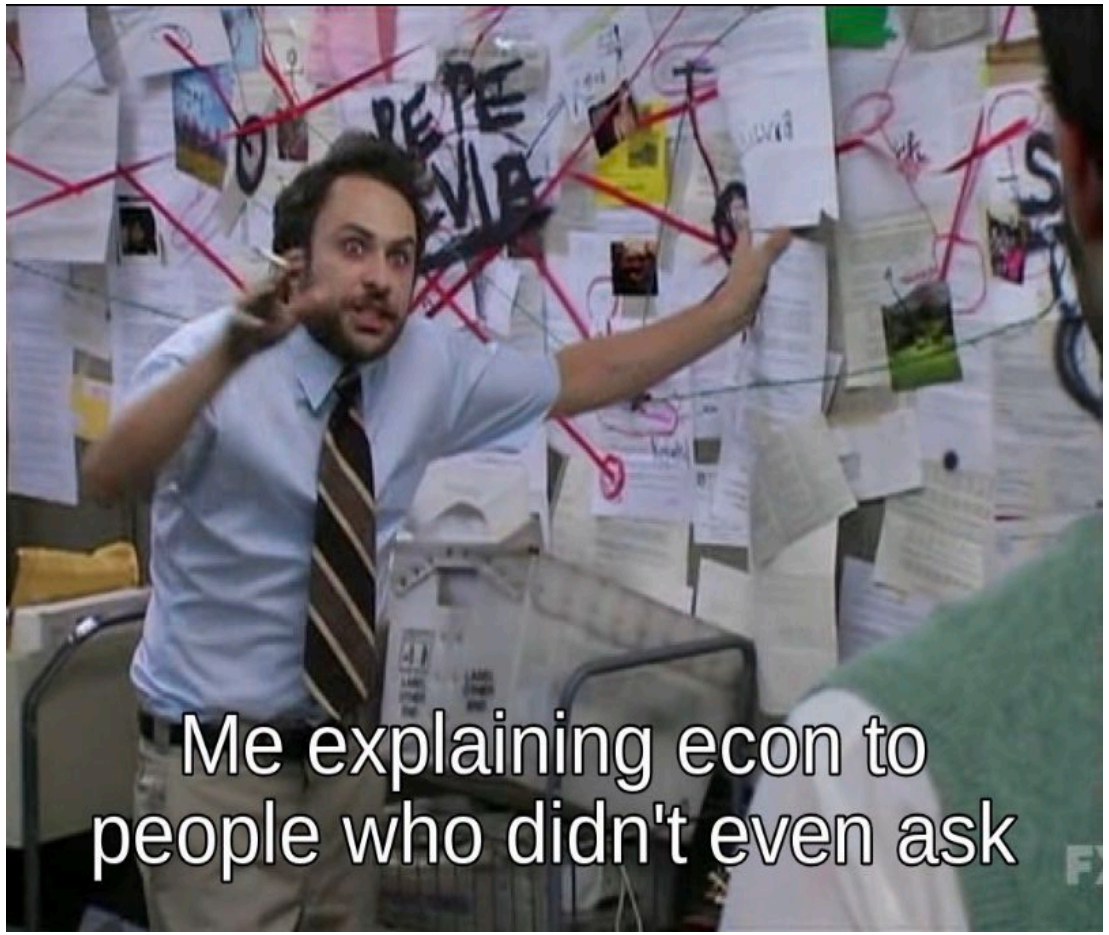
Now What?
Expectations for 2023 and Beyond

NACMBCS - Webinar

Chris Kuehl - Armada

January 2023



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Real GDP Outlook Remains Flat Until End of '23

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3. Back to sub-2% growth through '25

	2022				2023				2019	2020	2021	2022	2023	2024	2025
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4							
Real GDP	-1.6	-0.6	2.6	0.7	-0.6	-1.5	-0.4	1.2	2.3	-2.8	5.9	0.5	0.5	1.6	1.8
Unemployment rate (%)	3.8	3.6	3.6	3.7	3.7	4.3	4.6	4.6	3.7	8.1	5.4	3.7	4.6	4.6	4.5
PCE Inflation (%Y/Y)	6.4	6.6	6.3	5.7	4.7	3.6	3.2	3.1	1.5	1.1	4.0	5.6	3.1	2.5	2.1
Core PCE Inflation (%Y/Y)	5.3	5.0	4.9	4.7	4.0	3.6	3.5	3.5	1.7	1.3	3.5	4.8	3.5	2.5	2.1
Fed Funds Rate	0.4	1.6	3.1	4.4	4.9	5.1	5.1	5.1	1.6	0.1	0.1	4.4	5.1	4.1	3.1

1. Greatest recession risk is between Q1 and Q3 of 2023

2. Q3 could invert positive if business inventories fall faster than expected. But pressure on consumer household spending could keep inventory building activity weaker than expected in Q3. Q4 is lackluster, especially if the unemployment rate hits 4.6% or higher.

4. To hit 2% inflation target, estimates suggest the Fed will have to hit a peak Effective Funds Rate of 5.1% and unemployment will likely approach 4.6%.

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Source: Conference Board

Good News on the Horizon or Not?

- **Global Inflation Peaking?**
  - Factory gate pricing – producer price index
  - Commodity prices declining
  - Shipping rates down
  - Expectations for inflation have diminished (somewhat)
- **Central Banks Talking Rate Slowdown**
- **Potential Improvement in Supply Chain (depends on China)**
- **Job Growth Still Exceeding Expectations**
- **Oil and Gas Remain Volatile Until Europe Gets Through Winter**
- **China Still Pushing Zero Tolerance**
- **Global Wage Growth, More Risk of Strikes and Generally More Labor Leverage**

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Inflation – What the Fed Is 'Really' Watching…

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Six-month PCE inflation, annual rate

	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sept-22
PCE	7.1	7.1	8.0	6.6	5.9	4.6
PCE ex F&E	5.3	5.0	5.2	4.3	4.6	4.8
Trimmed mean	4.3	4.5	5.0	4.5	4.8	5.0

12-month PCE inflation

	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sept-22
PCE	6.4	6.5	7.0	6.4	6.2	6.2
PCE ex F&E	5.0	4.9	5.0	4.7	4.9	5.1
Trimmed mean	3.9	4.1	4.5	4.5	4.7	4.7

