



Dazed & Confused

ACMA Summer Conference

July 14, 2023

Presented By:

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Elliott D. Pollack & Company
Court, Merritt, Pollack, & Stevenson

“The Federal Reserve...is in the position of the chaperone who has ordered the punch bowl removed just when the party was really warming up.”

William McChesney Martin,
Chairman, Federal Reserve
System

October 1955





The Party is Over

In fact, the Fed was late to the party and let things get out of hand with very low interest rates.

STAGFLATION



Are we headed towards a Recession?

Uncertain!!

- NBER's Definition – A recession involves a significant decline in economic activity that is spread across the economy and lasts more than a few months.
- It is normally visible in real GDP, real income, **employment**, industrial production and wholesale/retail trade and there are other signs/indicators as well.



High Interest Rates

- Housing is not the target of the Fed's actions. BUT IT IS THE TARGET.
- Other interest sensitive sectors include:
 - Commercial construction
 - Consumer durables such as autos
 - Business spending on plant and equipment
 - Commercial real estate and banking (which we are now experiencing)

History Repeats Itself

It's like déjà vu all over again.

- We have been here before but have not had a period of high inflation for 40+ years since the 1970's and 1980's.
- Inflation declined then but stayed high by today's standards throughout the 80's.
- Inflation this time around has been high for only the last six quarters.
- Therefore, it is much less ingrained in the economy and should be a "quicker" fix.
- High inflation is unfamiliar to most people because:
 - You have to be 60 years old or more to have experienced it in the past
 - You totally forgot about it
 - Or you weren't born



Historically, high inflation and recessions were caused by energy spikes.

More recent recessions have been caused by financial crises.

- 1990 Savings & Loan Crisis
- Dot.com bust
- Great Recession



Monetary Policy



Arthur Burns
Did Not Finish The Job
1970-1978



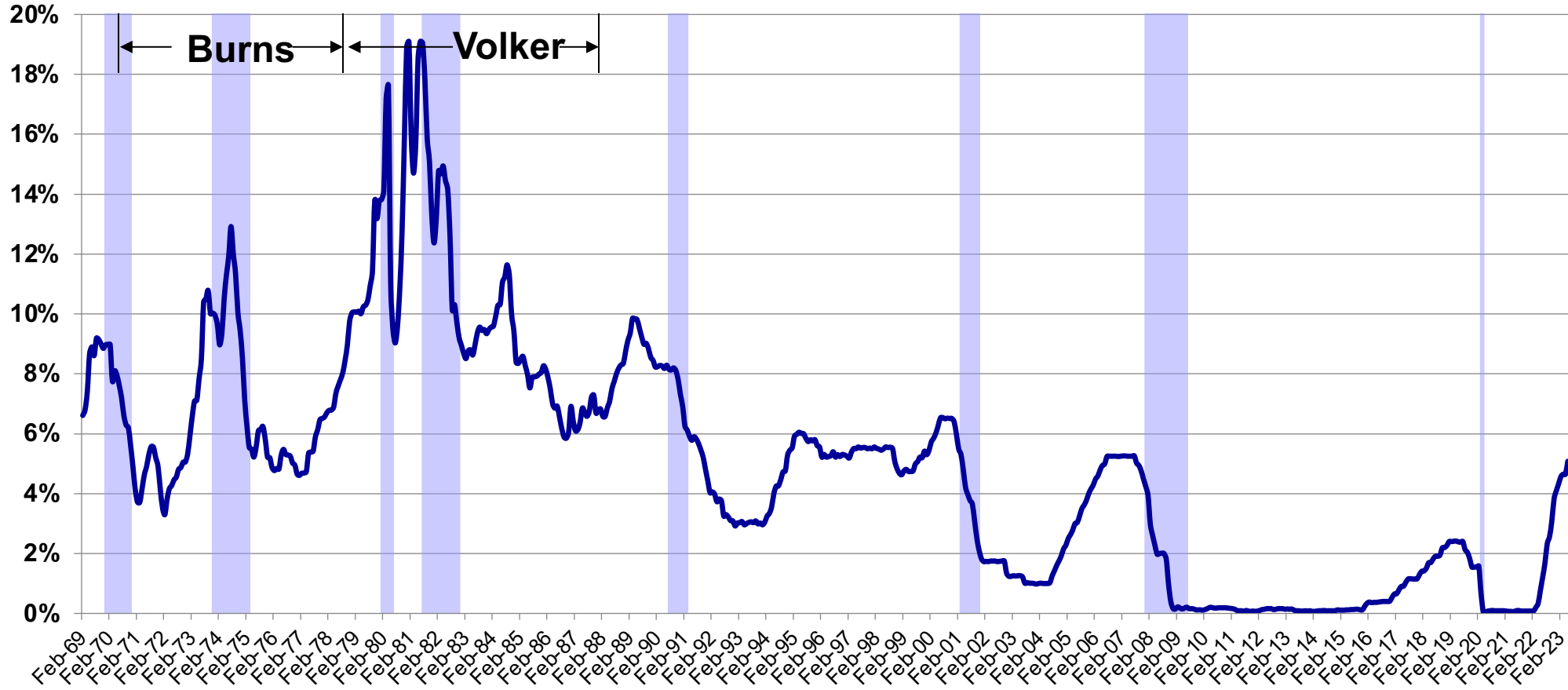
Paul Volcker
Finished the Job
1979-1987



Jerome Powell
To-be-determined
2018-?

