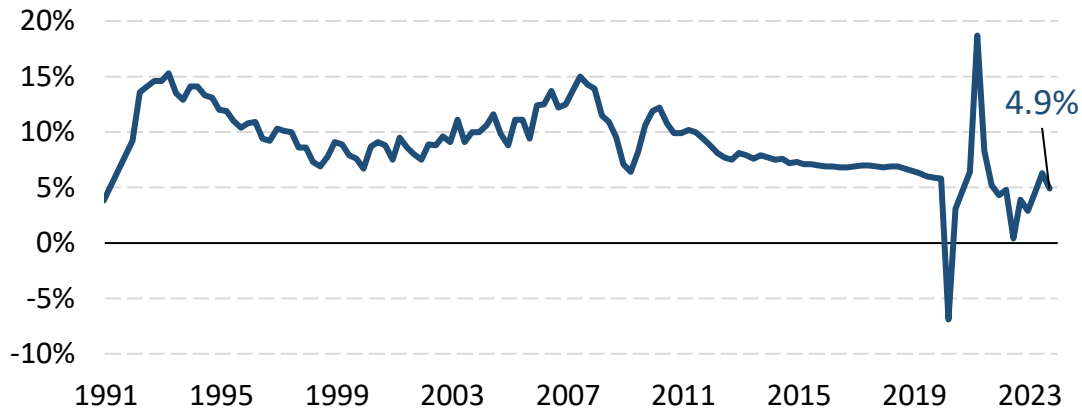
Global Markets



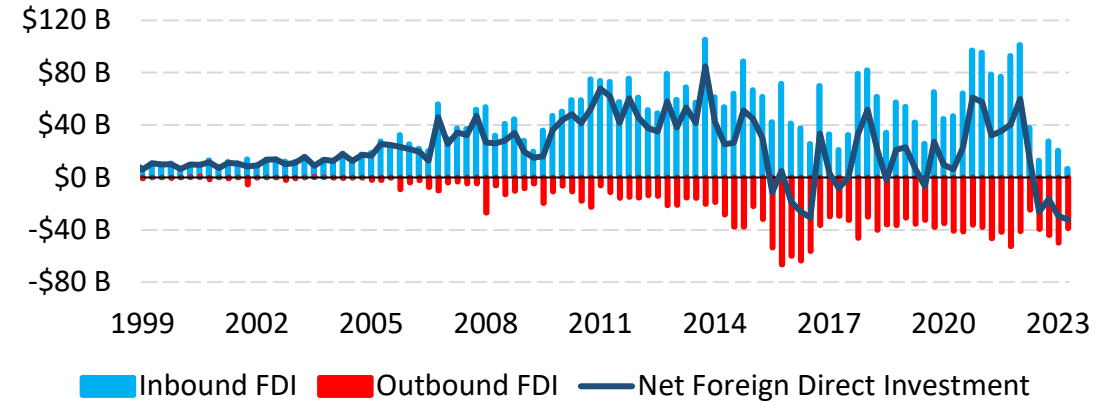
China's Growth Story Is Now Over



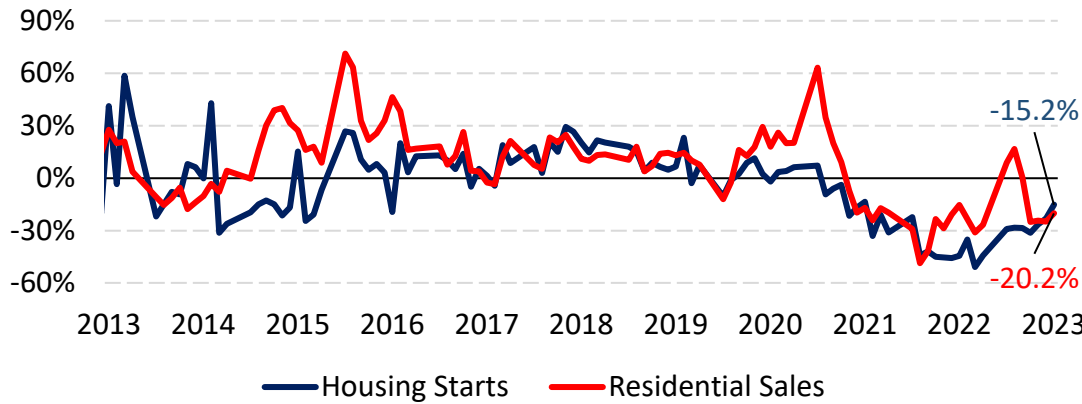
China GDP YoY Growth (%)