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Source: Federal Reserve

Peak Rate Would Hit Levels Prior to Great Recession

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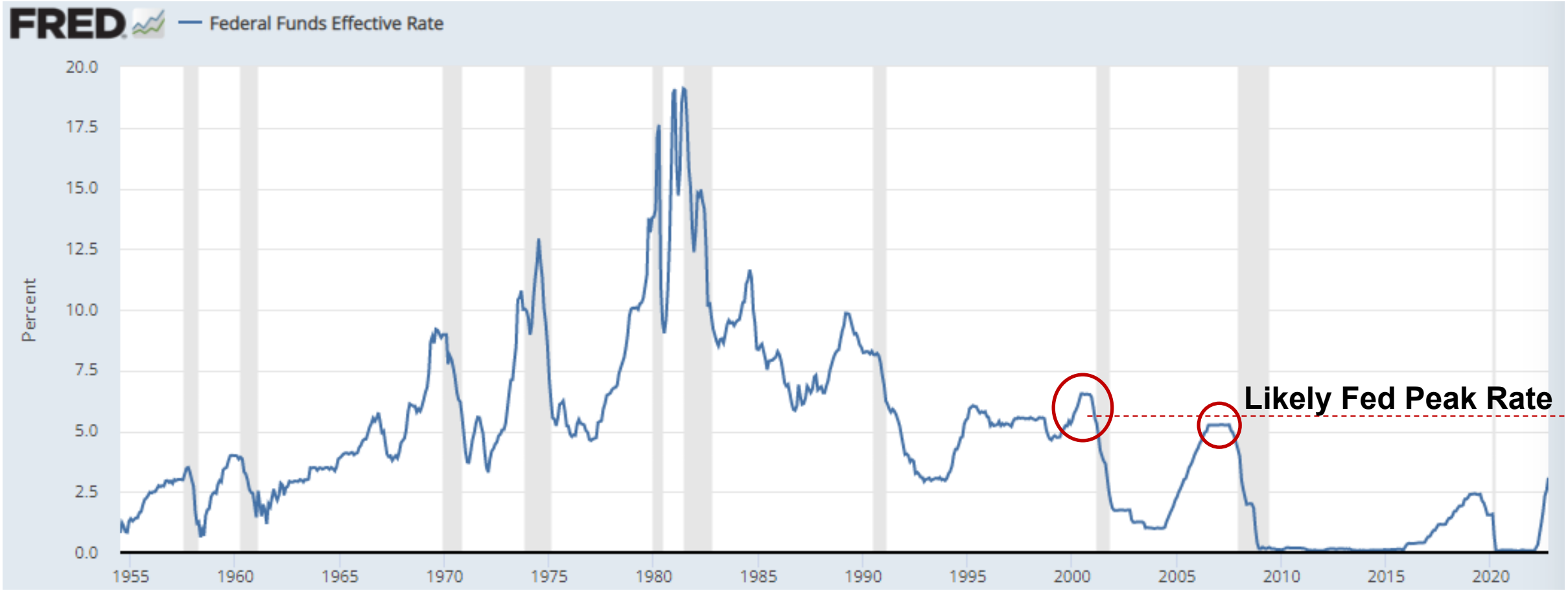
- Many companies have not operated in this environment for 24 years…we forget what it looks like.



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"Corporate amnesia is about 3 years…"

Import Demand: the US Dollar Continues to Gain Strength, Importing Will Continue to be Robust

- Risk: the developing world can't afford to purchase food, energy, etc. Anything denominated in dollars.
- Even Europe is struggling.
- This could eventually become a headwind, but for now it remains a tailwind for US importers.

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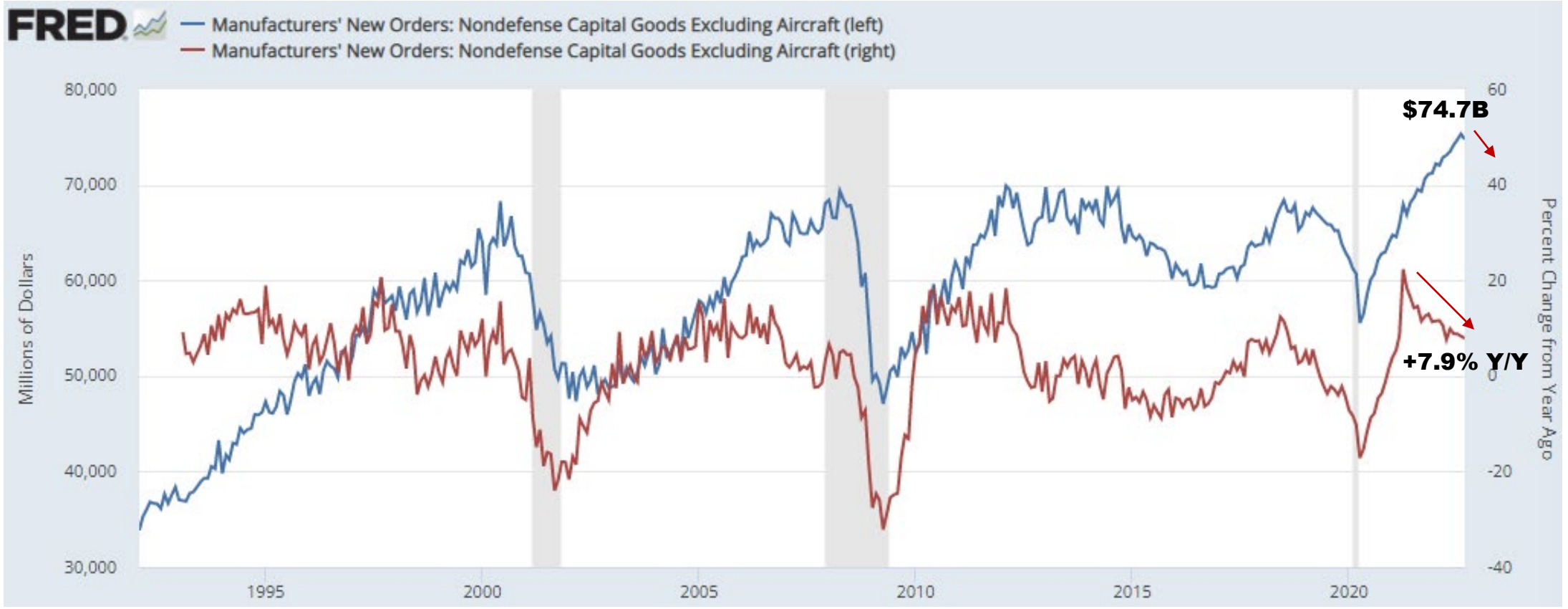
Source: US Dollar Index; MarketWatch Chart

Corporate Investment Now Starting to Show the Fourth Quarter Decline that We Have Been Expecting

- Some surveys of corporate CEO's have indicated planned slowing of spending in the second half of the year if recessionary risk continues to grow.
- US Private investment driving Manufacturing (automation and robotics); Construction



Source: Federal Reserve

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A Lot Of Cash Still Sitting On The Sidelines

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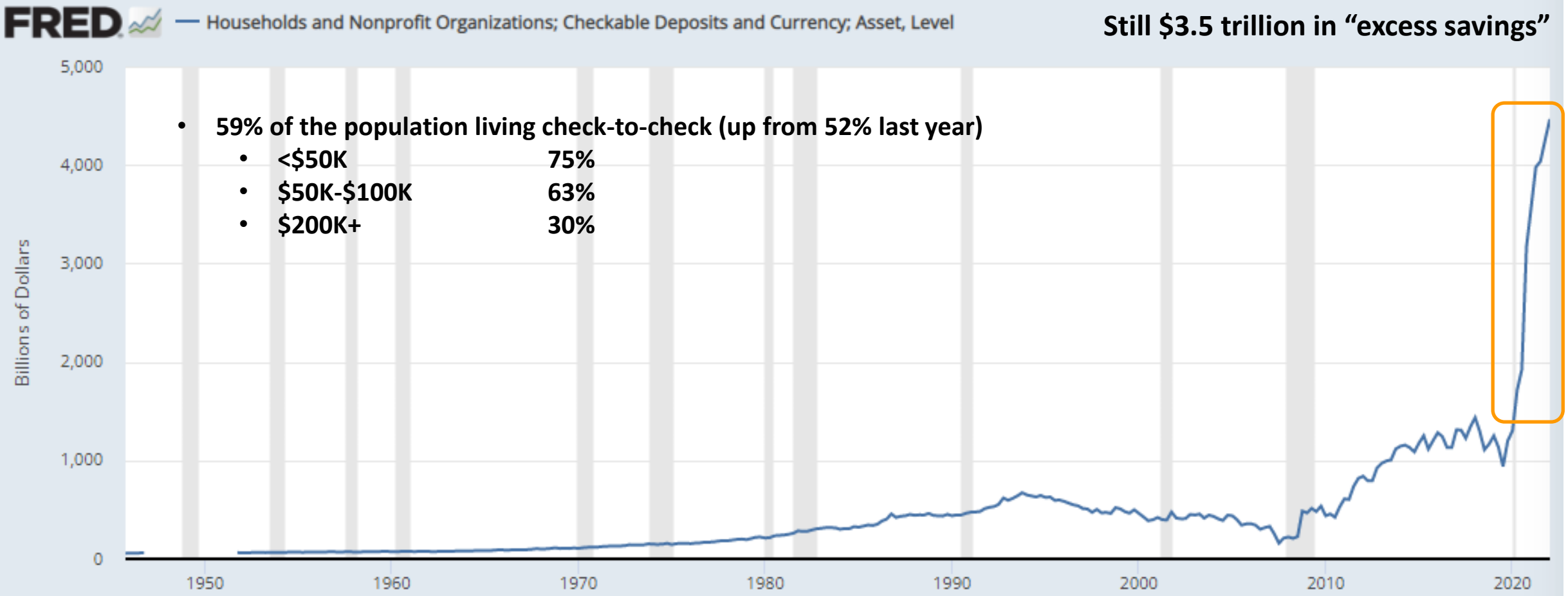