Federal Funds Effective Rate 1968-2022

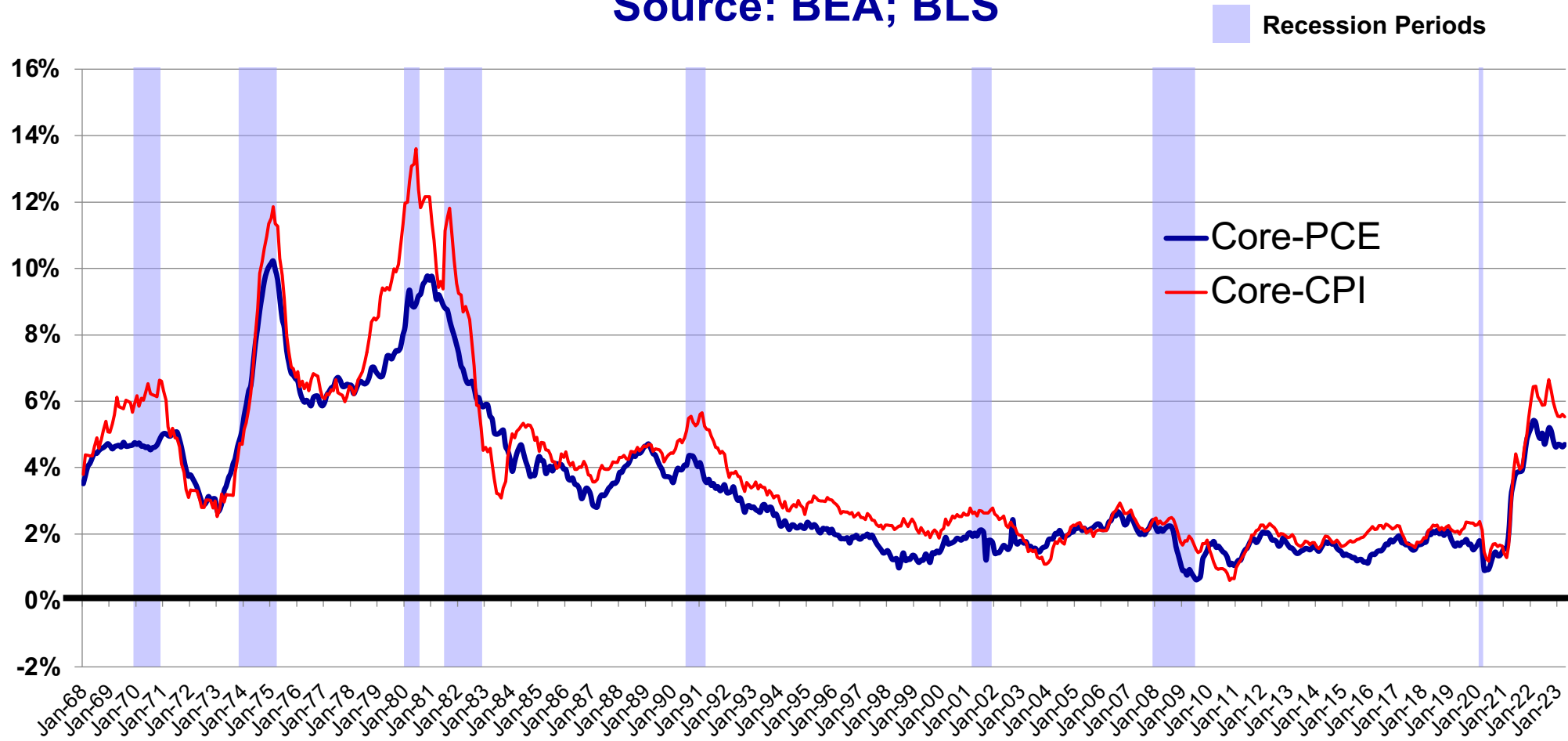
Source: BLS



Core-PCE and Core-CPI

% Change Y/Y

Source: BEA; BLS



The Last People at the Fed to Fight Inflation



Conflicting Economic Data



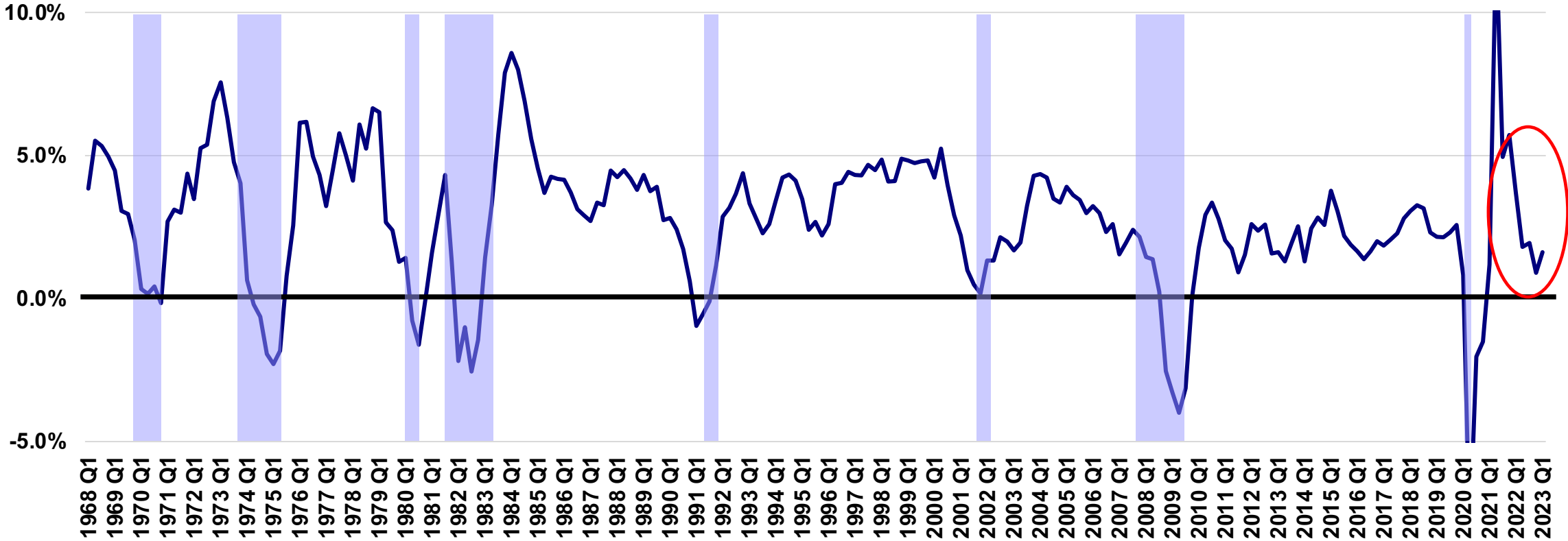
Real GDP

% Change Y/Y

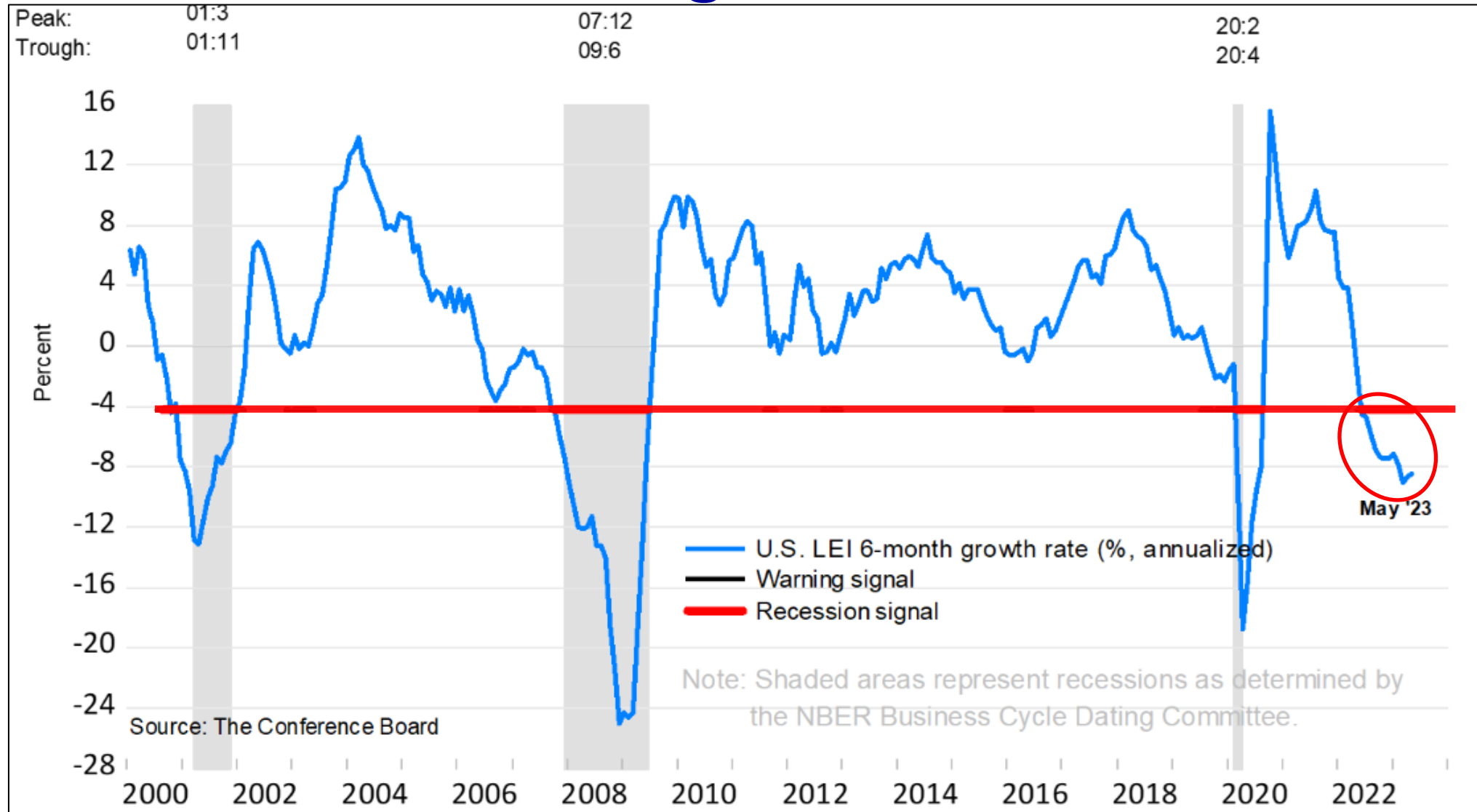
1968 – 2023

Source: BEA

Recession Periods



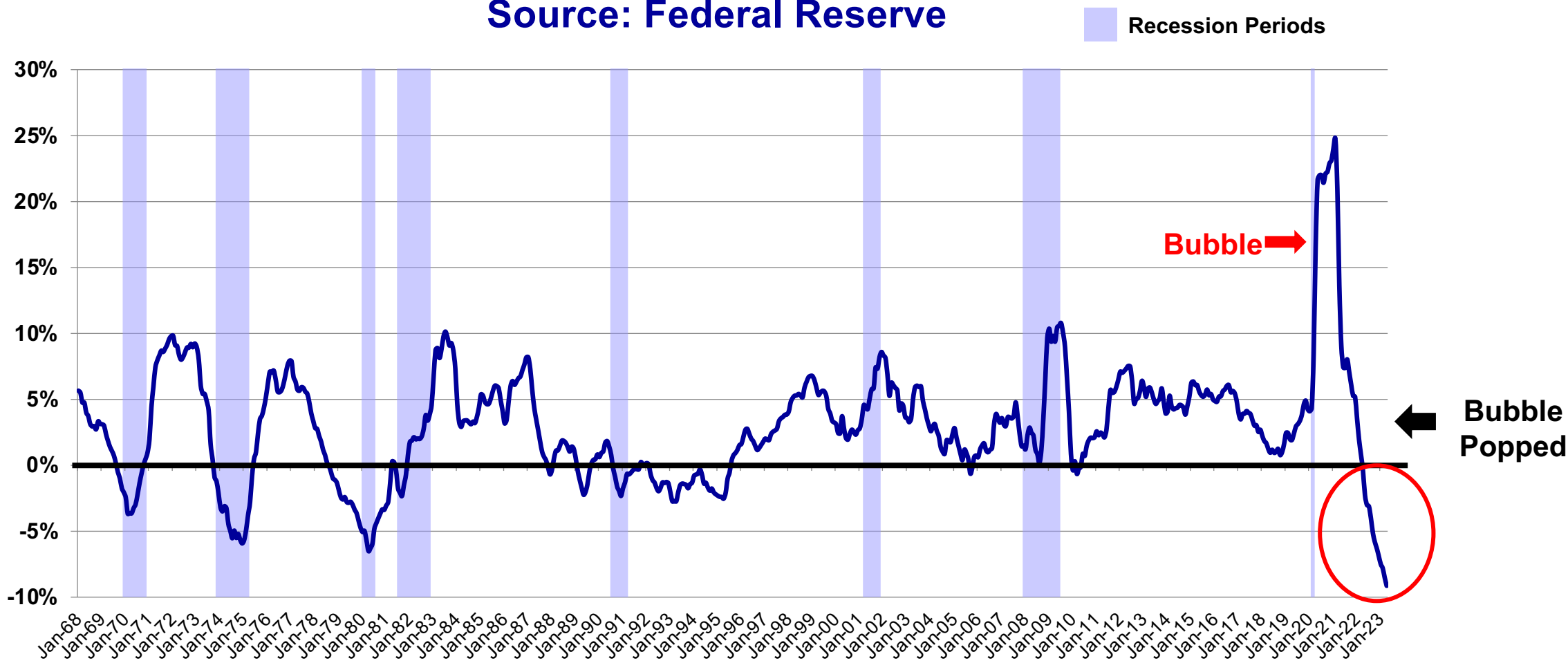
Leading Indicators



Real M2

% Change Y/Y

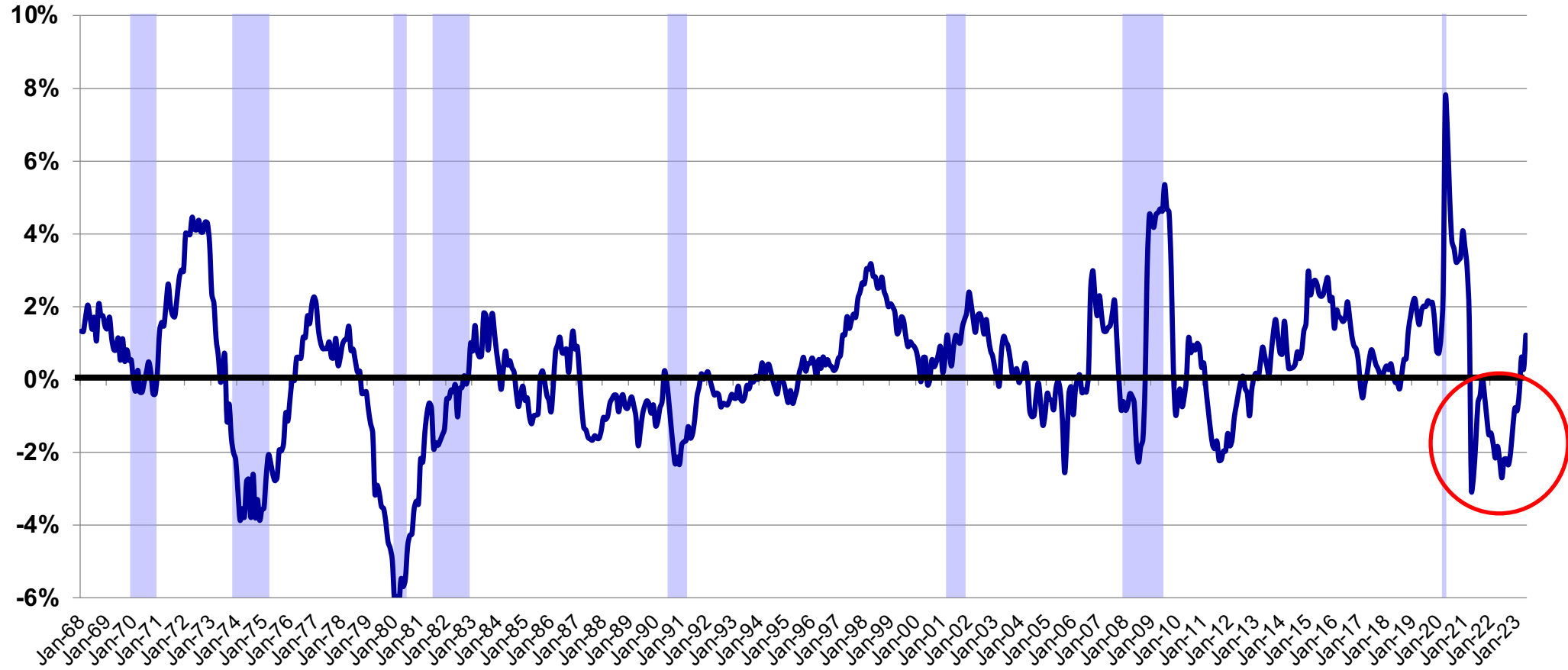
Source: Federal Reserve



Real Hourly Earnings Growth

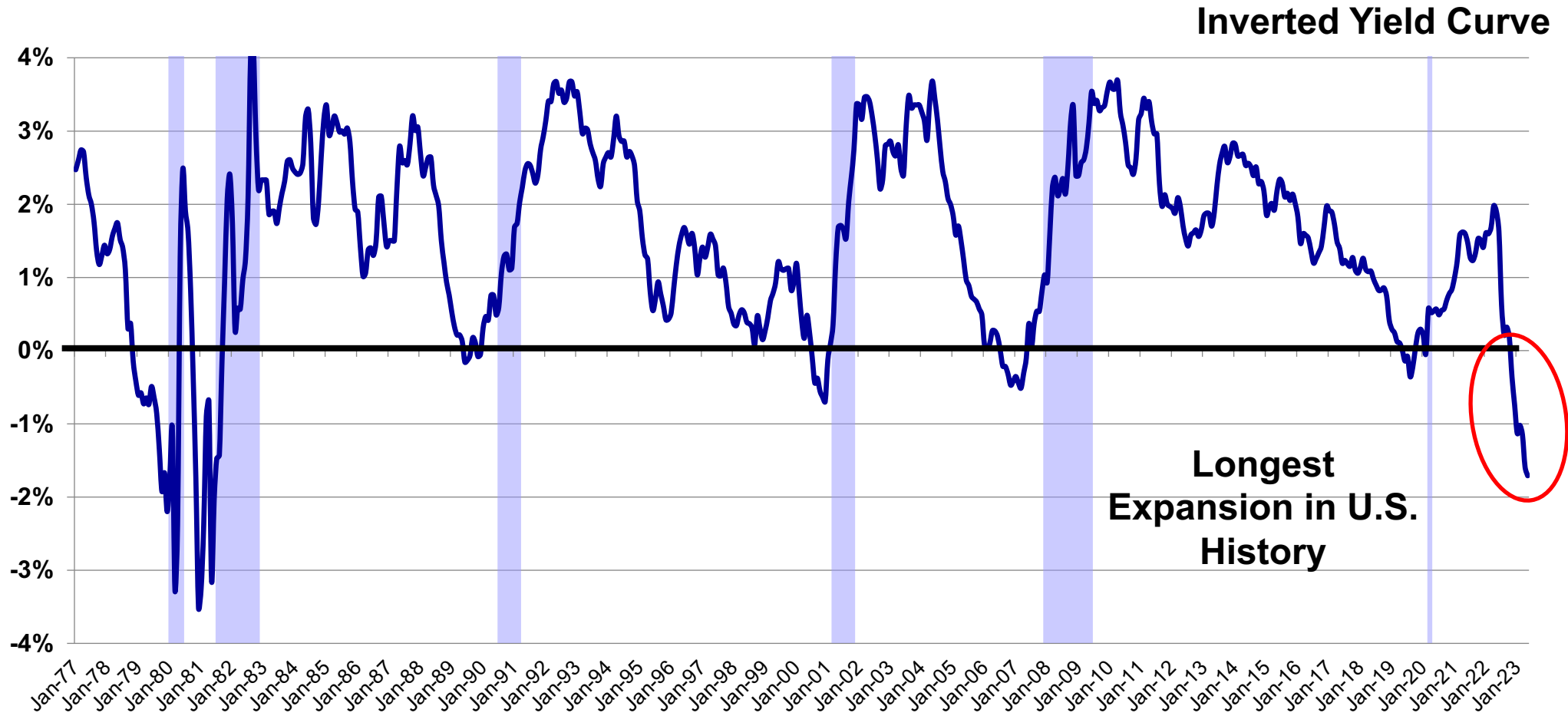
% Change Y/Y

Source: BLS



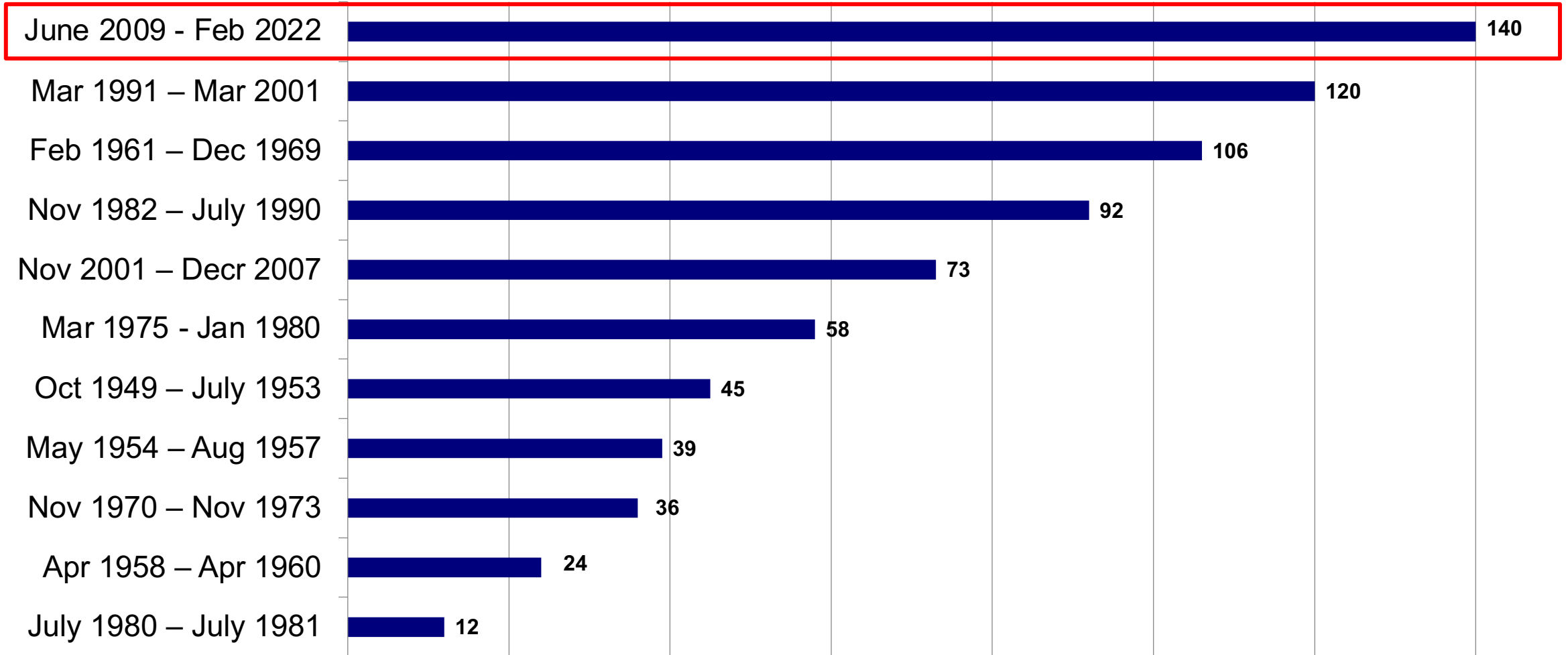
Treasury Spread 10-Year minus 3-month

Source: Federal Reserve



U.S. BUSINESS CYCLE EXPANSIONS

Source: National Bureau of Economic Research



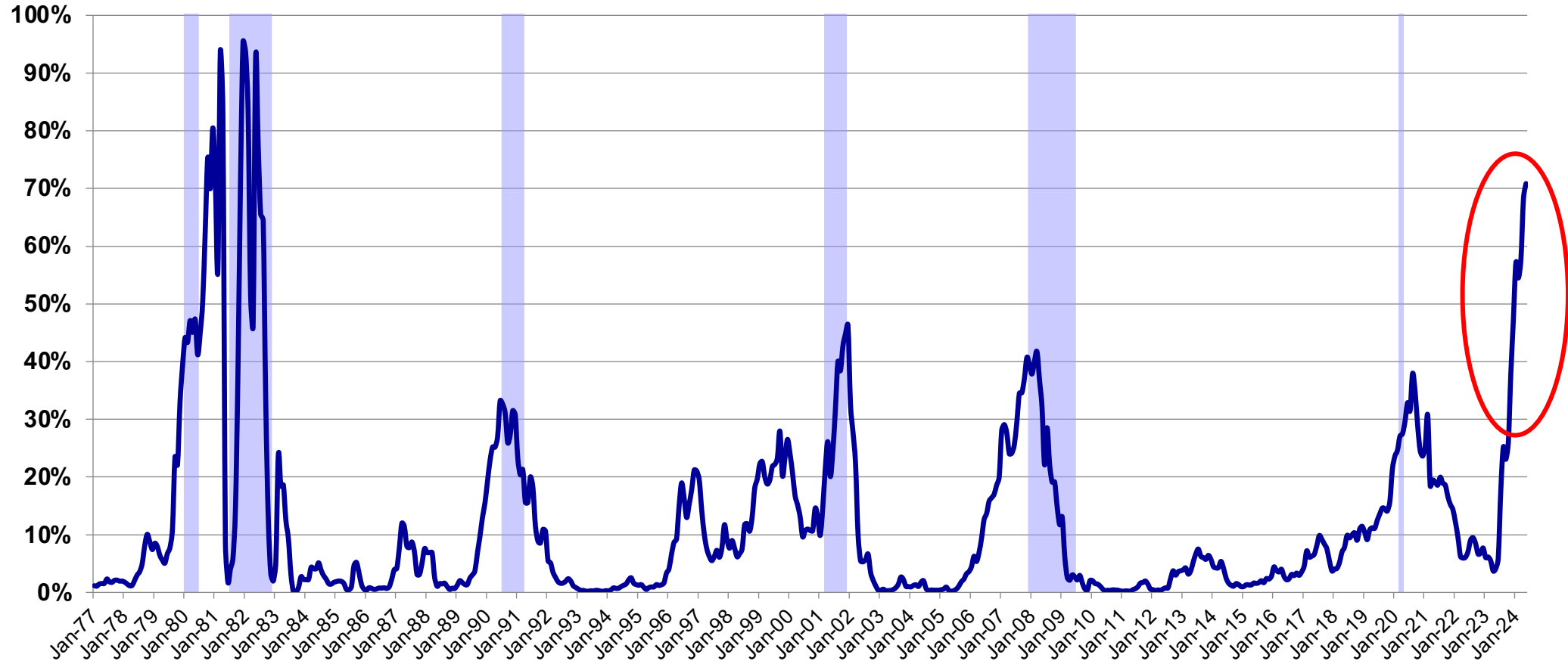
Expansions don't die of old age

They die because an economy becomes vulnerable to exogenous shocks or asset bubbles or a tightening in the credit market.