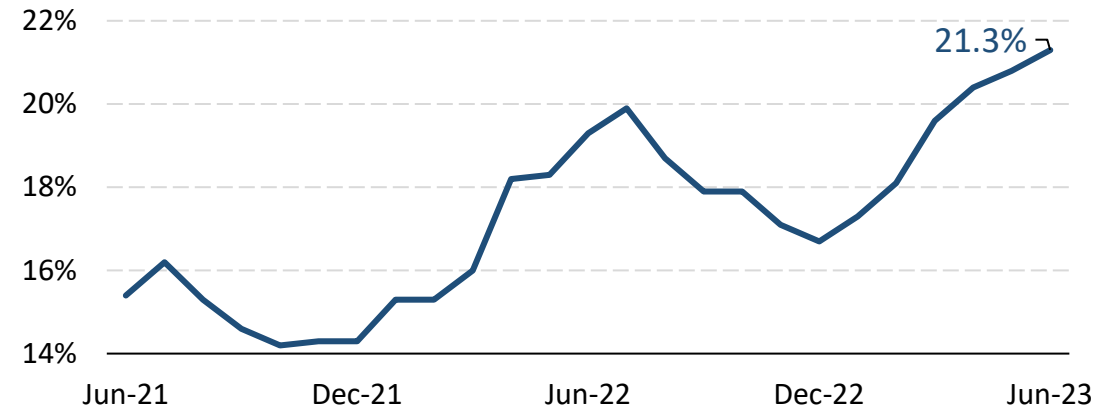
Foreign Direct Investment in China (in \$ billions)



China Housing Starts and Sales YoY Change (%)



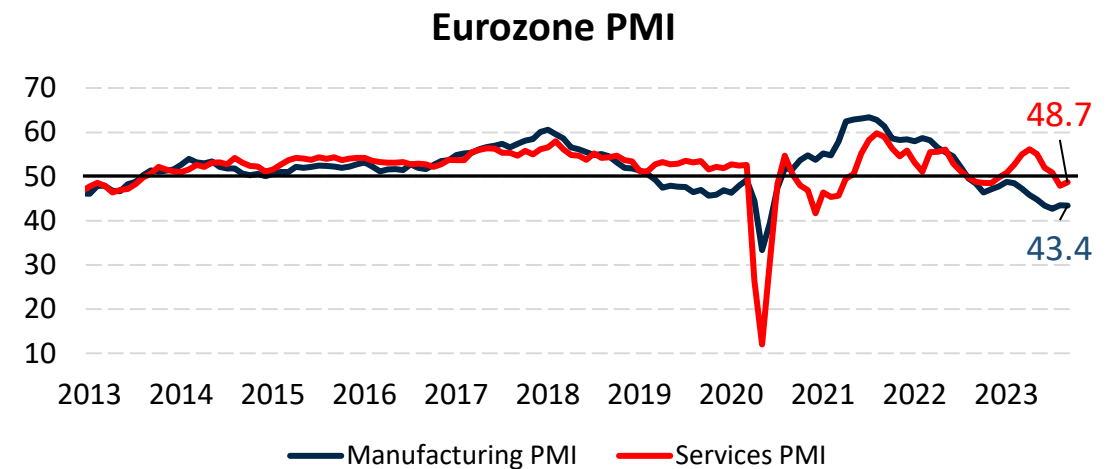
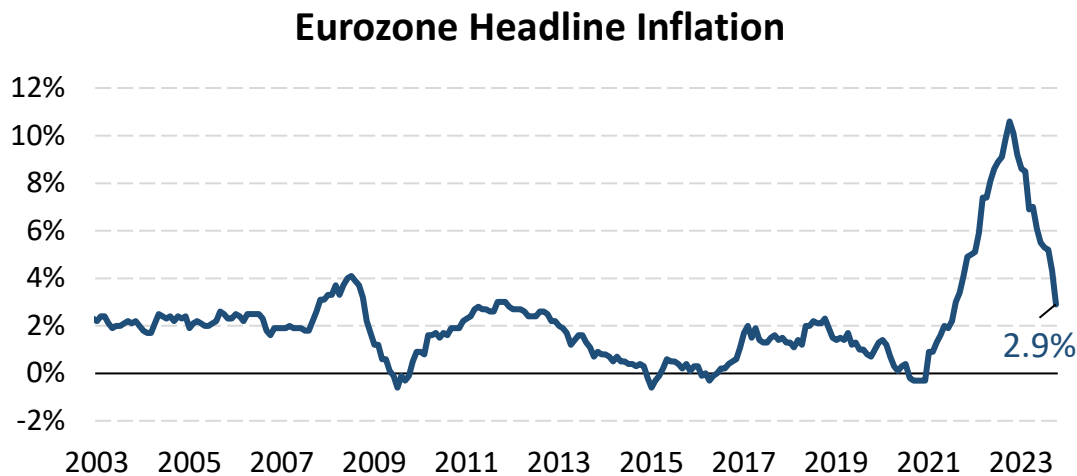
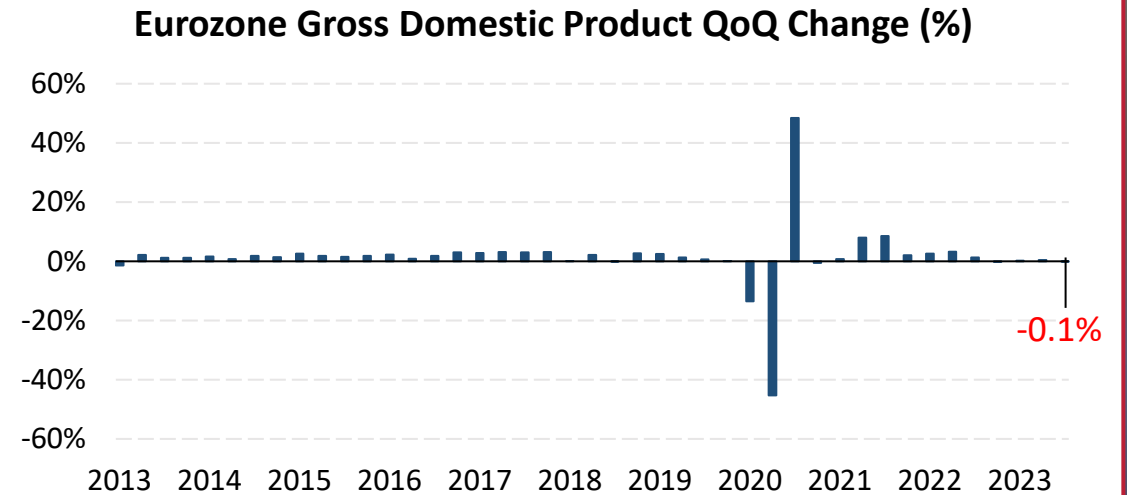
China Youth Unemployment Rate (%)