Still $3.5 trillion in "excess savings"

- **59% of the population living check-to-check (up from 52% last year)**
  - **<$50K 75%**
  - **$50K-$100K 63%**
  - **$200K+ 30%**

Source: Federal Reserve

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Consumer Spending Still High, Despite Some Flattening

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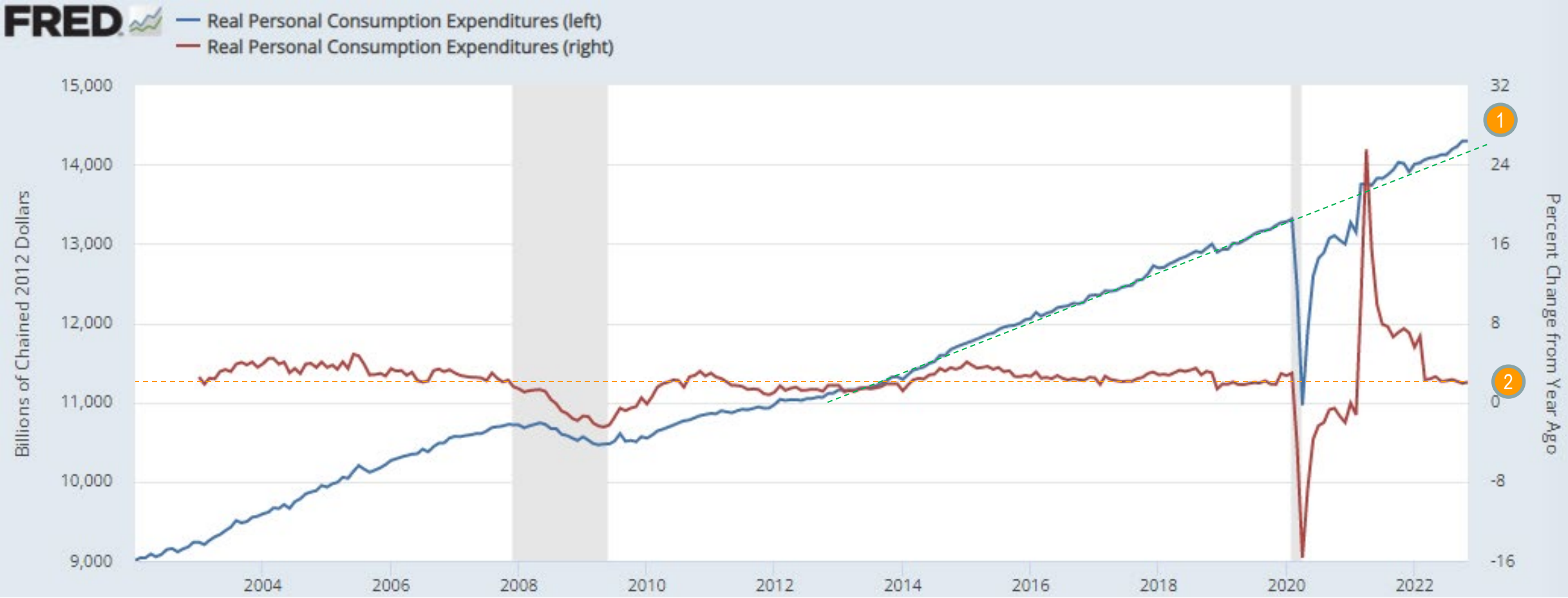
1. **Inflation-Adjusted Spending Through November Remained Stable,**
2. **But were beginning to flatten**



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Retail Specific Spending Shows the Same Spending Trend

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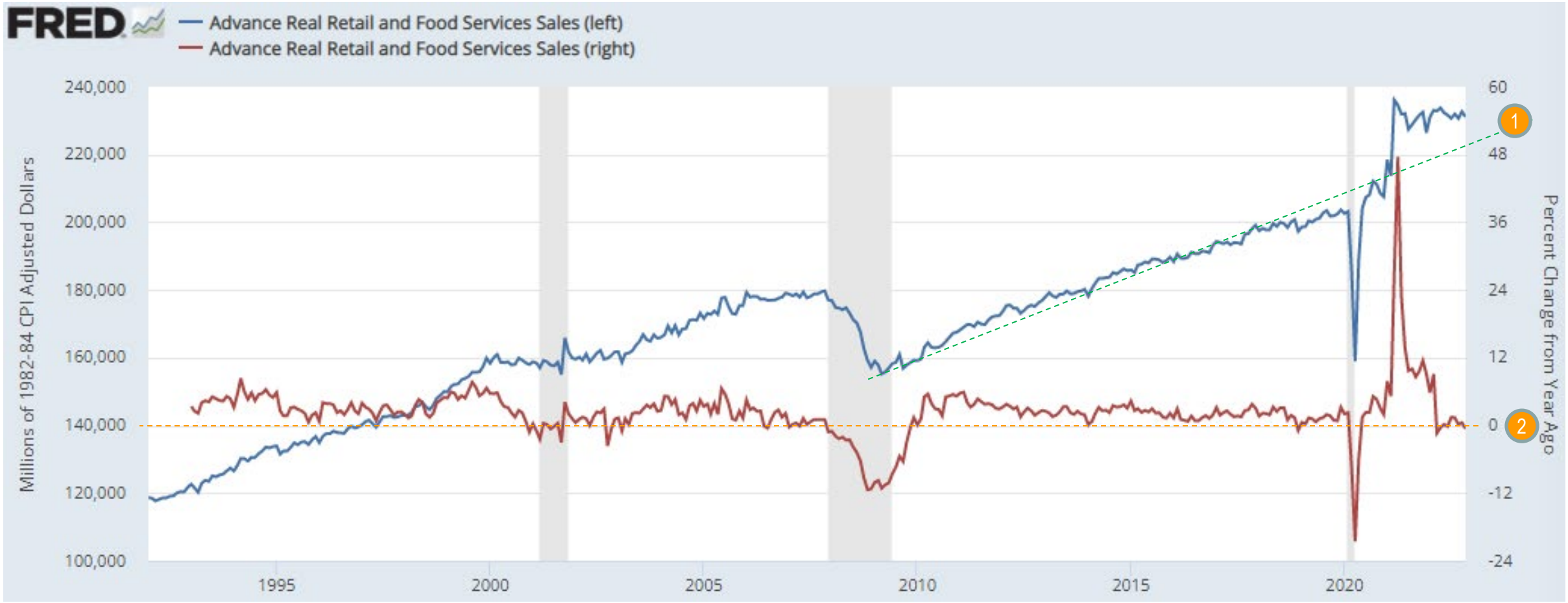
1. Inflation-Adjusted Retail spending through November remains well above the 13-year trend
2. But year-over-year, the deceleration was evident