Treasury Spread Probability of Recession

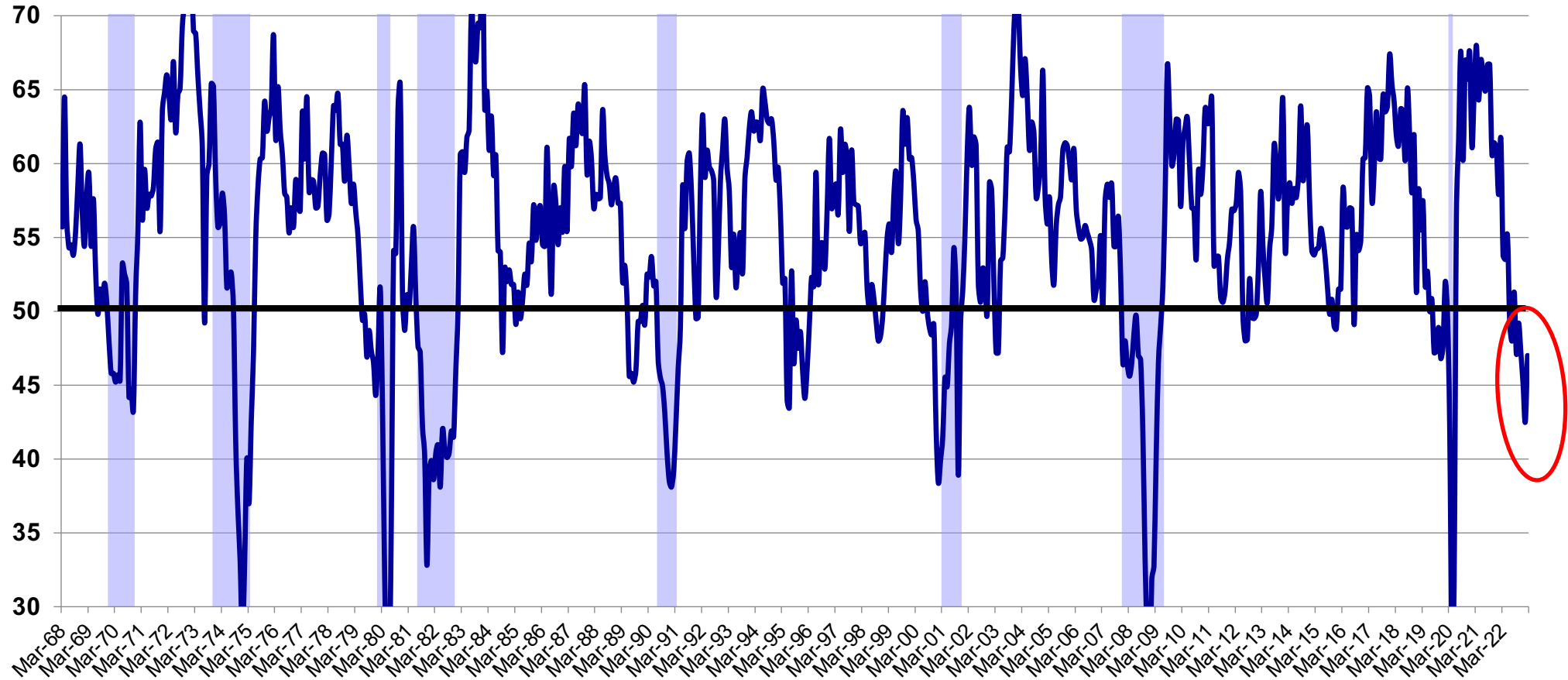
Source: Federal Reserve



ISM's Manufacturing PMI: New Orders

1968 – 2023*

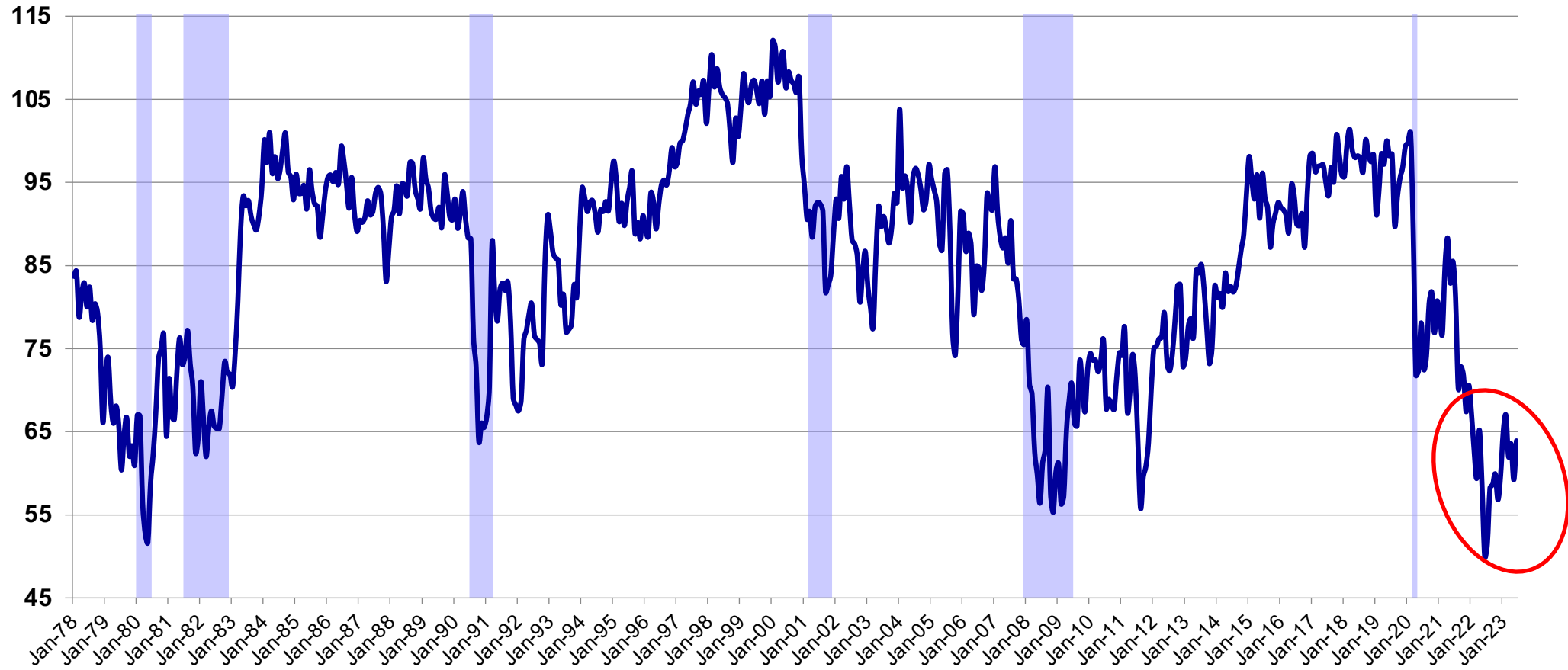
Source: ISM



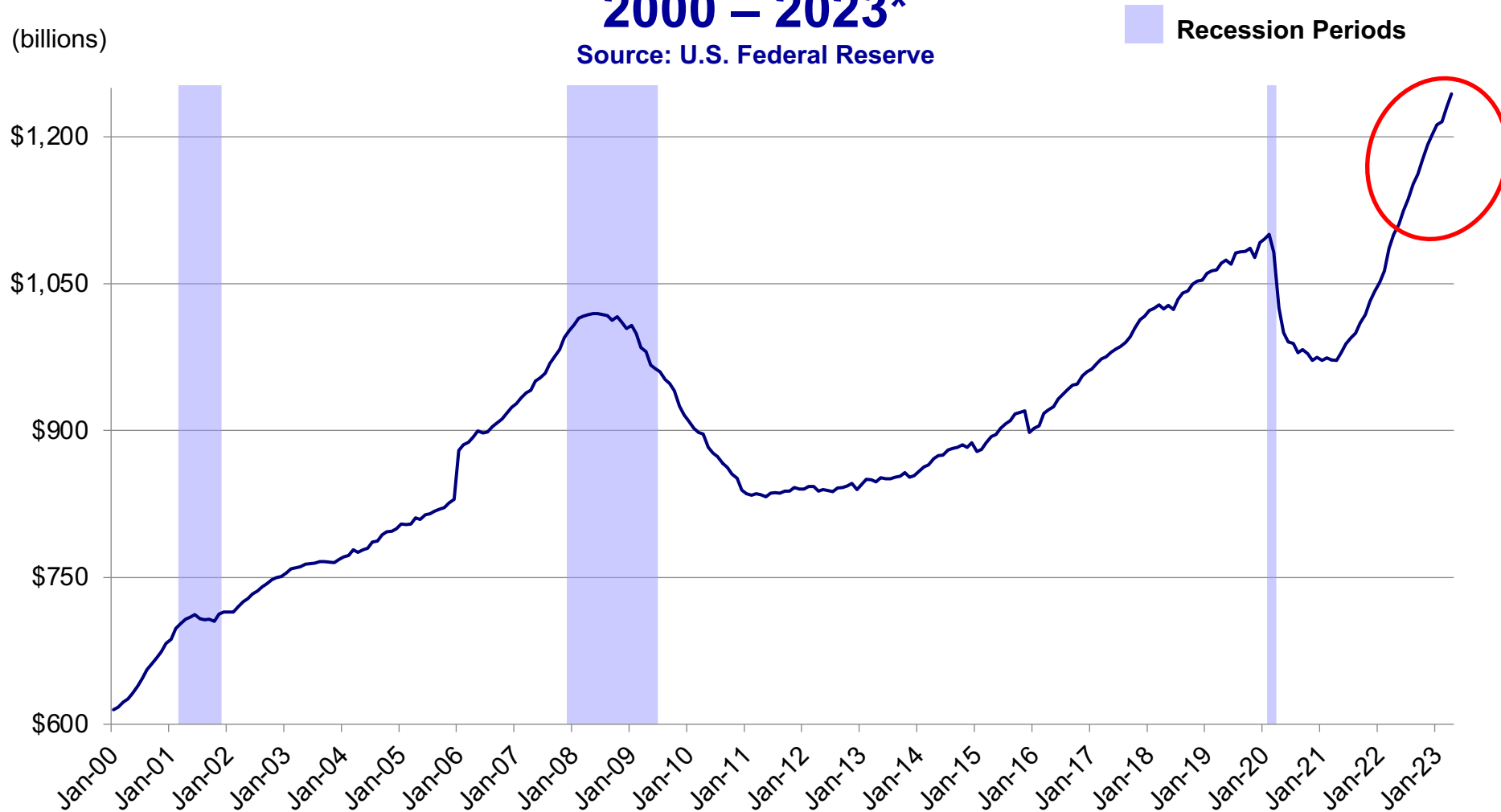
University of Michigan: Consumer Sentiment

1978 – 2023*

Source: University of Michigan



U.S. Consumer Credit Total Revolving Credit Outstanding 2000 – 2023*

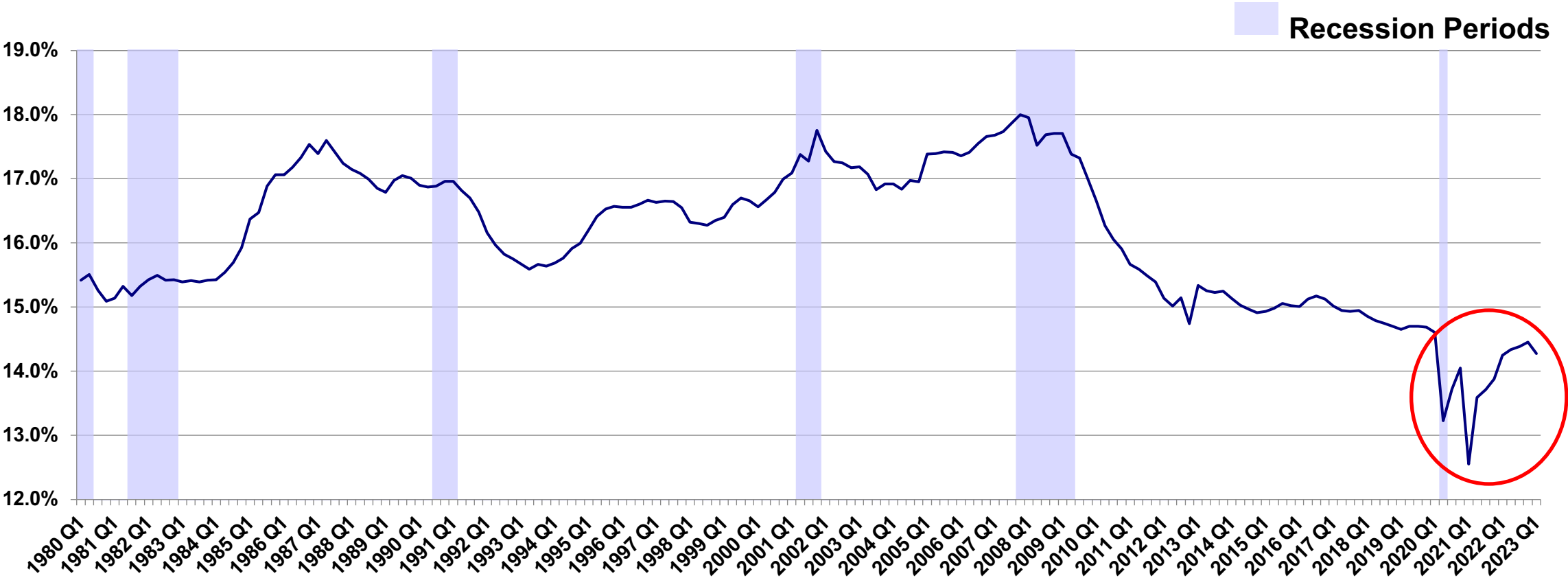


Revolving Credit Plans – may be unsecured or secured by collateral and allow a consumer to borrow up to a prearranged limit and repay the debt in one or more installments.

Financial Obligation's Ratio*

1980 – 2022**

Source: Federal Reserve

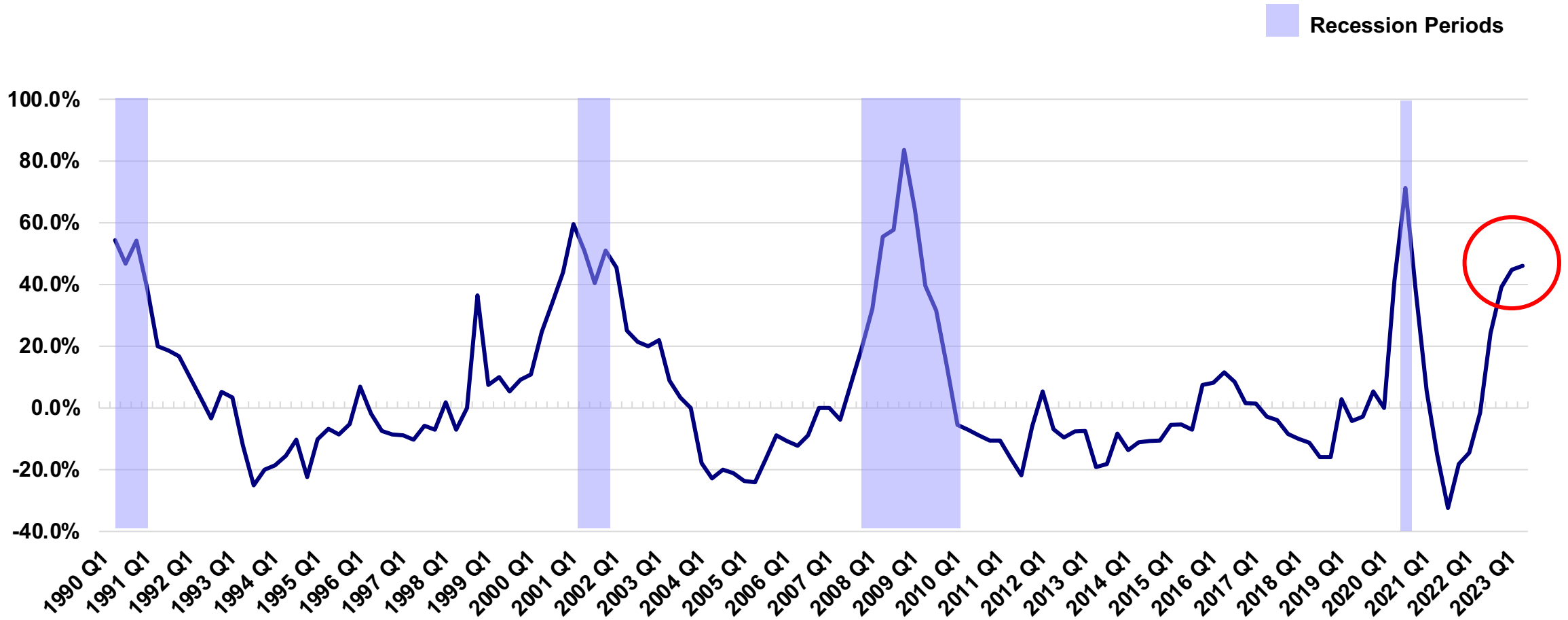


*Ratio of mortgage and consumer debt (including auto, rent and tax payments) to disposable income.