Source: National Bureau of Statistics of China

Eurozone Is in Recession

Country		GDP QoQ (%)
Spain		+0.3%
France		+0.1%
Germany		-0.1%
Italy		-0.4%
Ireland		-1.8%

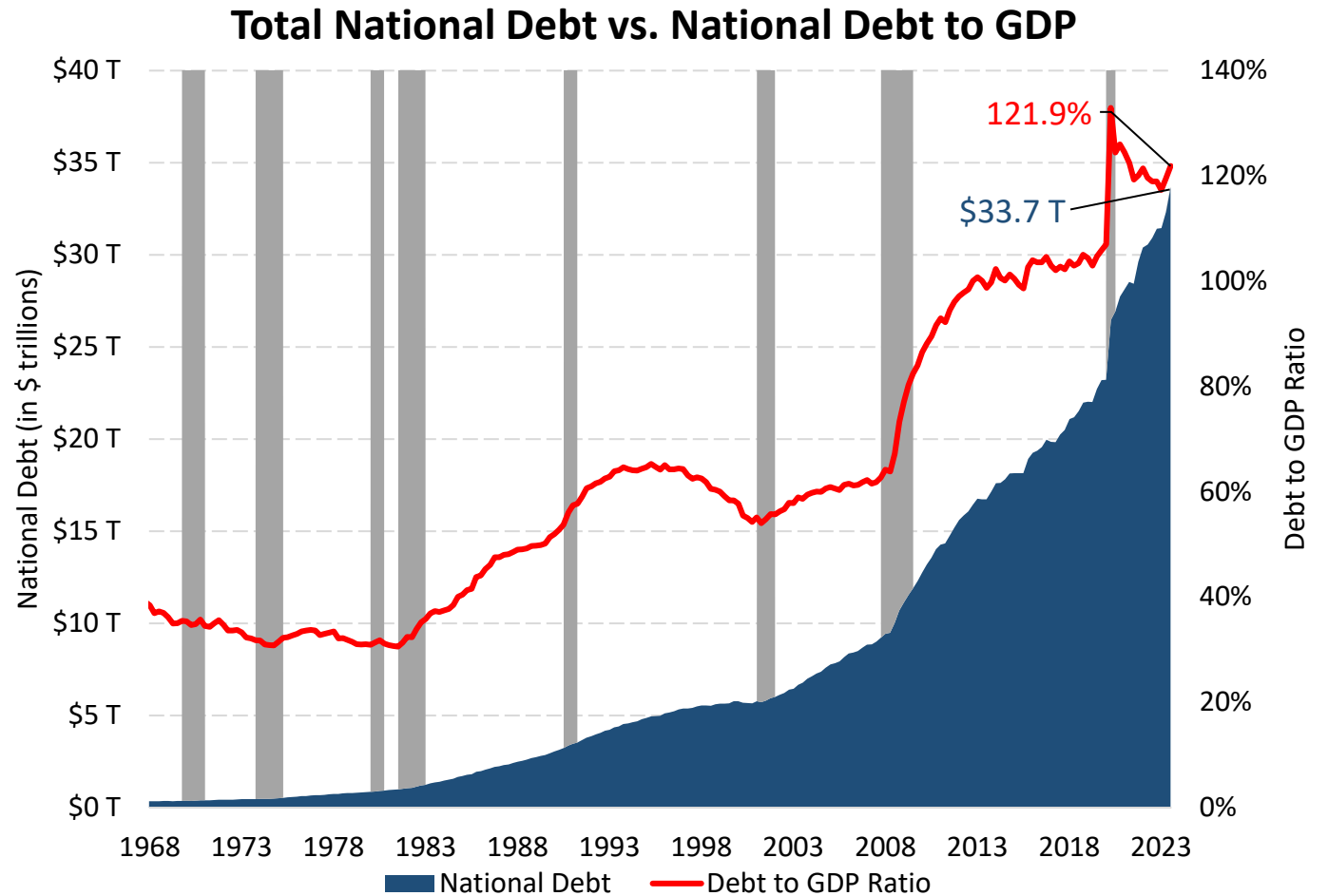


The U.S. Government – Lender of Last Resort Is Broke



The U.S. Has Entered a Debt Trap

- The Debt to GDP stands at 122%. Total debt is now \$33.7T.
- At the end of World War II, the country's debt to GDP peaked at 106%, and it took two decades of sacrifice and financial repression to get back below 40%.
- The U.S. is now consistently running massive deficits. The U.S. ran a deficit of \$1.7T in 2023 and is expected to run a deficit of \$1.8T in 2024, even with full employment.