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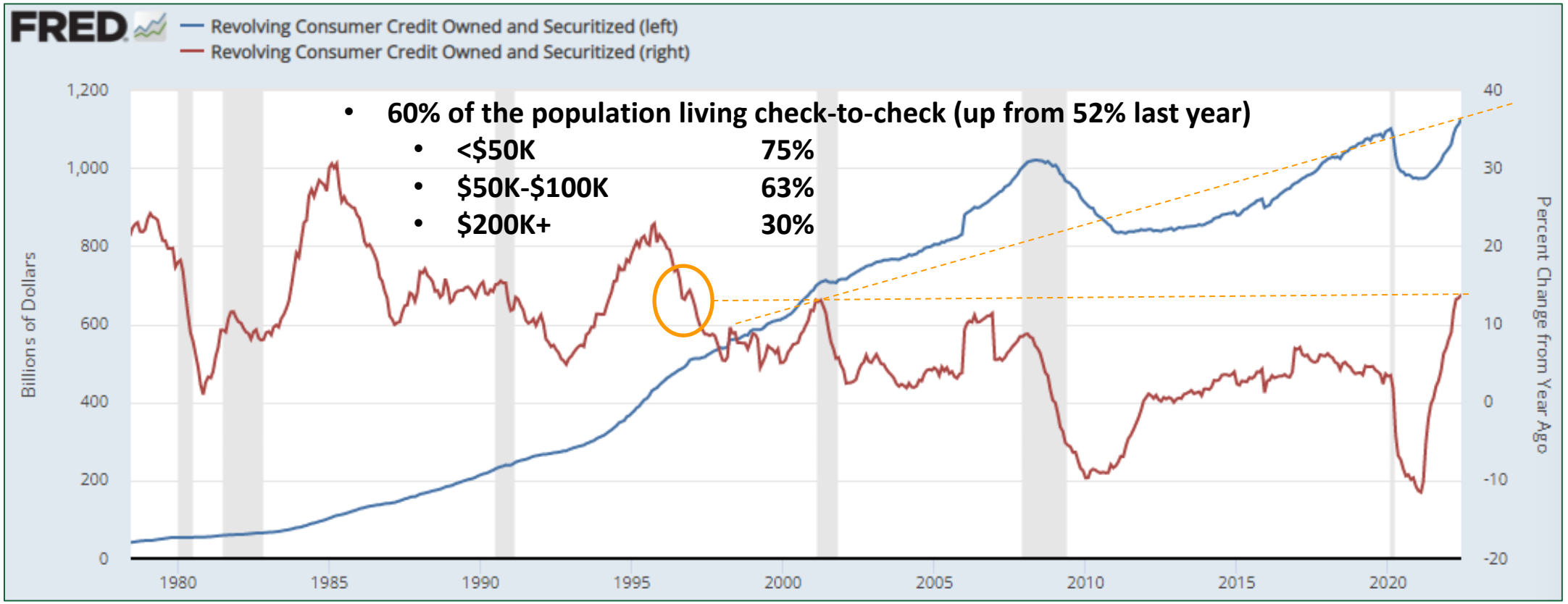
Consumer Credit Use Is Surging…Or Is It?

- Here is the other side of that equation. Household use of revolving debt has hit record levels. The overall savings rate has also now dropped below the 10-year trend and households are under increasing pressure.



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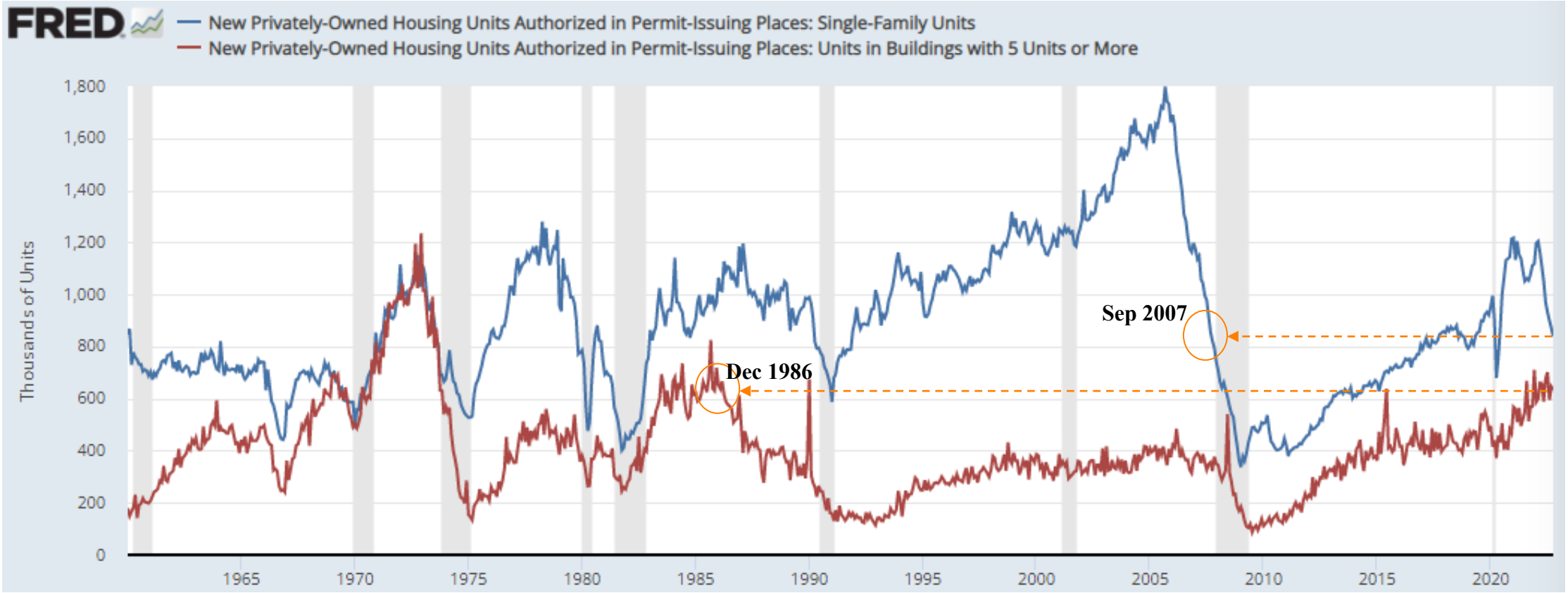
Housing Getting Hit – But Multifamily Still Stable

- Permits are forward-looking, total permits down 10.1% Y/Y.
- Multi-family strongest permits since 1986, up 11.2% Y/Y through October.
- Single family home permits getting hit hard, permits down 22.1% Y/Y.
- Estimates that the US still needs 2.8 million units (not including migrant population) affordability is the issue, hence multi-family.



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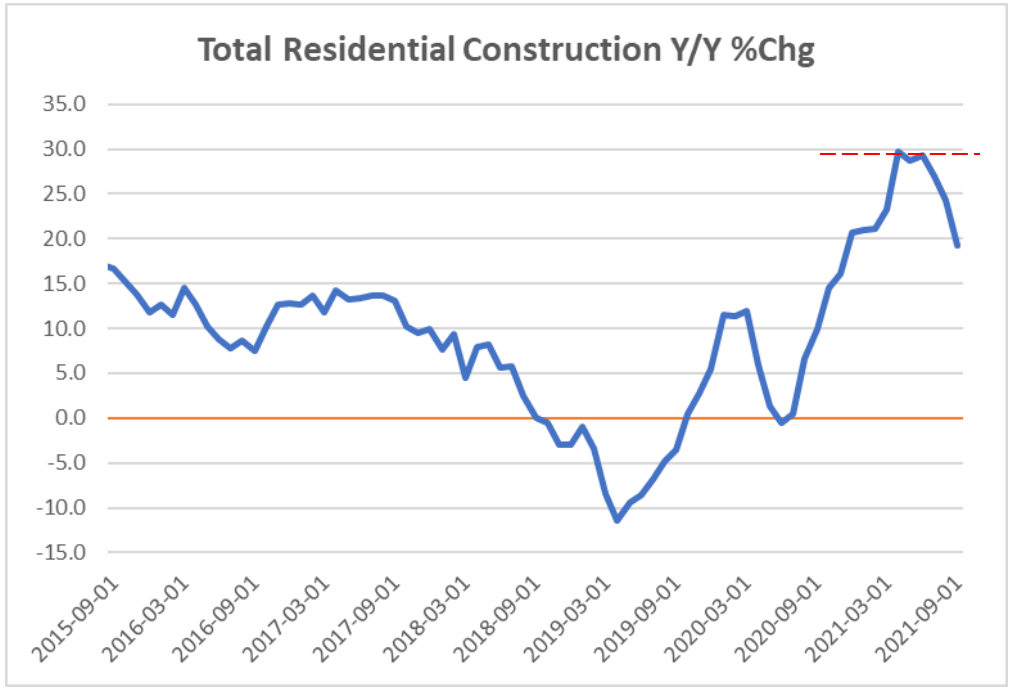
Some Continued Recovery in Commercial Construction