**Data through the first quarter 2023

Net Percentage of Domestic Banks Tightening Standards

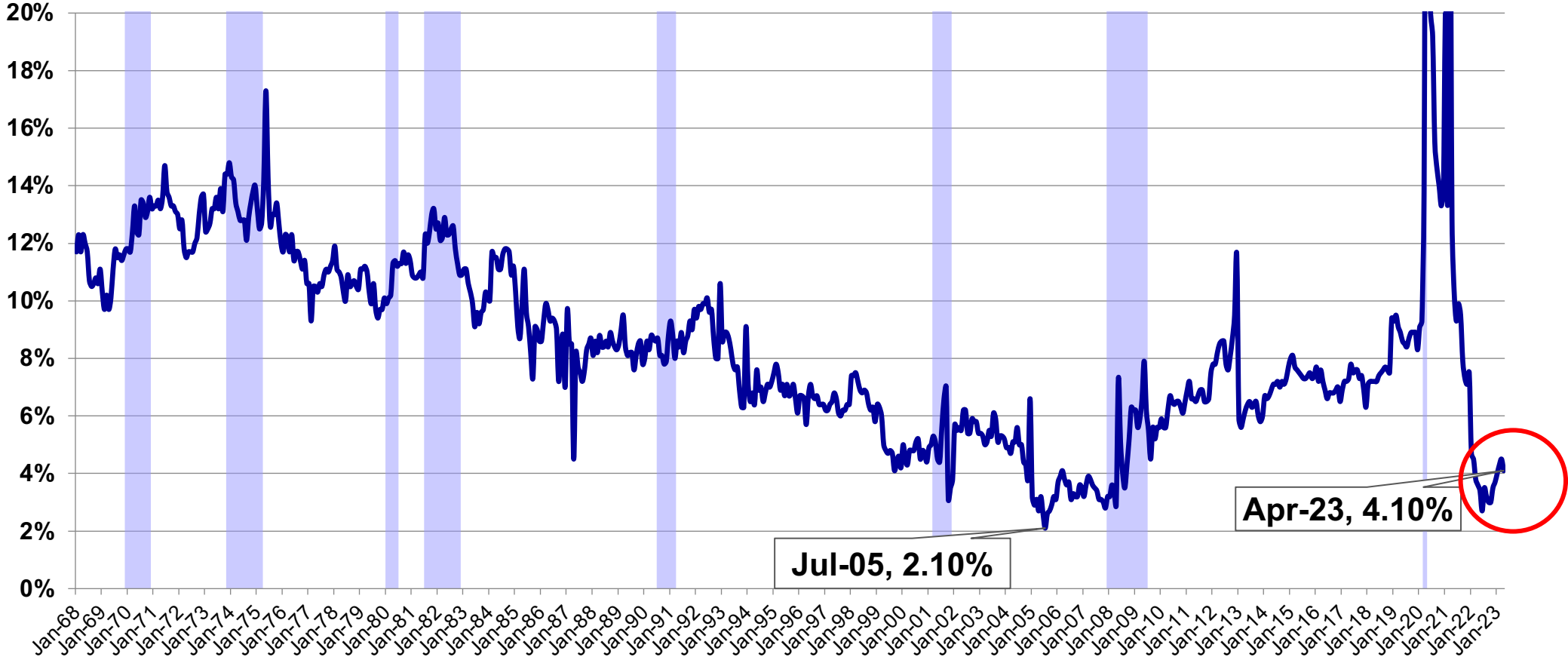
Source: Board of Governors of the Federal Reserve System



Savings Rate

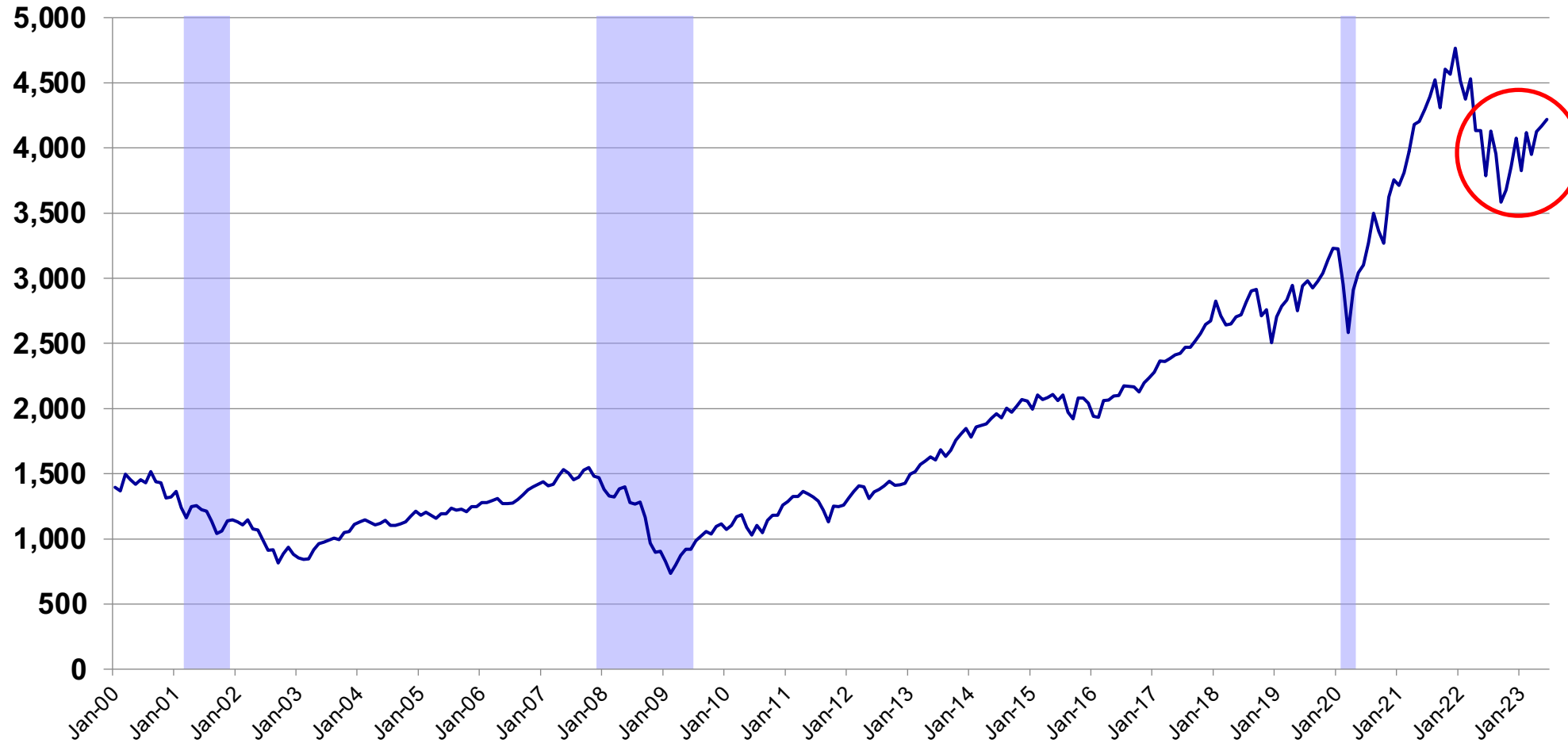
1968 - 2023

Source: BEA

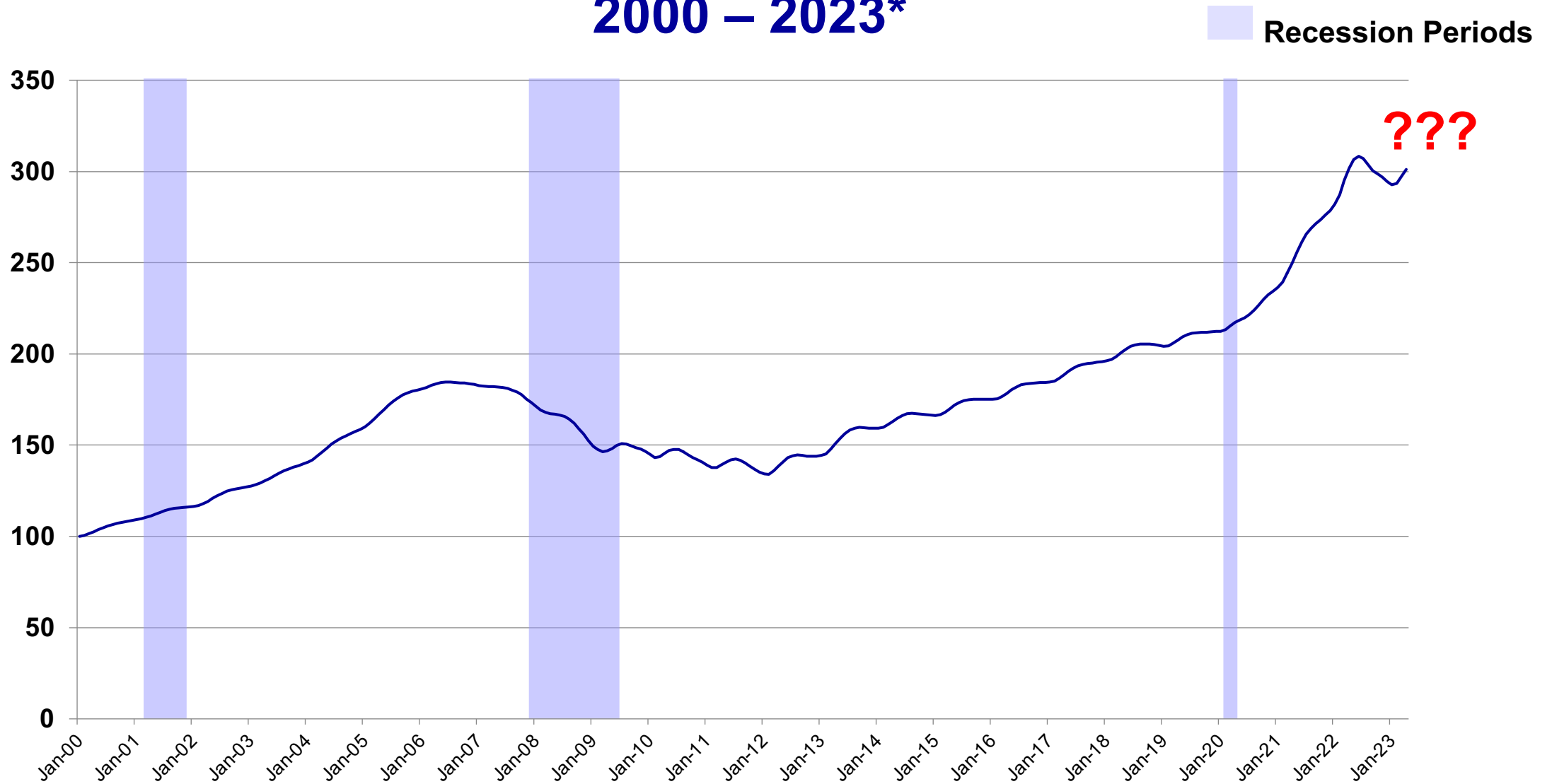


S&P 500 2000 – 2023*

Recession Periods



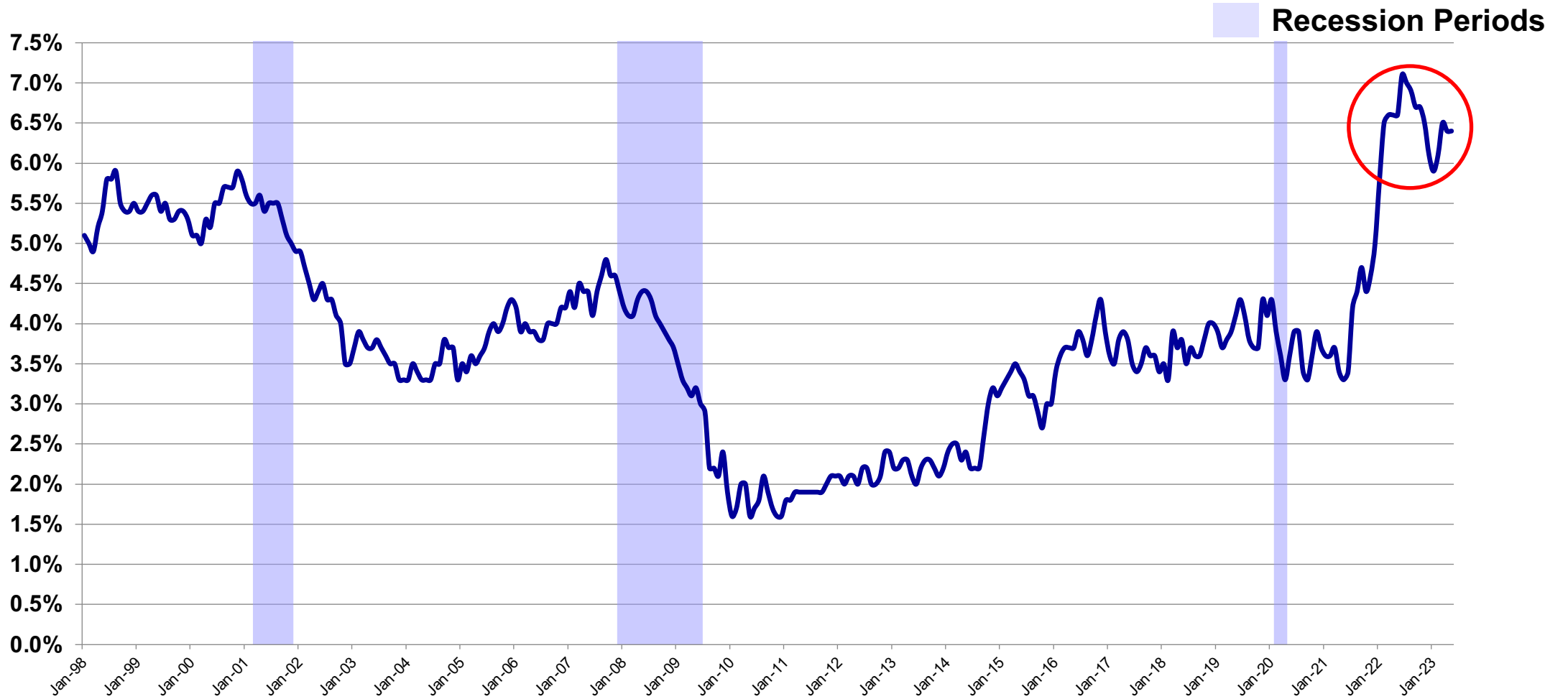
U.S. S&P/Case-Shiller Home Price Indices 2000 – 2023*



Weighted Overall Wage Growth Tracker, 3-Month Moving Average

1998 - 2023

Source: Current Population Survey, Bureau of Labor Statistics, and Federal Reserve Bank of Atlanta Calculations.