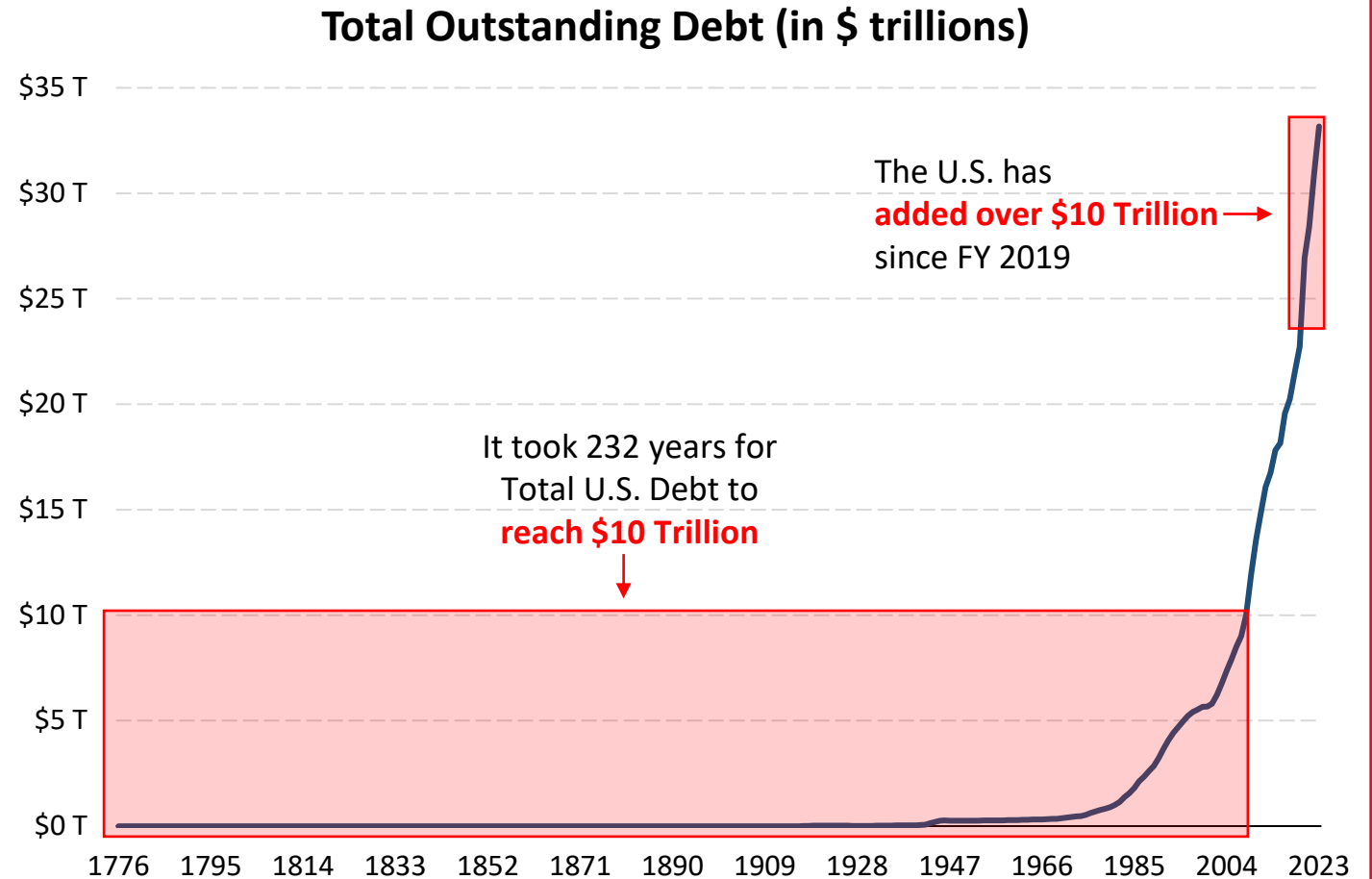


Grey Bars Indicate Recession

Source: U.S. Treasury Department, Bureau of Economic Analysis

Over Two Hundred Years of Debt Amassed in Four

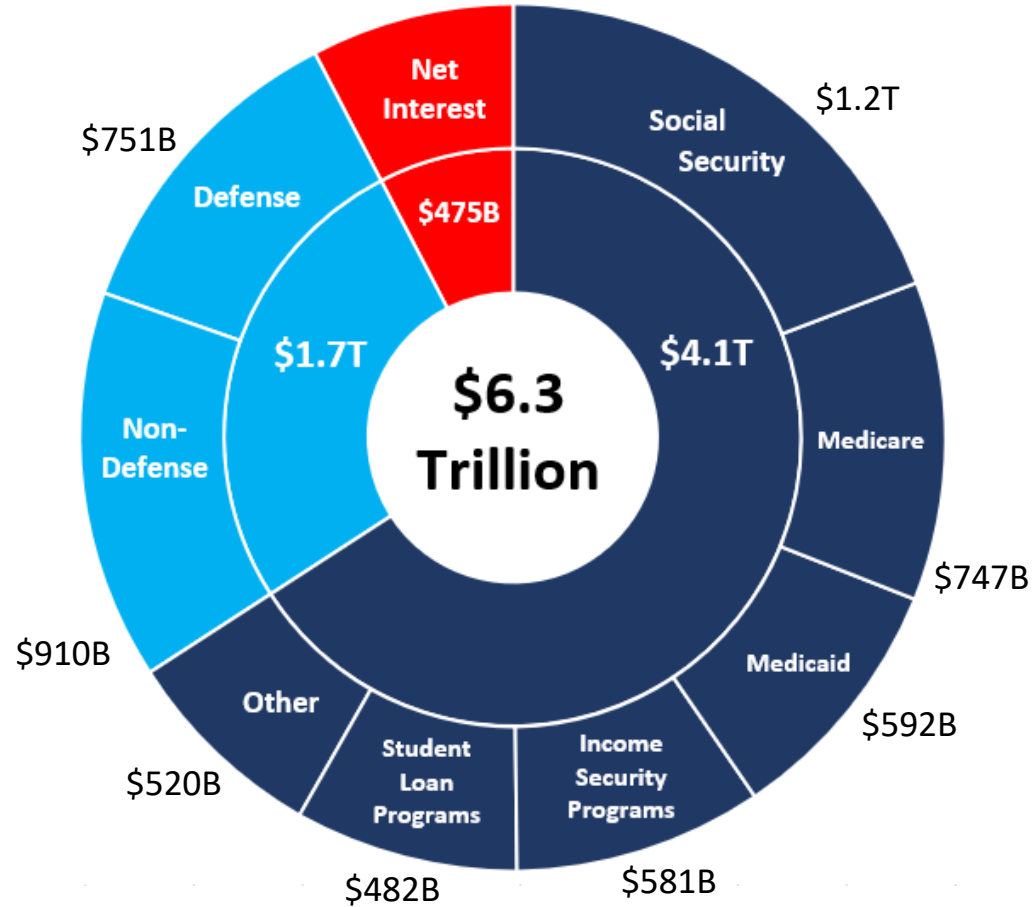
- The U.S. has added \$10T of debt since the end of the 2019 fiscal year. This amounts to more debt added in 4 years than in our nation's first 232 years combined.
- Currently, the US is adding on average:
 - **\$604B** per month
 - **\$20B** per day
 - **\$833M** per hour