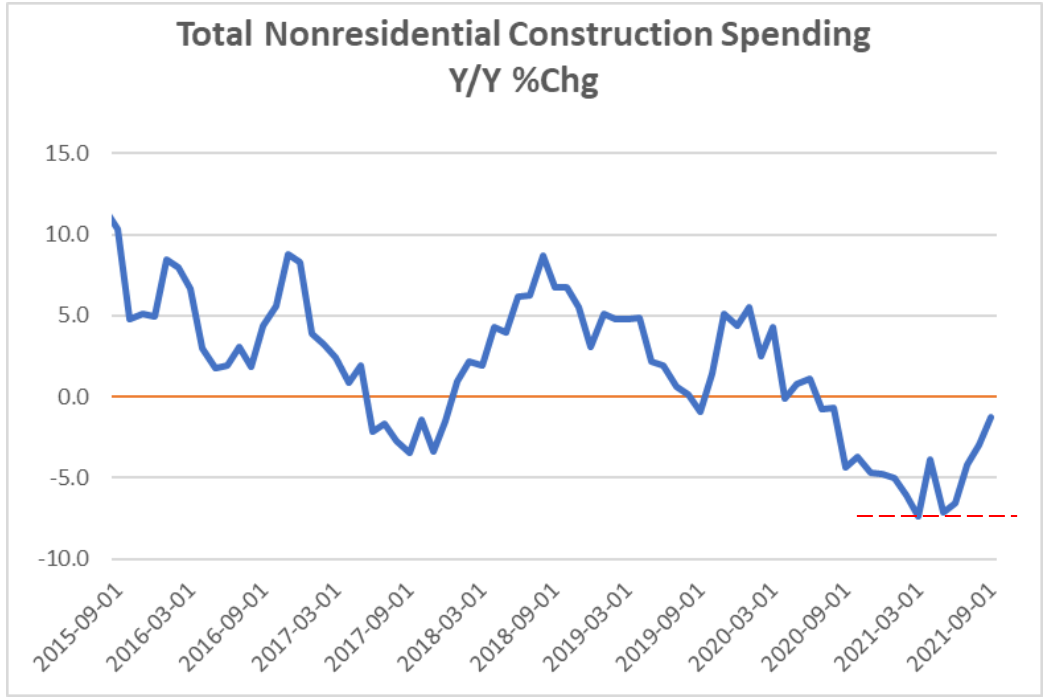


Private Annualized Spending

2019: $550B
2021: $786B

+19.3% YoY

+24.3% in last update



Private Annualized Spending

2019: $815B
2021: $788B

Jan 20' peak: $885B

-1.3% YoY

-3.0% in last update

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Likely the New Normal vs 2019 – Keeping Commuter Traffic Down

- The back-to-office barometer is not changing materially in most markets.
- This could be the new normal relative to pre-pandemic levels.
- Any dramatic changes to the percentages of people going back to the office would change commuter volumes and increase fuel consumption in the process.

	Wed 11/9	Wed 11/16	% Change
Houston metro	56.6%	58.5%	1.9% ▲
San Francisco metro	41.6%	43.1%	1.6% ▲
Los Angeles metro	44.7%	46.1%	1.5% ▲
Average of 10	**47.5%**	**48.1%**	**0.6%** ▲
Austin metro	62.2%	62.7%	0.5% ▲
San Jose metro	37.5%	37.0%	0.5% ▼
New York metro	47.2%	47.6%	0.4% ▲
Dallas metro	53.8%	54.0%	0.3% ▲
Philadelphia metro	40.9%	41.2%	0.3% ▲
Washington D.C. metro	44.7%	44.6%	0.2% ▼
Chicago metro	46.0%	46.0%	0.1% ▲

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20 Countries Remain In Contraction

- **In December, 20 countries/regions had manufacturing sectors in contraction (unchanged from last month).**
  - All major producer markets except India and Mexico in contraction
  - 10 had services sectors in contraction in November (signaling broader economic pressure)

- **S&P Global PMI shows US manufacturing contraction (includes a smaller percentage of public spending than the ISM PMI)**

- **Manufacturing themes in December:**
  - Global new order demand was falling quickly across every region
  - But some input costs were still rising
  - Manufacturer product output prices were dropping amid discounting to spur demand
    - This combination could pressure manufacturer profits
  - Inventories remained stable, but inventory building activity is expected to slow amid concerns over demand in 2023

Country	Current Month	Latest Month Manuf. PMI	Prior Month Manuf. PMI	M/M Change
Global PMI	Dec	48.6	48.8	-0.2
Eurozone PMI	Dec	47.8	47.1	0.7
US	Dec	46.2	47.7	-1.5
China	Dec	49.0	49.4	-0.4
Canada	Dec	49.2	49.6	-0.4
Mexico	Dec	51.3	50.6	0.7
Japan	Dec	48.8	49.0	-0.2
Germany	Dec	47.1	46.2	0.9
South Korea	Dec	48.2	49.0	-0.8
UK	Dec	45.3	46.5	-1.2
France	Dec	49.2	48.3	0.9
India	Dec	57.8	55.7	2.1
Italy	Dec	48.5	48.4	0.1
Taiwan	Dec	44.6	41.6	3.0
Brazil	Dec	44.2	44.3	-0.1
Spain	Dec	46.4	45.7	0.7
Russia	Dec	53.0	53.2	-0.2
Netherlands	Dec	48.6	46.0	2.6
Ireland	Dec	48.7	48.7	0.0
Greece	Dec	47.2	48.4	-1.2
Poland	Dec	45.6	43.4	2.2
ASEAN	Nov	50.7	51.6	-0.9
Vietnam	Dec	46.4	47.4	-1.0
Philippines	Dec	53.1	52.7	0.4
Australia	Dec	50.2	51.3	-1.1
Switzerland	Dec	54.1	53.9	0.2
Hong Kong	Nov	48.7	49.3	-0.6
Singapore	Nov	56.2	57.7	-1.5

Source: Markit and Various Global Reporting Agencies/Banks

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Spending has Started, Manufacturing Construction 33.5% Higher Y/Y On $112B In Total Spending

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- Manufacturing construction activity among the fastest non-infrastructure sectors growing.
- Some of the manufacturing re-shoring speculation is starting to show up in real spending – manufacturing construction spending up 33.5% year-over-year. There are big pockets of demand out in the marketplace.
- Infrastructure spending also picking up pace.