Real GDP Forecast

Blue Chip Economic Indicators

(June 2023)

Year	2023	2024
Average	1.2%	0.7%
Top 10	1.7%	1.7%
Bottom 10	0.8%	-0.1%

The average annual growth rate between 2010-2019 was 2.3%

Current Status

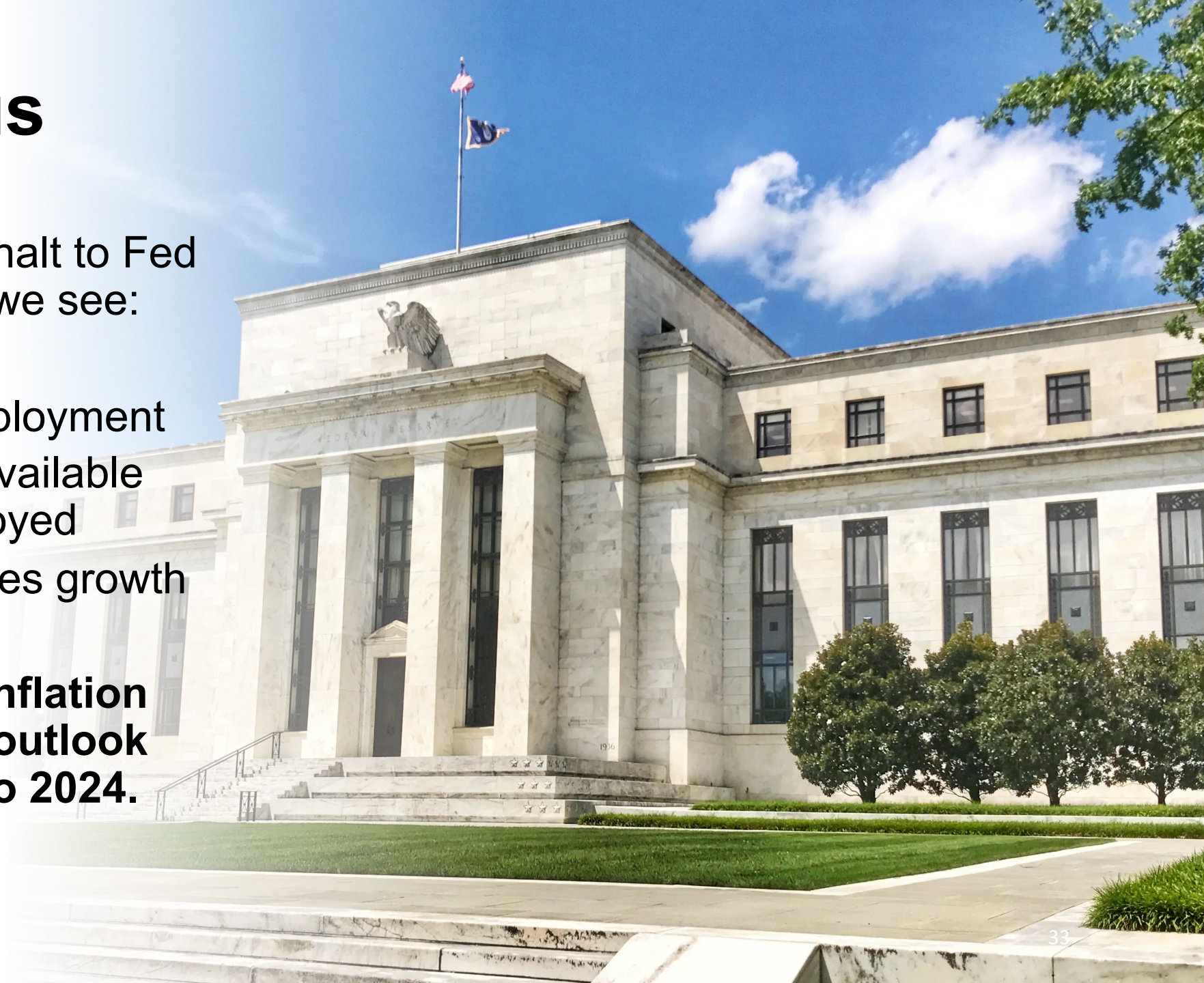
- We have never tried to induce a recession when:
 - there 10.1 million unfilled jobs and only 6.1 million unemployed.
 - the federal government created a situation where consumers almost have \$1.0 trillion dollars more in cash than normal.
- **These things combined with supply chain issues has made the economy more difficult to slow than under normal circumstances.**
- **Add a credit crunch to the mix and things become dicey.**

Current Status

We likely will not see a halt to Fed interest rate hikes until we see:

- A slowdown in hiring
- An increase in unemployment
- A balance between available jobs and the unemployed
- A slowing of retail sales growth

The effort to reduce inflation requires a long-term outlook extending at least into 2024.



The Fed's Task

A SOFT LANDING

- Unemployment increases, inflation declines to the Fed's goal, and we avoid a recession, or a recession is mild.

A HARD LANDING

- The Fed affects unemployment more measurably resulting in a more difficult recession.

In either case, the Fed must stay the course and rein in inflation or we could have a repeat of the 1970's early 1980's.