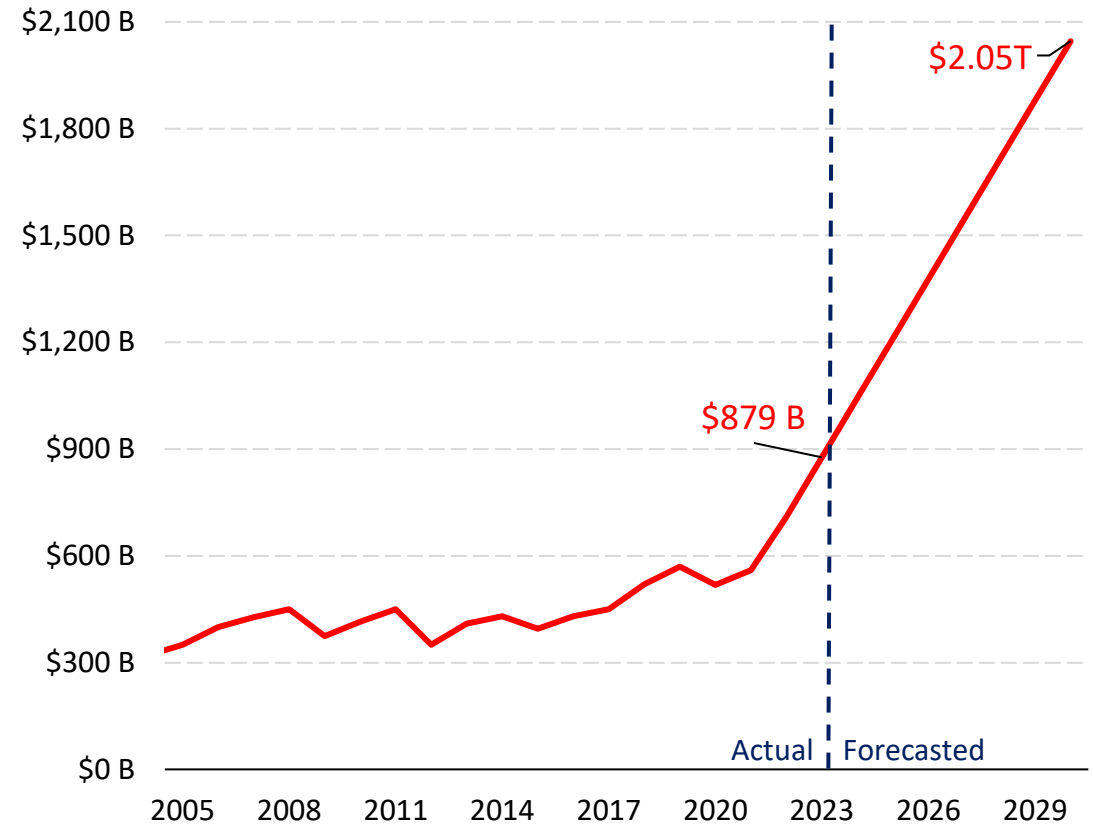
Interest Expense to Be Second Largest Expenditure



Fiscal Year 2022



Gross Federal Interest on Treasury Debt (in \$ billions)