Type of Construction	Oct 2022[p]	Sep 2022[r]	Oct 2021	Percent change Oct 2022 from - Sep 2022	Percent change Oct 2022 from - Oct 2021
Total Construction	**1,794,949**	**1,800,105**	**1,644,332**	**-0.3**	**9.2**
Residential	896,505	899,328	825,903	-0.3	8.5
Nonresidential	898,444	900,777	818,428	-0.3	9.8
Manufacturing	111,618	115,451	83,632	-3.3	33.5
Water supply	25,470	25,660	19,140	-0.7	33.1
Commercial	117,411	117,924	95,950	-0.4	22.4
Lodging	19,125	18,882	15,655	1.3	22.2
Sewage and waste disposal	32,706	33,061	28,051	-1.1	16.6
Amusement and recreation	28,186	27,475	25,026	2.6	12.6
Highway and street	114,273	115,096	102,161	-0.7	11.9
Conservation and development	9,114	9,040	8,171	0.8	11.5
Public safety	11,736	11,556	10,601	1.6	10.7
Health care	52,410	52,207	48,655	0.4	7.7
Educational	98,218	97,817	93,380	0.4	5.2
Transportation	56,597	56,633	55,314	-0.1	2.3
Office	87,138	86,891	86,352	0.3	0.9
Communication	24,849	24,707	24,777	0.6	0.3
Religious	2,835	3,148	2,889	-9.9	-1.9
Power	106,758	105,229	118,677	1.5	-10.0

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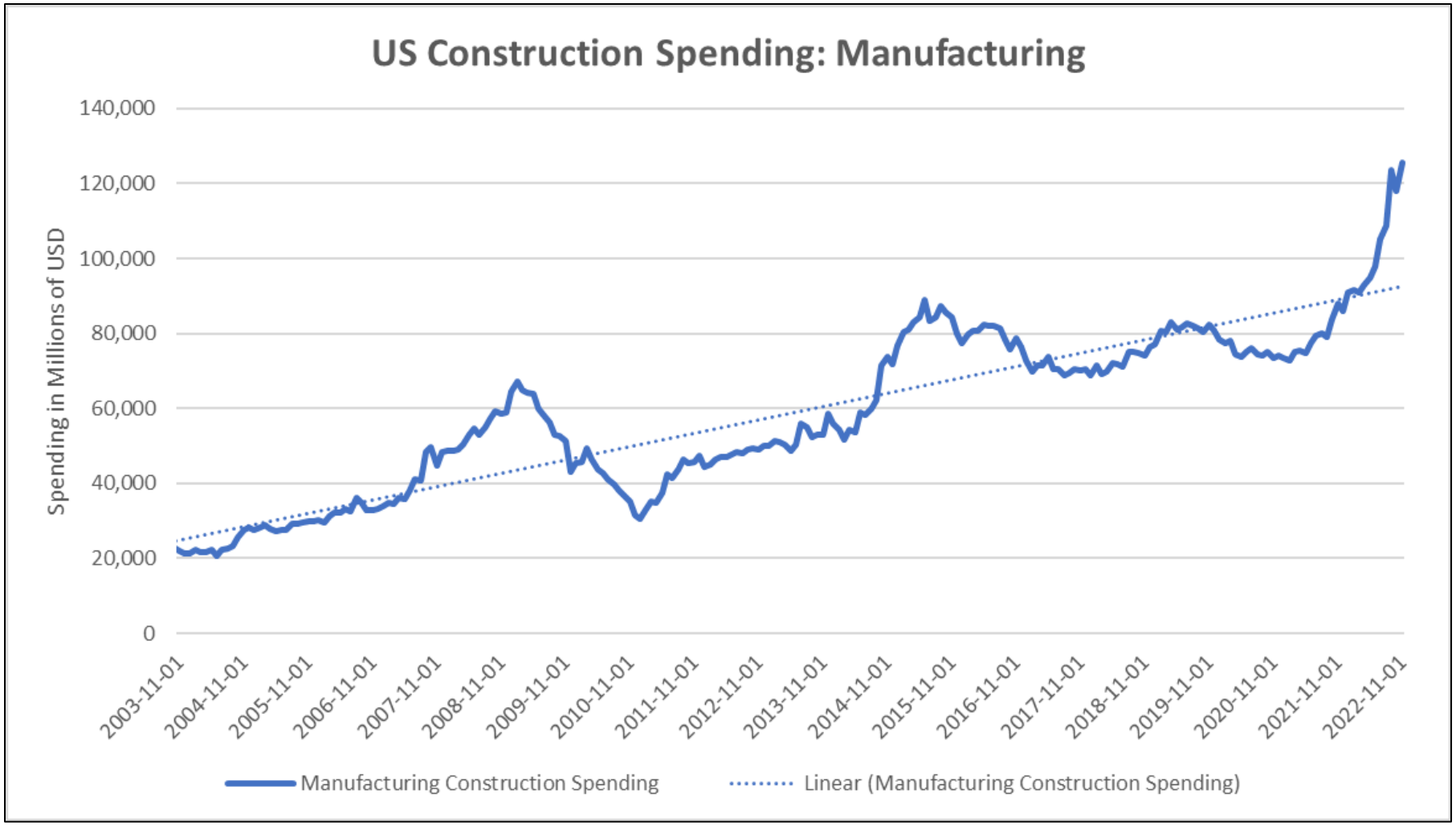
Source: Census Bureau

Reshoring Debate – is it happening? The Data would seem to suggest it.

- Spending on manufacturing was up 42.9% Y/Y in November.
- Versus the 20-year trendline, it was significantly higher than the trend – suggesting that current spending is not typical (even in the midst of a difficult construction environment).
- Inflation did play a role here, but the increases in spending is indicative of a re-shoring period, even if (in a worst-case scenario) it does become short-lived.



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Oil Outlook Still Uncertain; Diesel Higher

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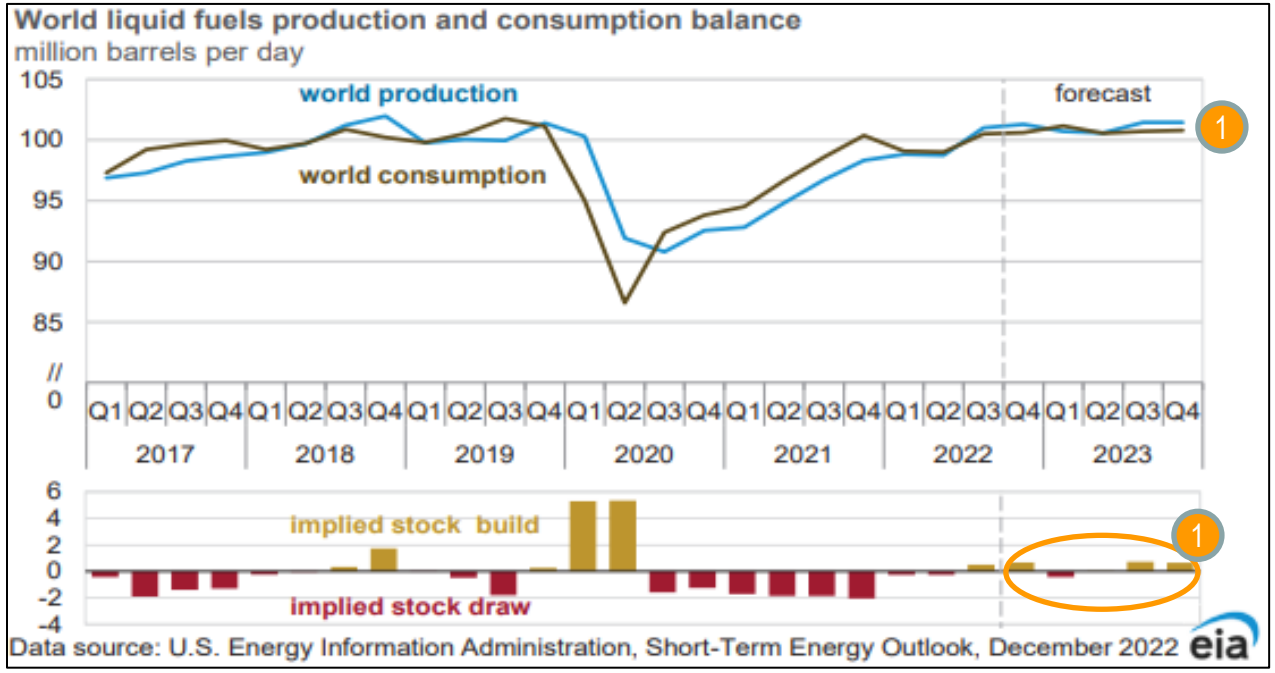
1. Implied net build through most of 2023 according to EIA. But:
   - US production will hit an all-time high next year of 13M Bpd
   - But, with commuter traffic cut off, consumption is still 20M Bpd currently
   - 7M Bpd gap must be imported
   - SPR releases (@1M Bpd) end in November?
   - The US will start rebuilding the SPR in 2023 and 2024