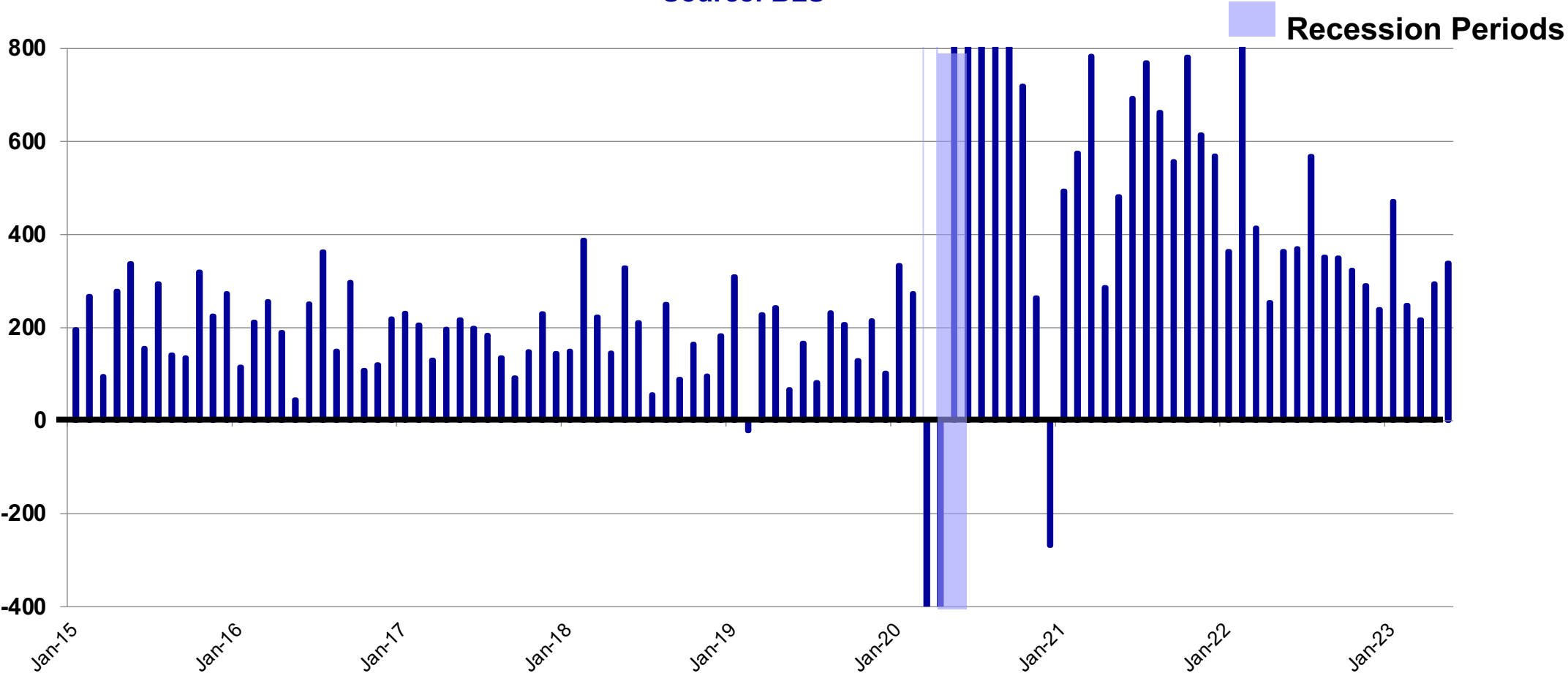


**Are we at the
beginning of
job
disruptions?**

Total Non-farm Employment

Net Monthly Change

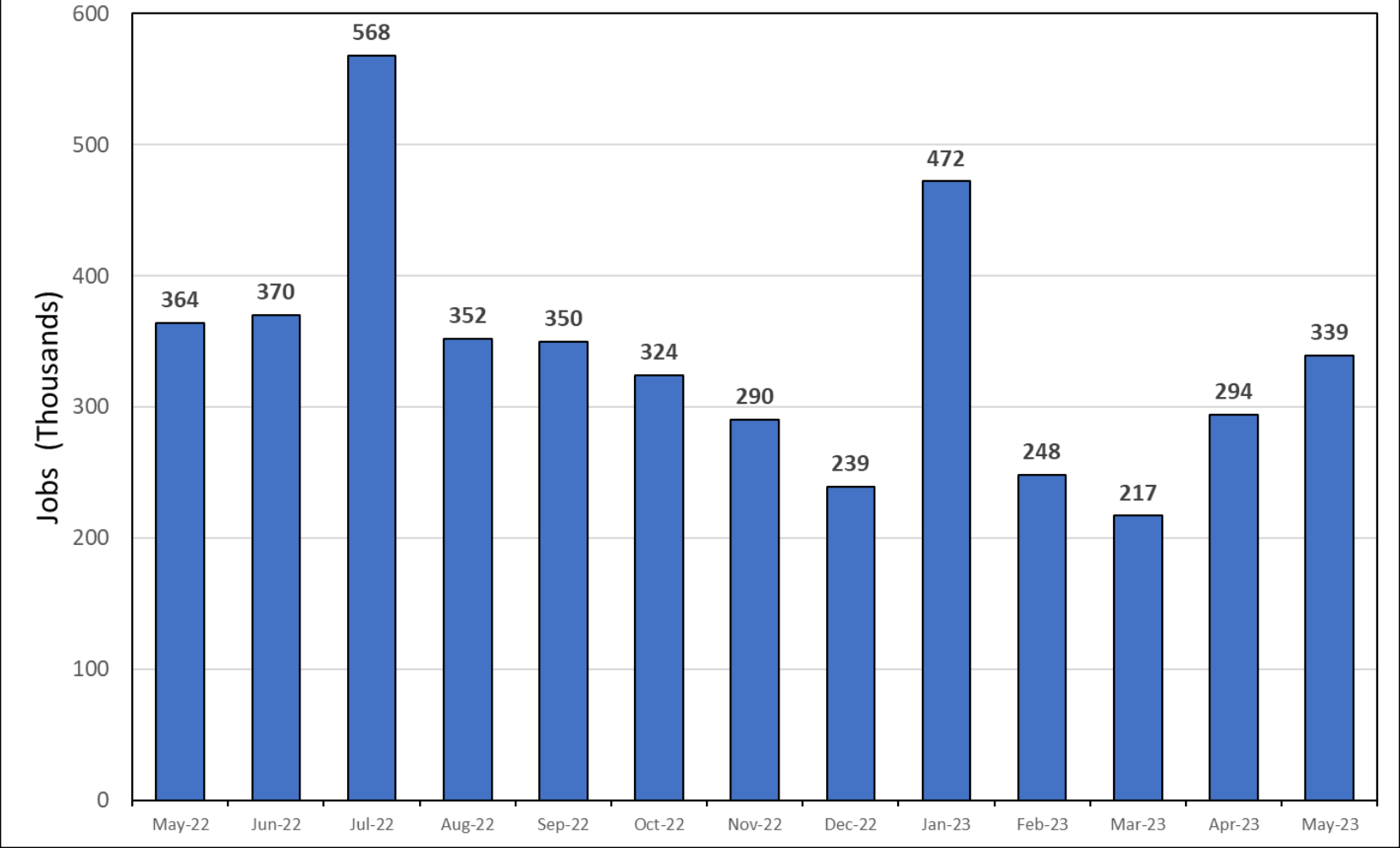
Source: BLS



Total Non-farm Employment in Last Year

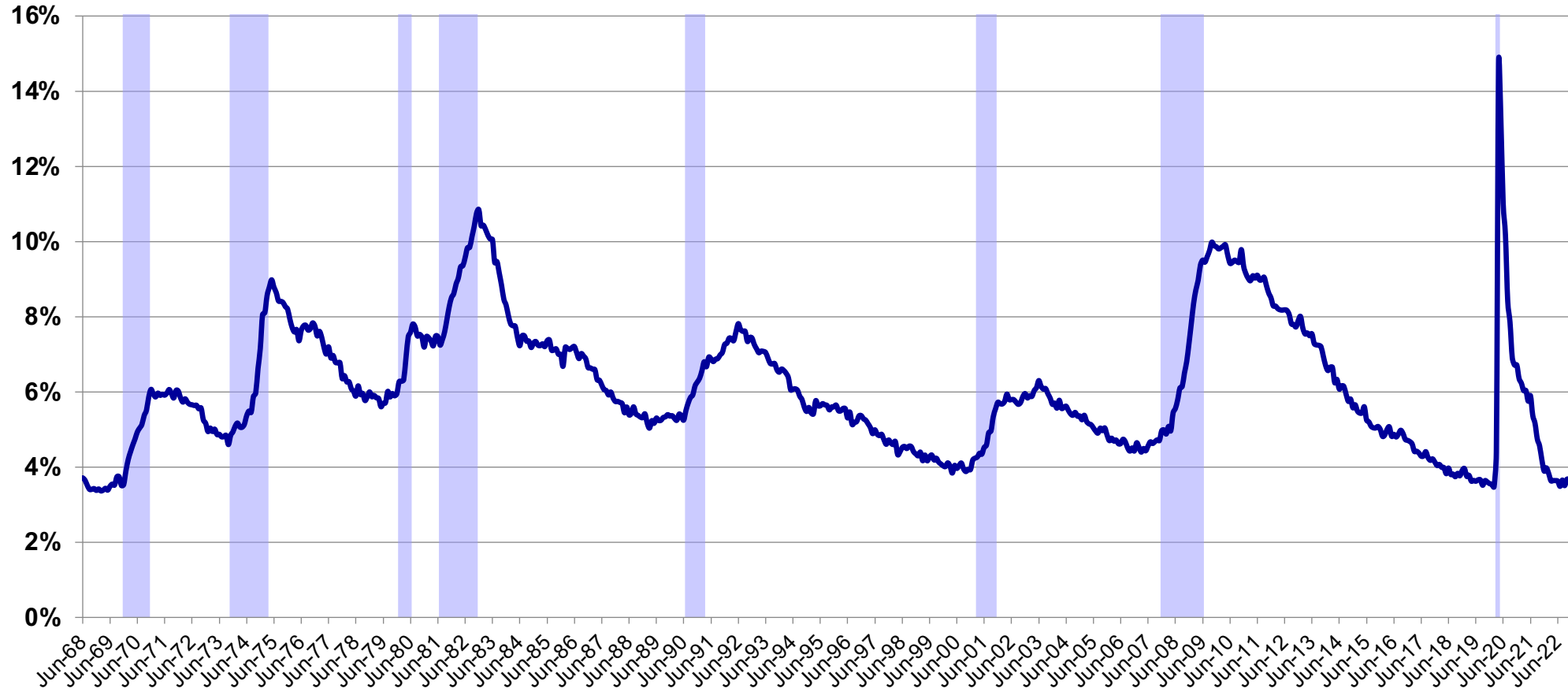
Net Monthly Change

Source: BLS



Unemployment Rate (U-3) 1968-2023

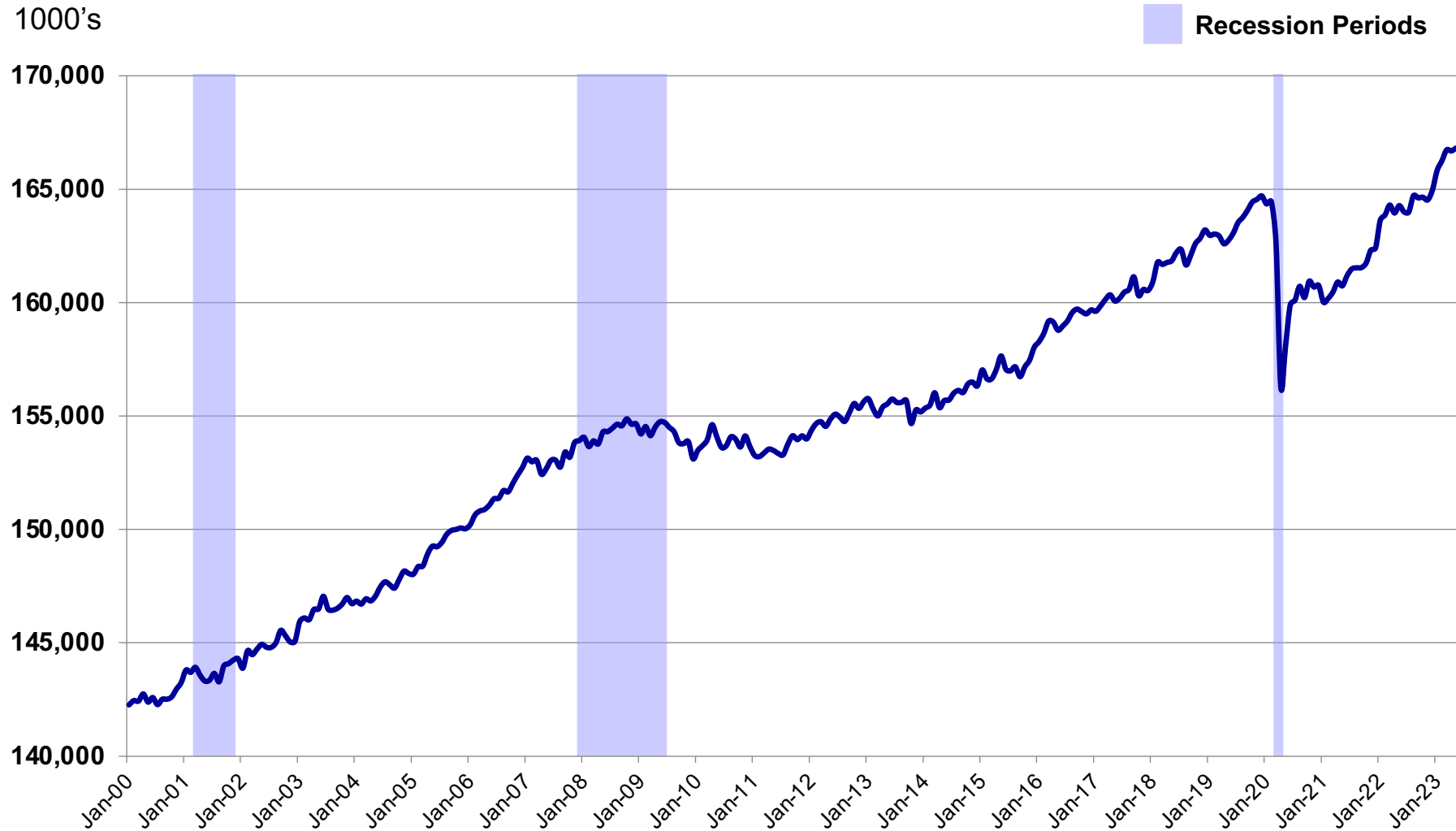
Source: BLS



Labor Force (S/A)