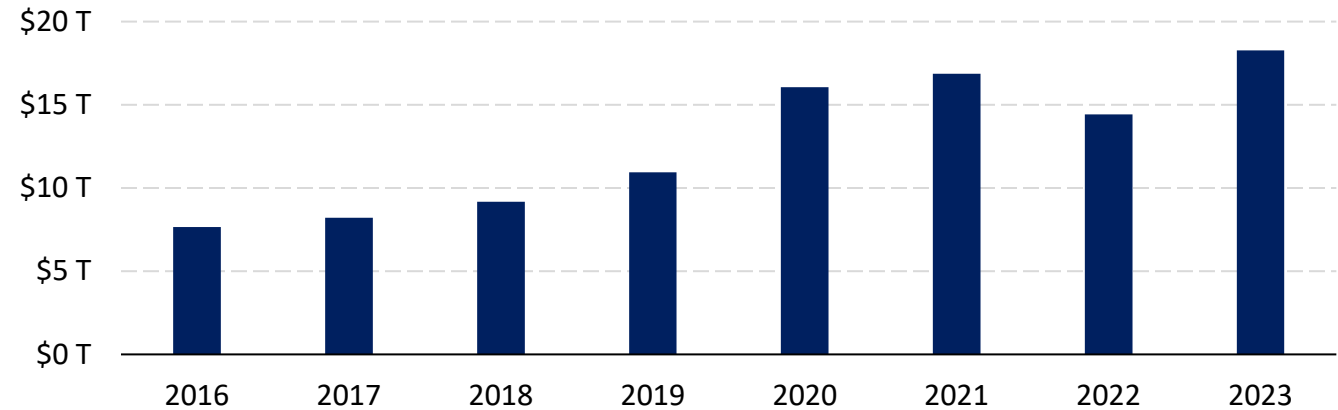


Source: Congressional Budget Office, Fiscal Service

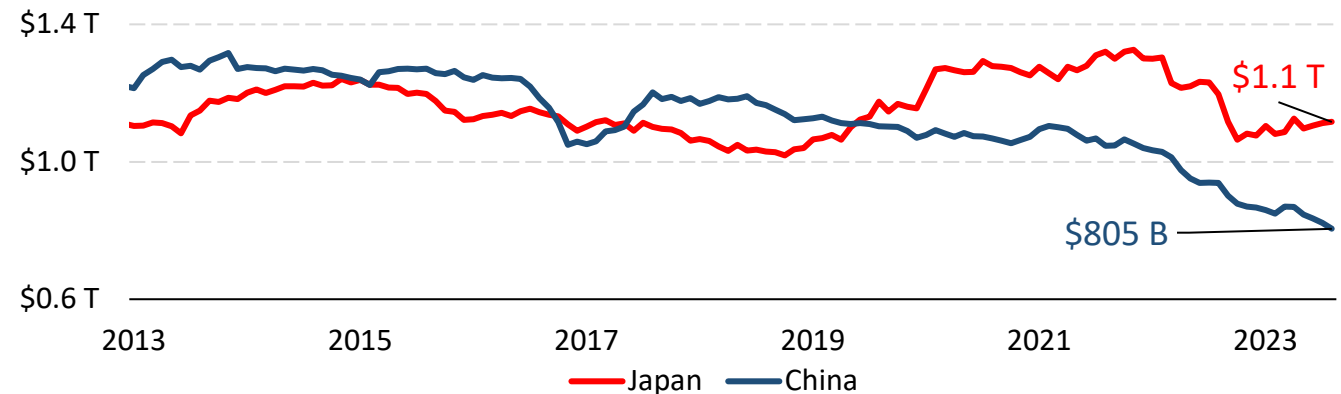
Where Will the Buyers of U.S. Treasury's Come From?

- There are \$18.3T in Treasury's that mature in 2023.
- This compares to \$16.9T and \$14.4T of Treasury maturities in 2021 and 2022, respectively.
- Treasury maturities in 2023 have more than doubled over the last 6 years from \$8.2T in 2017.
- 23% of the total federal gross debt is owned by foreign countries with Japan and China being the largest holders.

Treasury Securities Maturing (in \$ trillions)