   - Concerns that global excess capacity is just 1.2% higher at this time, when China and Europe are largely consuming less.
     - Chinese imports of petroleum down 4.3% YTD
     - But in September, Chinese exports of refined fuels surged by 36% - lack of demand in China for the fuels



Crude forecast:	
2021	$68.21
2022	$95.22
2023	$86.36

Gasoline forecast:	
2021	$3.02
2022	$3.99
2023	$3.51

Diesel forecast:	
2021	$3.29
2022	$5.05
2023	$4.48

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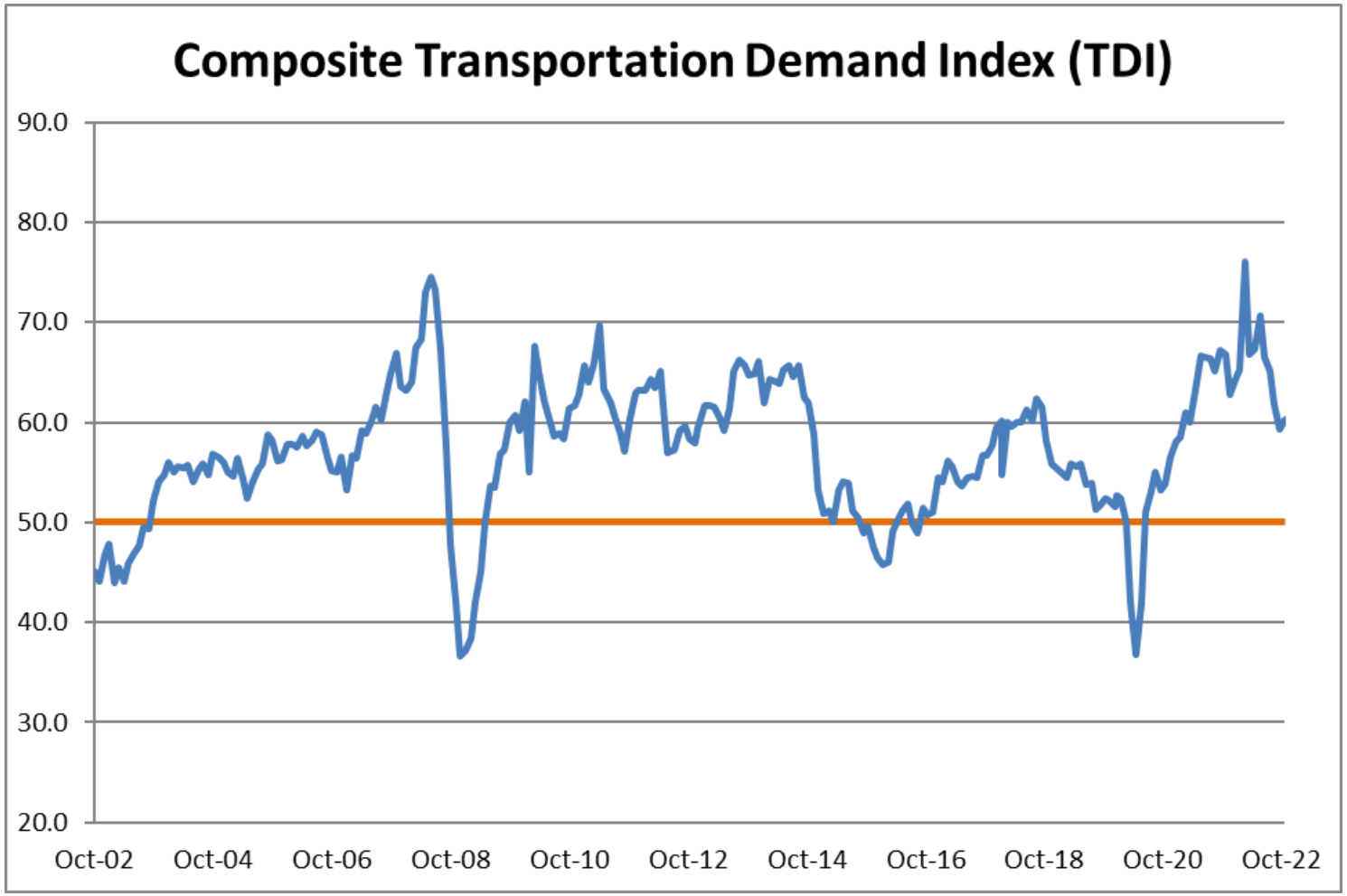
Source: EIA; Baker Hughes; Conoco-Philips

Transportation demand index falling back into a historically normal range

- Demand across the board stabilized slightly into seasonality between September and October.
- On a year-over-year basis, all of the modes were decelerating quickly against last year's strong (near historic) averages.
- Remember that 2018 was a strong demand environment for trucking, and the current TDI is returning into that range, still a solid story overall but decelerating.

	22-Oct	22-Sep	21-Oct	Y/Y Change %	M/M Change %
Composite	60.3	59.3	66.8	**-9.7%**	1.7%
Rail	57.8	57.5	64.2	**-10.0%**	0.5%
Trucking	60.6	59.5	66.9	**-9.4%**	1.8%
Air	63.1	63.1	74.3	**-15.1%**	0.0%
Maritime	61.2	61.6	72.6	**-15.7%**	**-0.6%**



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Unemployment Still Low – Fed Target is 4.5% - Which Is Still Low – Which Bodes Well for 2023 and 2024

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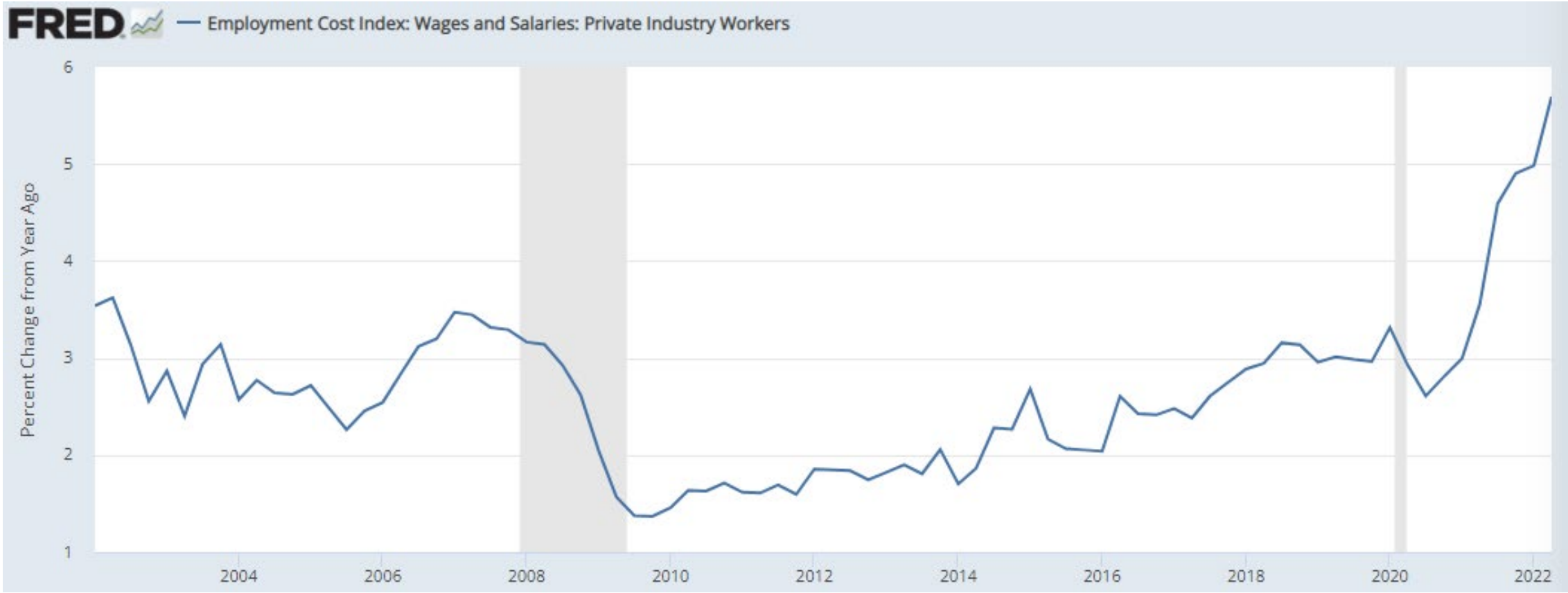
Labor Costs Are Sticky Inflation, Wages Rising Faster Than Any Time Since The Early 2000's