2000 – 2023*

Source: U.S. Bureau of Labor Statistics

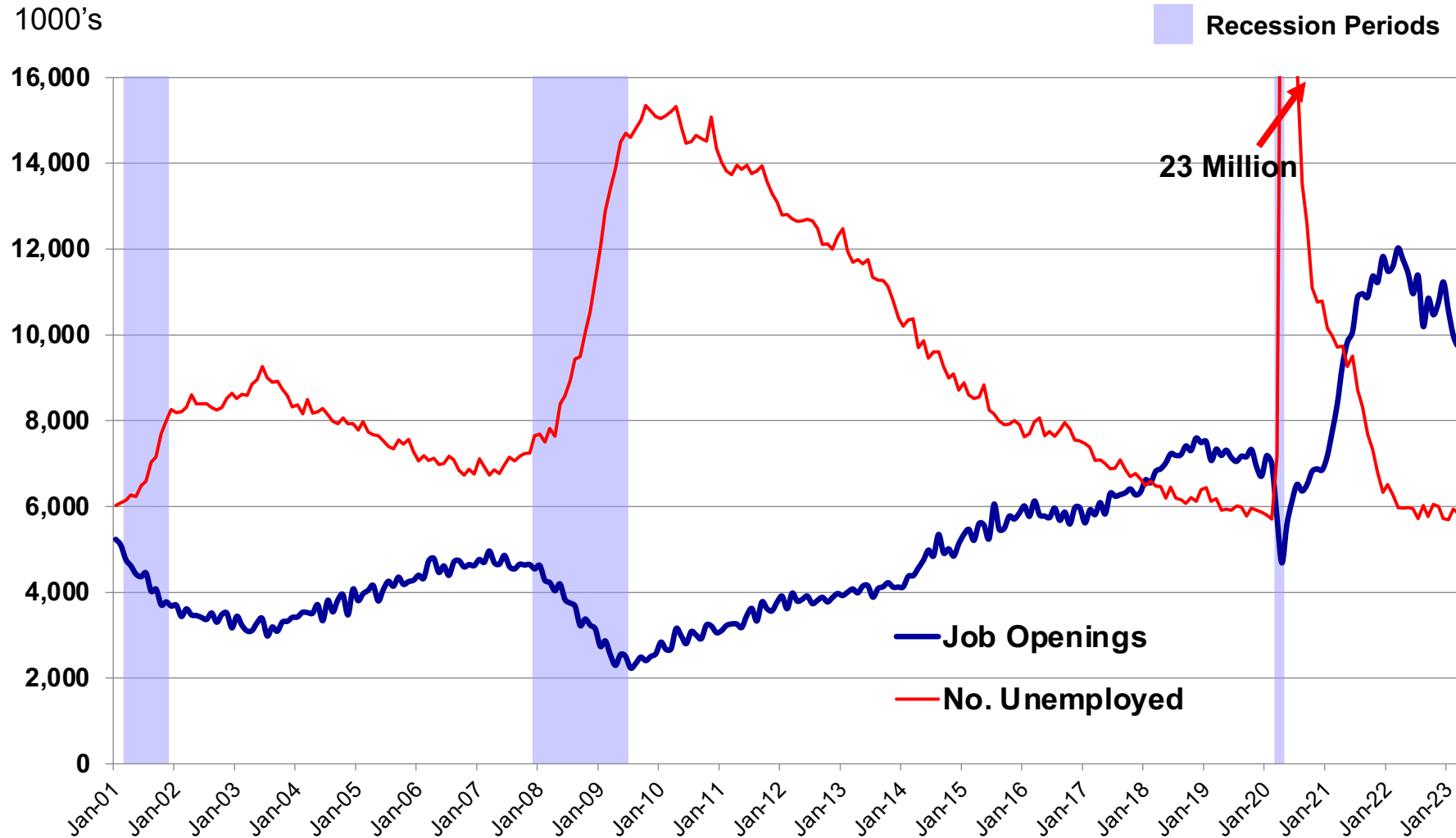




Job Openings and No. Unemployed

2001 – 2023*

Source: U.S. Bureau of Labor Statistics

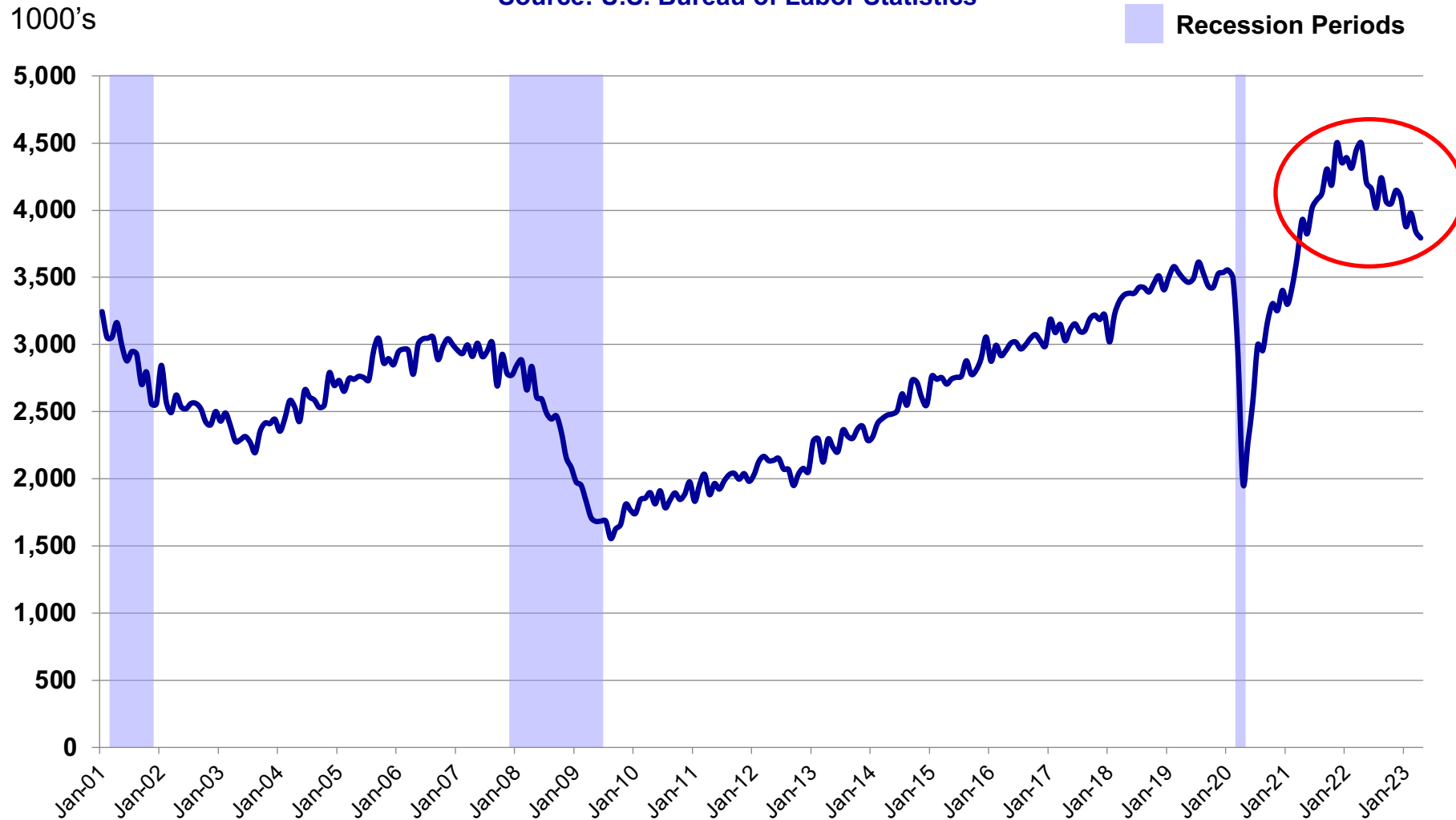


More Jobs Available than people unemployed

Quits

2001 – 2023*

Source: U.S. Bureau of Labor Statistics

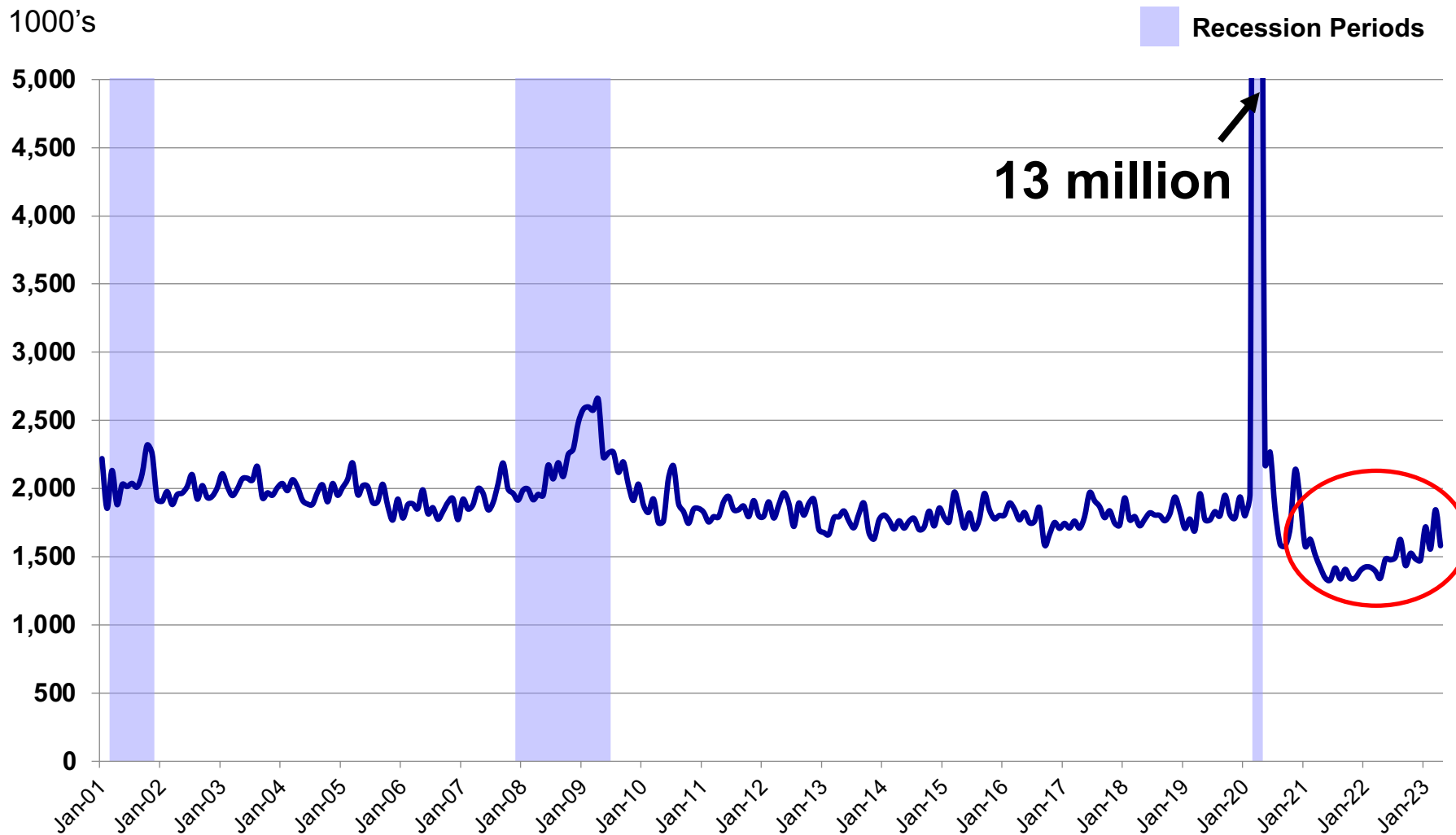


6,097,000 unemployed people in May 2023

*Data through April 2023

Layoffs 2001 – 2023*

Source: U.S. Bureau of Labor Statistics



6,097,000 unemployed people in May 2023

*Data through April 2023

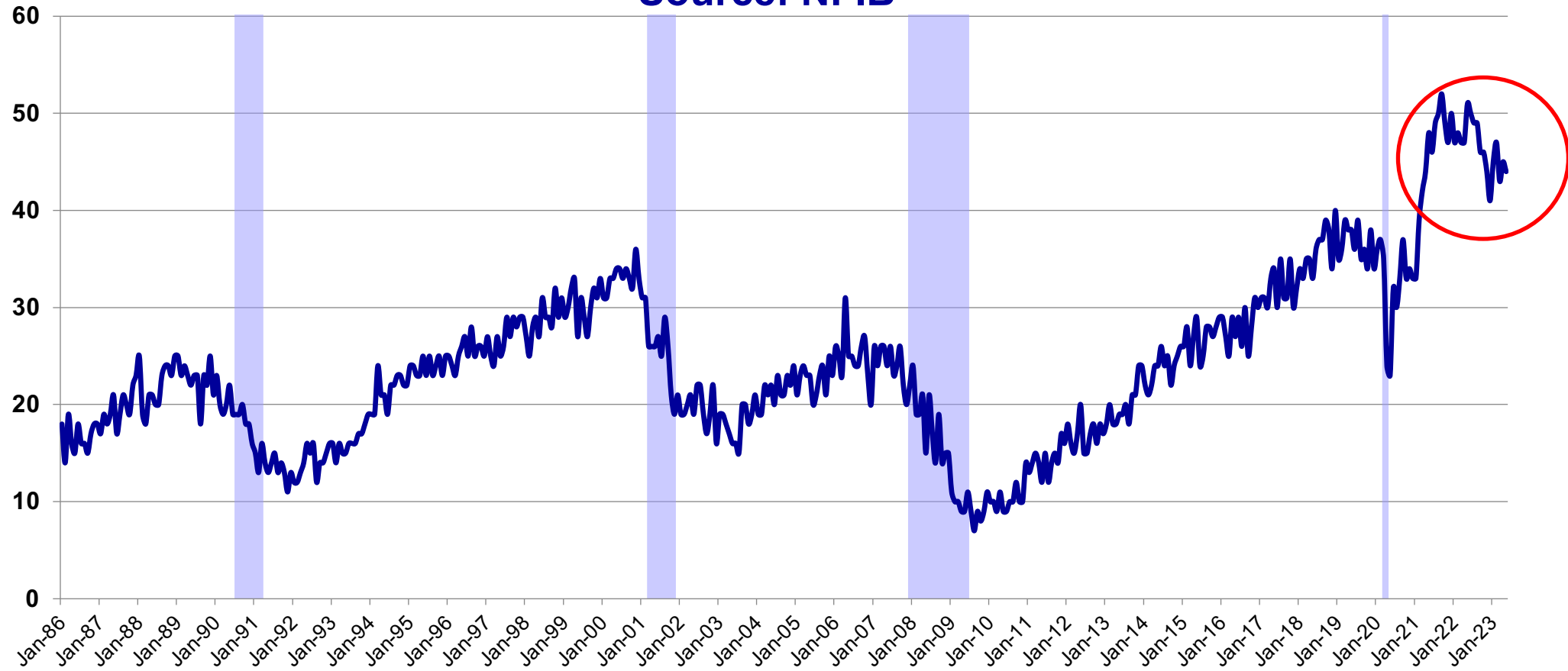


NFIB

Percentage of small businesses with unfilled job openings

1986-2023

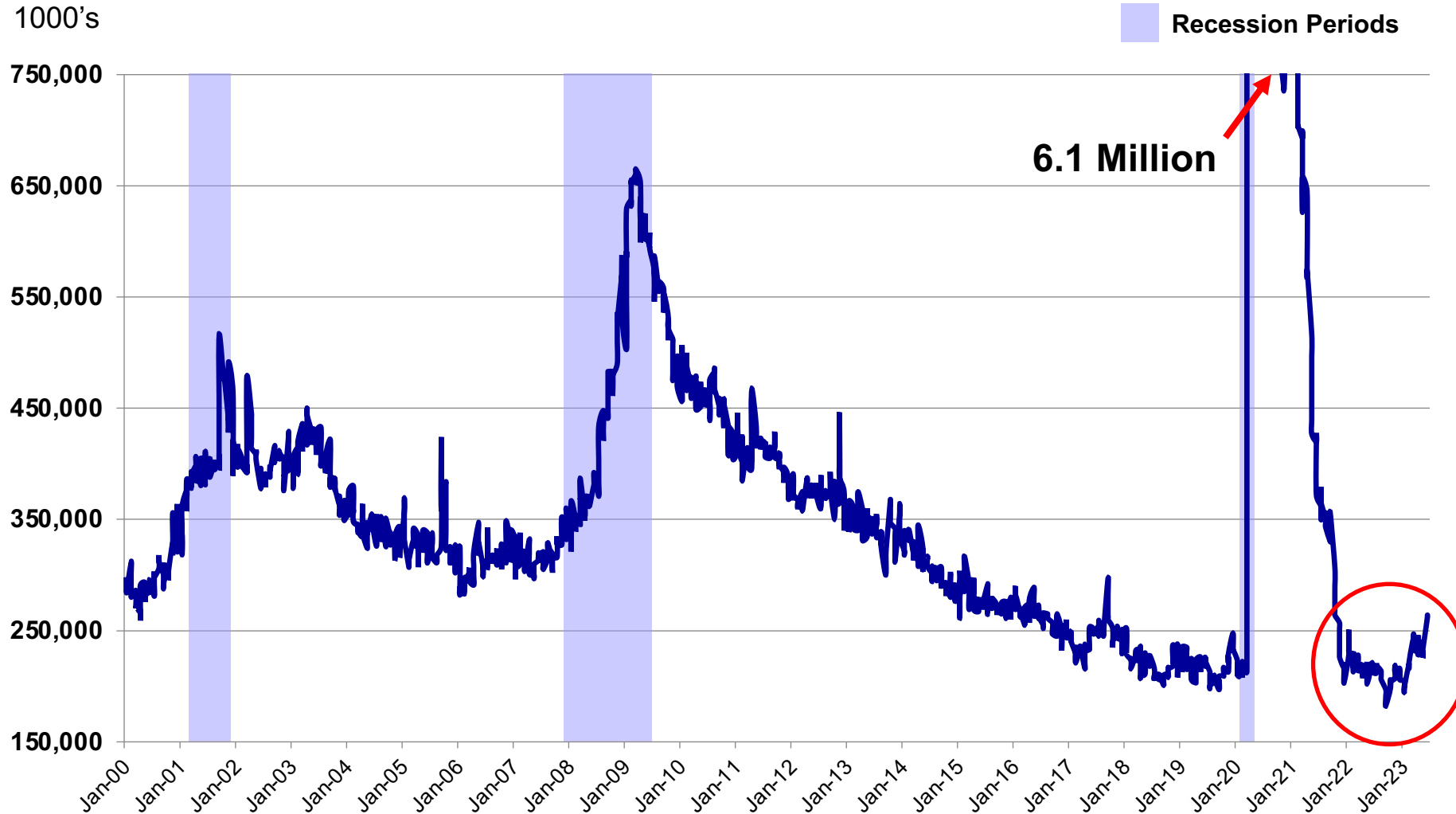
Source: NFIB



Initial Unemployment Claims

2000 – 2023*

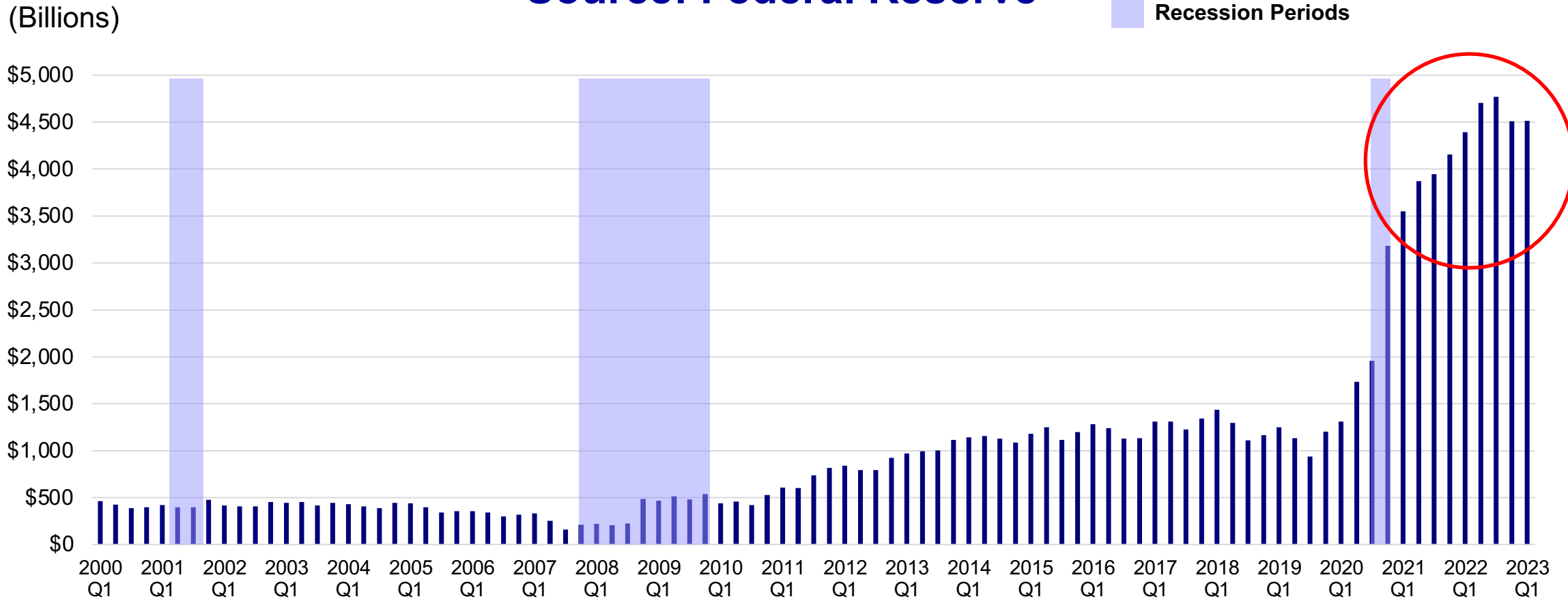
Source: U.S. Department of Labor



This bright employment picture could deteriorate as consumers and business are forced to cut back. We have not seen that occur so far.

Checkable Deposits and Currency of Households and Nonprofit Organizations

Source: Federal Reserve



What will Consumers do with Excess Cash?



- This excess cash will dissipate as the cost of necessities continues to rise.
- As the cash dissipates, consumer will cut back on discretionary spending and then non-discretionary spending to the extent possible.
- The lower the income, the more you will be affected.

We are in the Early Stages of a Credit Crunch

- Signature Bank and Silicon Valley Bank brought to light the impact of rising interest rates on banking.
- Banks are freezing credit, tightening lending standards, and recapitalizing.
- The government has stepped in to protect smaller banks from a classic bank run and avoid contagion.

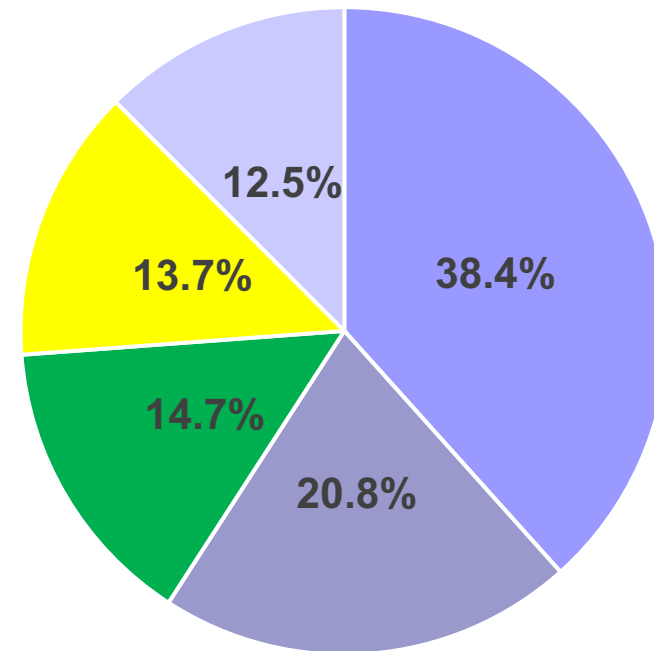


Commercial Real Estate (CRE) Lenders

\$4.5 Trillion Mortgage Market

Lender Percentages of CRE Mortgage Market

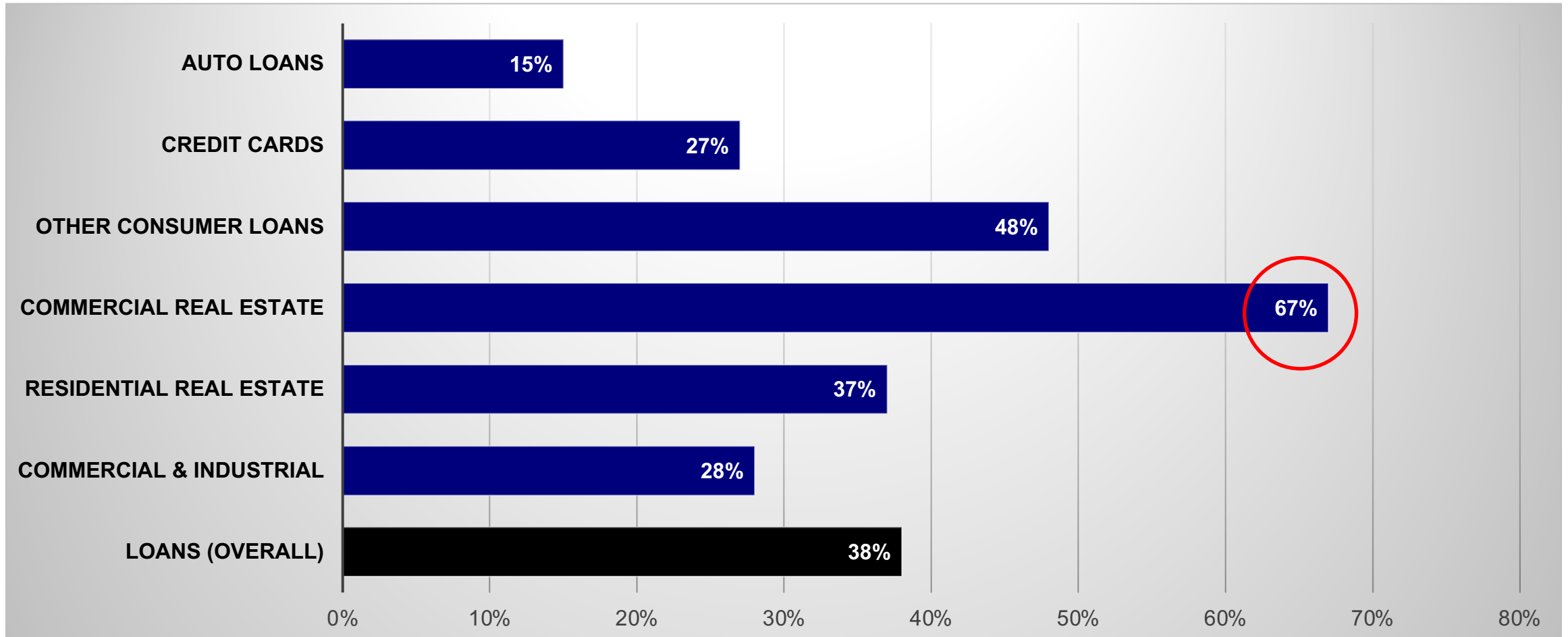
- Banks
- GSE Portfolios
- Life Insurance Co.
- CMBS, CDOs, ABS
- Other



Banking Definitions By Size

- Large Bank – The 25 largest financial institutions include U.S. firms with assets of \$100 billion or more and foreign banking organizations with combined U.S. assets of \$100 billion or more.
- Regional Bank – Total assets between \$10 billion and \$100 billion.
- Community Bank – Total assets between Less than \$10 billion
- Small Bank – Total assets with assets of less than \$1.384 billion

Regional and Community Banks Share Of All Outstanding Bank Loans By Type



Commercial Real Estate Loans as % of Assets Regional & Community Banks

Loan Type	Percent
Commercial Real Estate as % of Total Bank Assets*	29.4%
Commercial Property Loans	17.8%
Estimated Office Property Loans	3.0%

*Construction, farm, multifamily & commercial property loans.