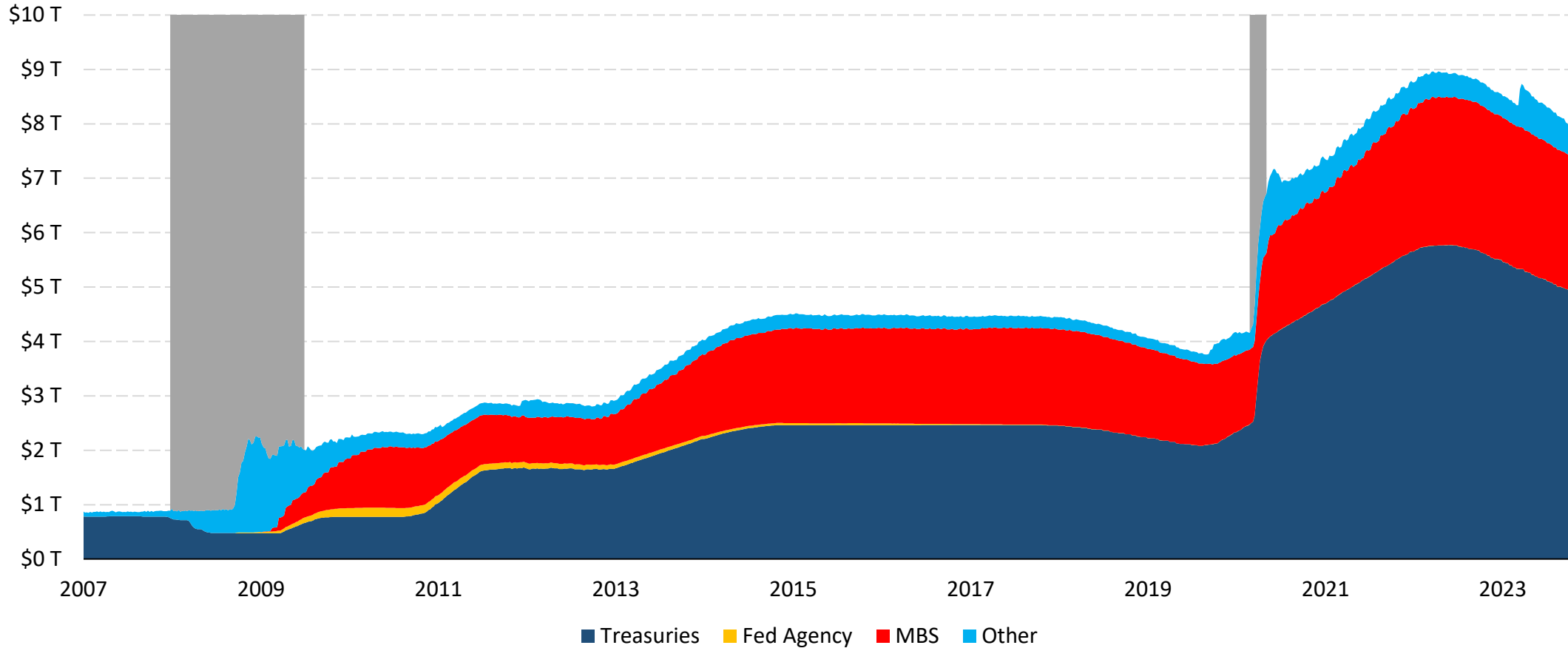
U.S. Government Debt Held by Foreign Countries (in \$ trillions)



Source: U.S. Treasury Department

How Big Will the Fed Balance Sheet Grow?

Federal Reserve Assets (in \$ trillions)



Grey Bars Indicate Recession

Source: St. Louis Federal Reserve

Drumroll....



Predictions for the Economy 2024

- **U.S. Economy:** The consumer will run out of gas, and the U.S. will enter a recession that could turn into a hard landing; however, GDP will be lumpy with one potential positive quarter in 2024.
- **Unemployment Rate:** Corporations will start to downsize in early 2024, and the unemployment rate will slowly lift through the year but remain slightly below 5%.
- **Interest Rates:** The Fed at most will have one more 25-basis point increase and will be forced to cut rates at some point in mid- to late-2024, but do not expect rate cuts of more than 75-basis points in 2024 unless a global crisis ensues.
- **Fed Balance Sheet:** The Fed will continue with QT through the remainder of 2023 and will be forced to stop again in the first half of 2024.

Predictions for Asset Values in 2024

- **U.S. Equities:** The equity market will have a selloff of 15% in the next 6 months as investors realize that the country will be entering a recession. Once the Fed indicates that it will pivot, the equity markets will have a moderate rally.
- **Fixed Income:** The bond markets, after having 3 consecutive down years, will reverse course and have a positive year in 2024.
- **Residential Real Estate:** Housing values will continue to decline by up to 10% but will again remain more resilient because of limited supply.
- **Commercial Real Estate:** CRE values will continue to decline through 2024 as foreclosures and distress sales become a significant part of transaction volumes. Multi-family will surprise to the downside given its outperformance over the past decade.

Political and Global Predictions for 2024

Only a fool would try to predict anything in politics in the year ahead. Nevertheless, here are my foolish guesses:

- **Presidential:** Joe Biden will not be President after the next election. It is my only strong conviction.
- **Senate:** Republicans will re-take the Senate with West Virginia, Montana, and Ohio flipping back into Republican hands, garnering them a one seat majority. The Republicans have a decent chance of winning up to three additional seats.
- **House of Representatives:** There will be losses and gains by incumbents of both parties, but the Republicans will retain a modest majority.

Global:

- There is over a 50% chance that China blockades Taiwan.

Final Word

“Every adversity, every failure, every heartache carries with it the seed of an equal or greater benefit.”

- Napoleon Hill

“The primary goal of investing in the years ahead should be the return of capital and not the return on capital.”

- Eric Hovde

Q&A



For all feedback or questions, please email us at
econupdate@sunwestbank.com

Thank You!