- Good for keeping a consumer consuming.
- Tougher for employers and maintaining profits.



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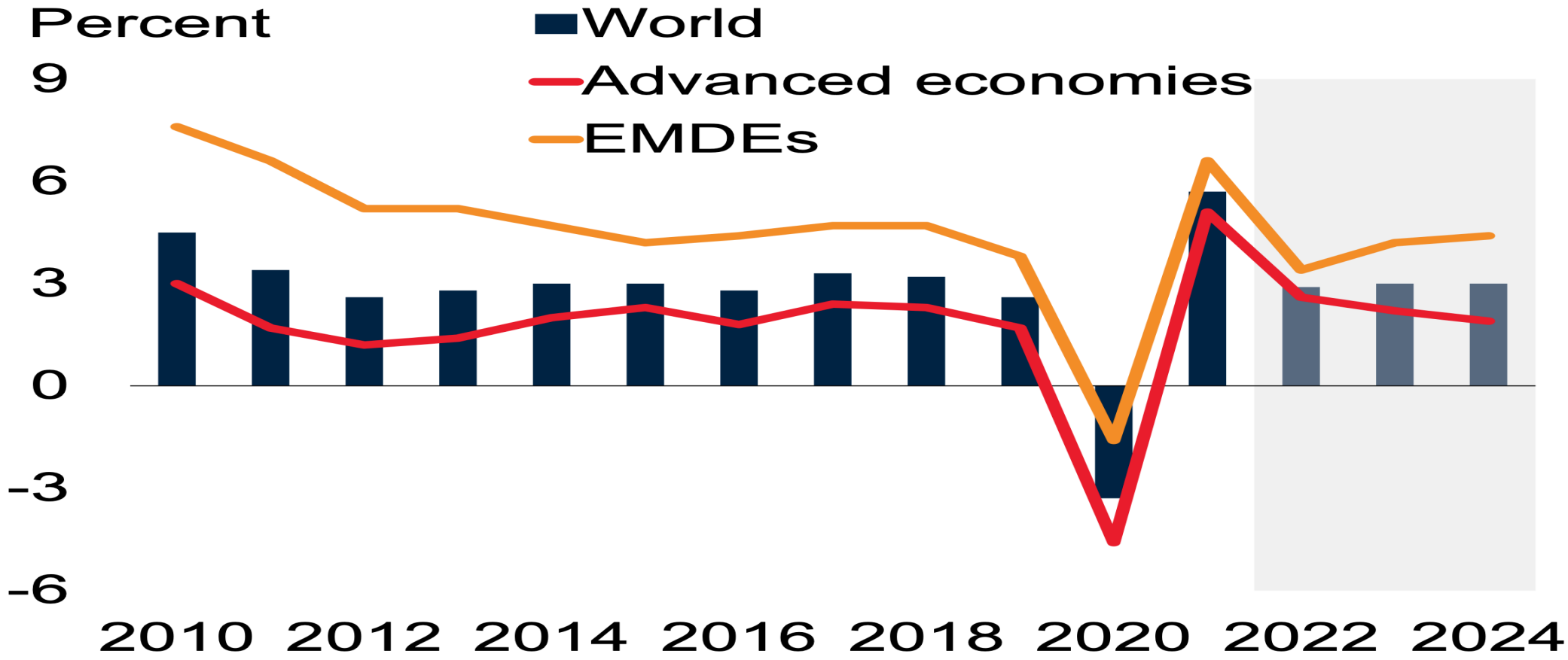
Not Expected to be Deep or Long Lasting



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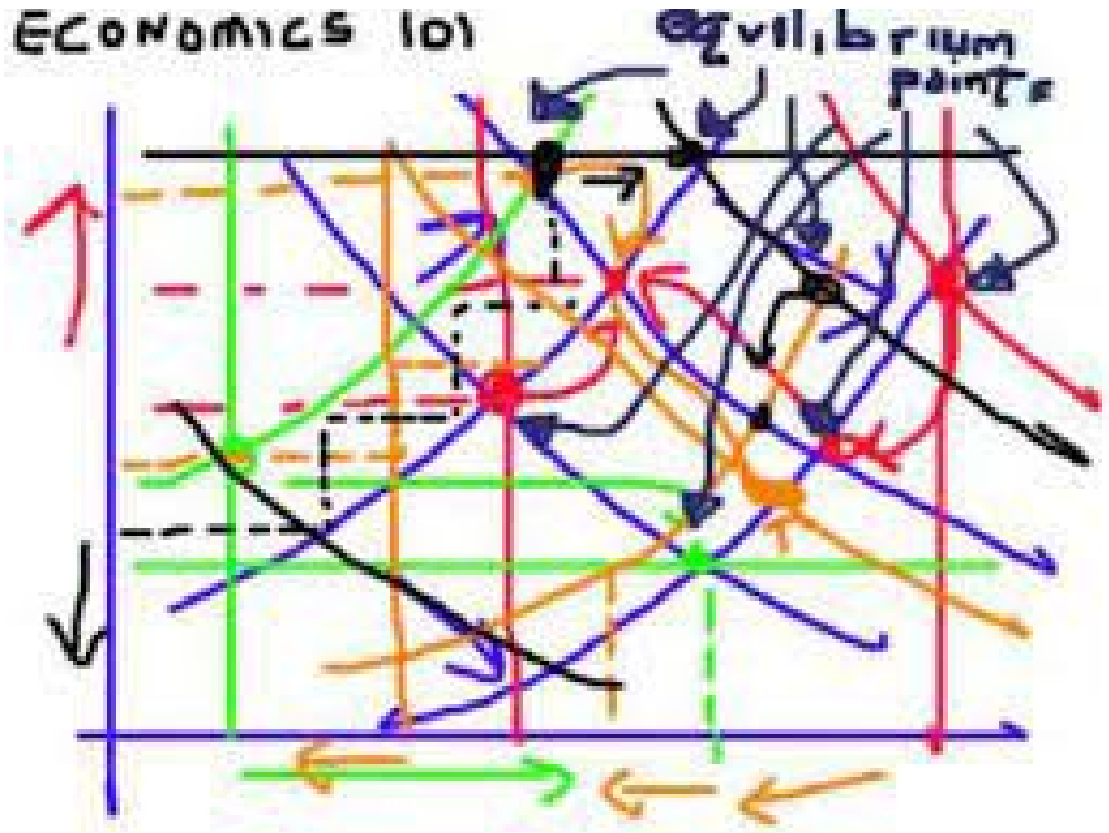
Which Way Are We Heading?



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