Source: The Federal Reserve

Risk Among All CRE Lenders

- \$728 billion in commercial loans will mature in 2023
- \$659 billion will mature in 2024
- Maturing OFFICE loans:
 - \$189 Billion in 2023
 - \$117 Billion in 2024
- Banking risk is divided among 4,700 smaller banks

Sources: Colliers, Cohen & Steers

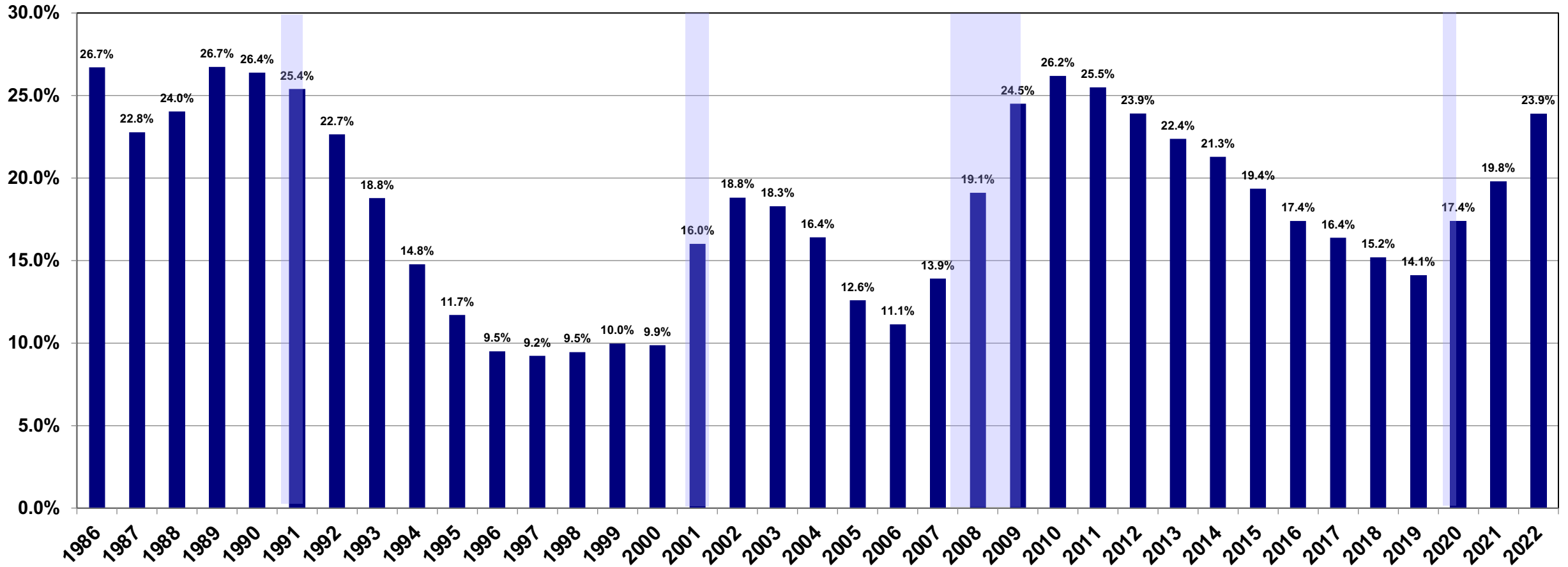
What Are Office Owners Facing?

- Remote work has changed the office market
- High vacancies across the country
- Office properties have potentially lost 30% of value
- Impact varies from region to region
- Impact also varies by building type – Class B & C properties impacted the worst
- Owners cannot cover operating and debt costs
- Refinancing, if possible, will only increase debt service

Office Space Year-End Vacancy Rates Greater Phoenix 1986–2022*

Source: CBRE

Recession Periods



Office Sublease Availability Greater Phoenix

Source: Colliers

- 2021 Q4 - 4,916,498
- 2023 Q1 - 7,178,585

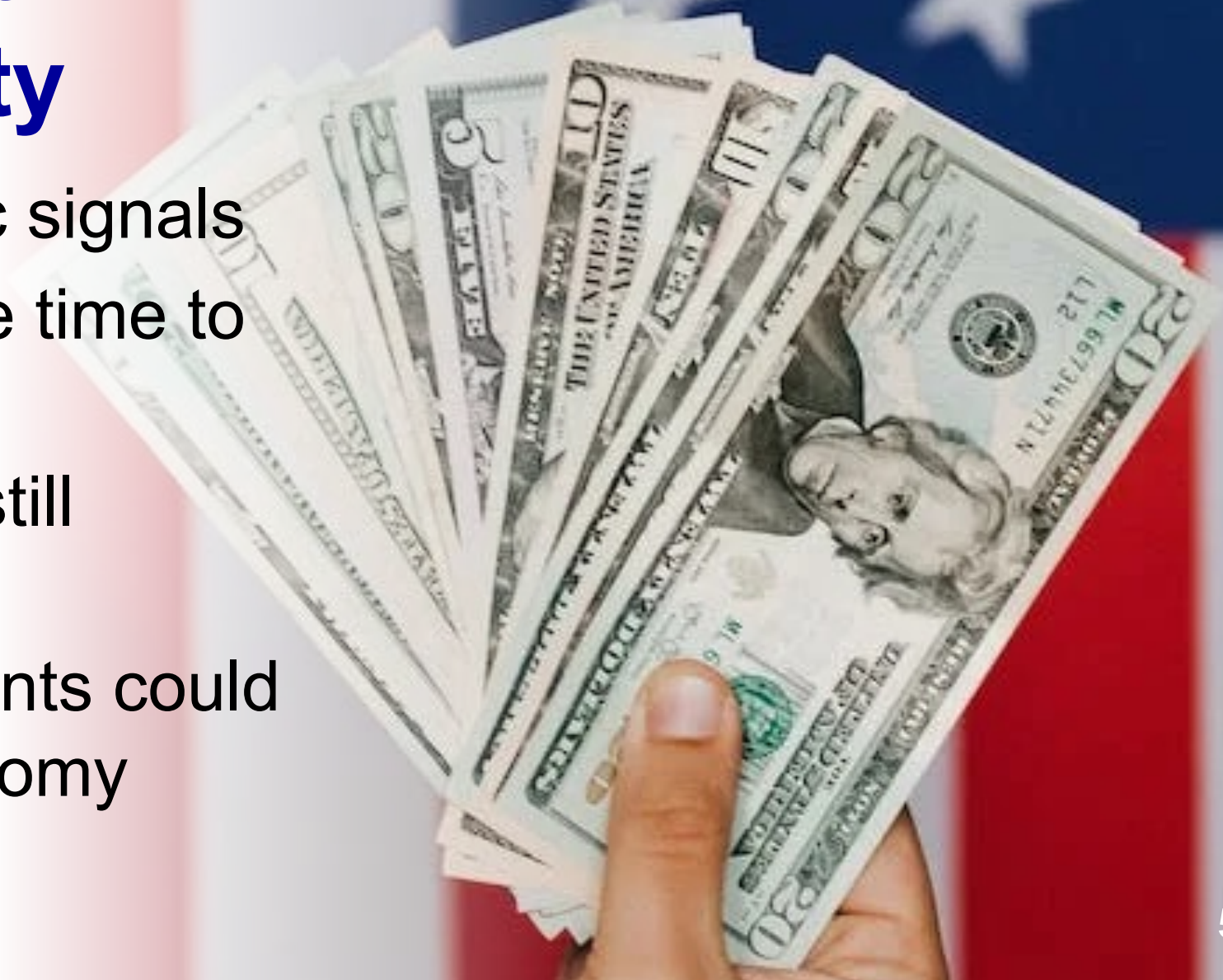


What Will the Banks Do?

- Recent “Guidance” from Fed and FDIC suggests lenders work with creditworthy borrowers
- Extend or renegotiate the loans, partial payments, deferred payments, etc.
- Require additional equity in projects
- Take back the properties and sell them at market

Economic Uncertainty

- Mixed economic signals
- Inflation will take time to tame
- Fiscal policy is still stimulative
- Geopolitical events could impact the economy



Fiscal Policy is Counter Productive

- Regardless of how you feel about the Inflation Reduction Act, it is designed to expand consumer's spending power. Thus, the programs increase demand.
- The increase in demand comes at a time the Fed is trying to slow demand to reduce upward pressure on prices.
- These and other moves make it tougher for the Fed to accomplish its goal.

Global Influences

Enormous RISKS to the economy, some of which are out of our control

- Geopolitical events: International Pariahs – add Russia to the list
- Energy
 - Purchasing oil from less than friendly countries
 - Administration has been demonizing the oil industry
 - We are going to need oil for decades to come



Energy Independence

“I just don’t think energy security and this move to sustainability and to cleaner energy should be mutually exclusive. I think they are two things we have to solve together.”

Citigroup CEO Jane Fraser





Projection of 26.4 million EVs on the road by 2030.

That accounts for just 10% of the 259 million light-duty vehicles expected to be on the road in 2030.

Source: Edison Electric Institute



Data to Watch

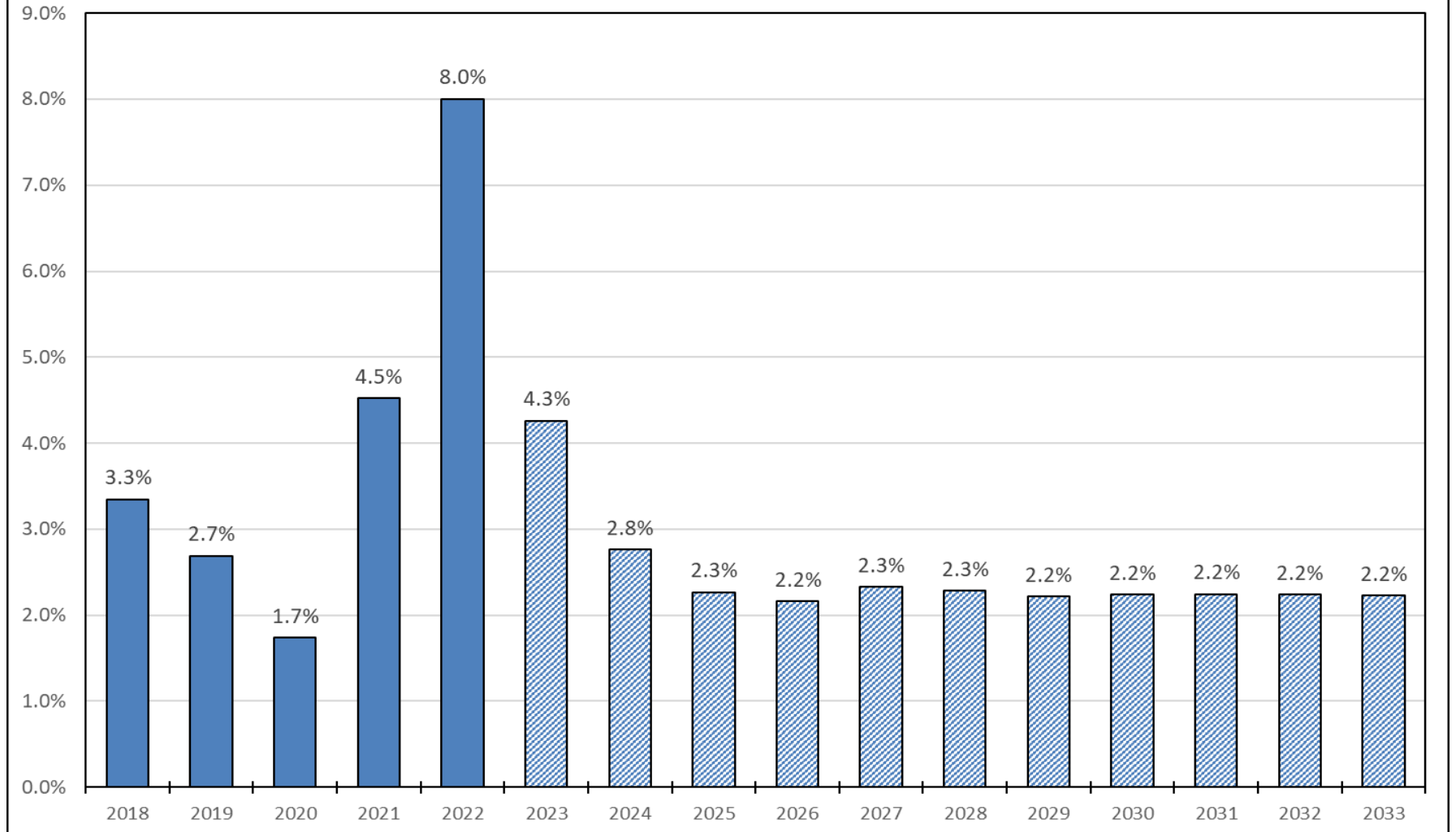
Forecasts are speculative
– will need to monitor
progress by Fed monthly

- Employment growth
- Unemployment levels
- Fed interest rate increases
- Progress on subduing inflation

Inflation Forecast

Inflation Forecast Western U.S. CPI All Urban Consumers

Source: U of A Forecasting Project



Recession Forecasts

- Mark Zandi – Chief Economist for Moody’s Analytics - now betting against recession
 - Excess Consumer Savings
 - Labor Hoarding – Businesses avoiding layoffs to hold onto talent
 - Light Debt Load – Consumer debt relative to disposable income
 - Anchored Inflation Expectations – Inflation receding, consumers will have a more positive outlook
 - Low Oil Prices – Prices have stabilized
- Goldman Sachs – Odds of a recession only 25%
- Bank of America- U.S. will achieve a soft landing next year



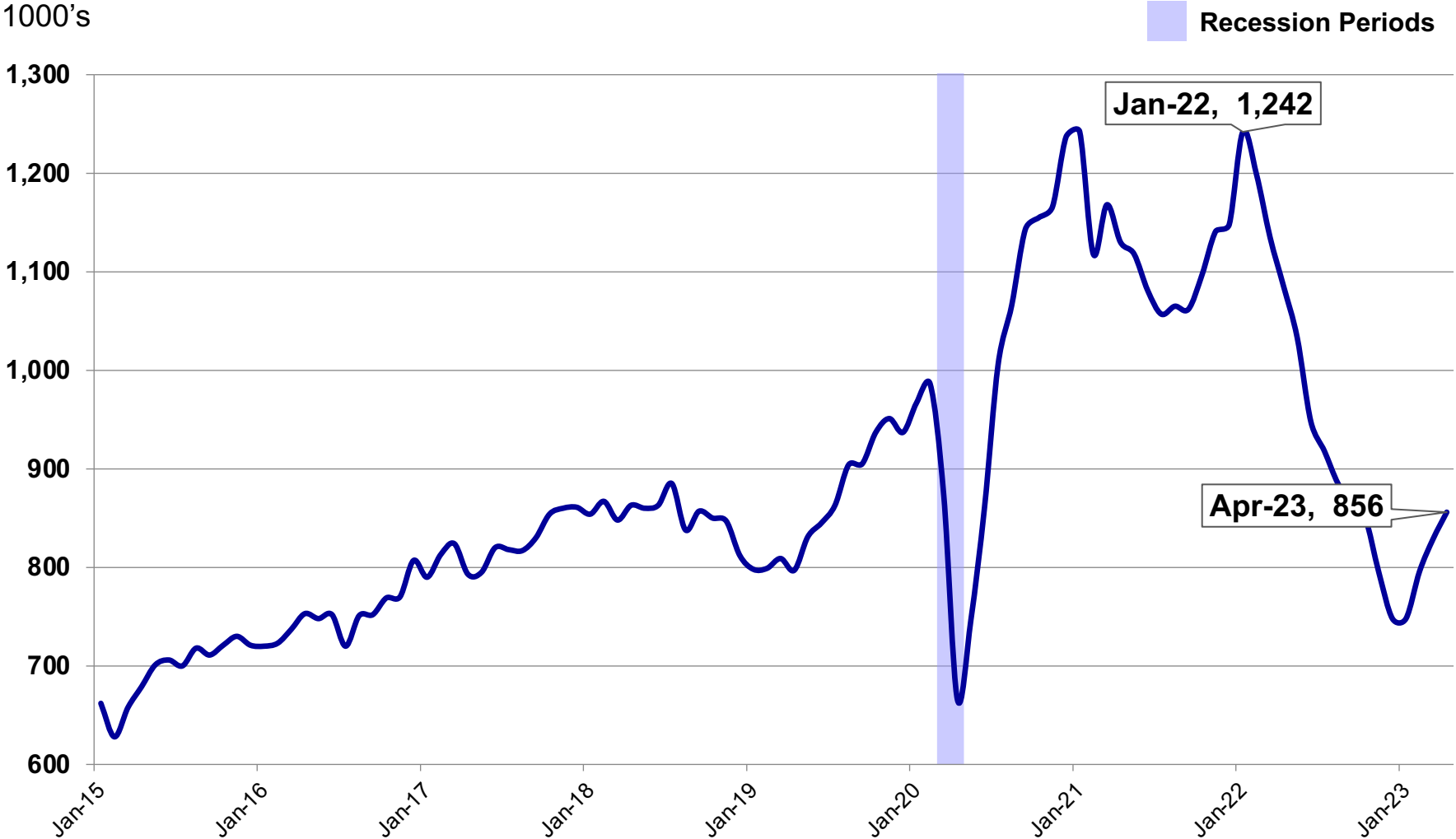
Housing



U.S. Single Family Permits

2015 – 2023*

Source: U.S. Census Bureau

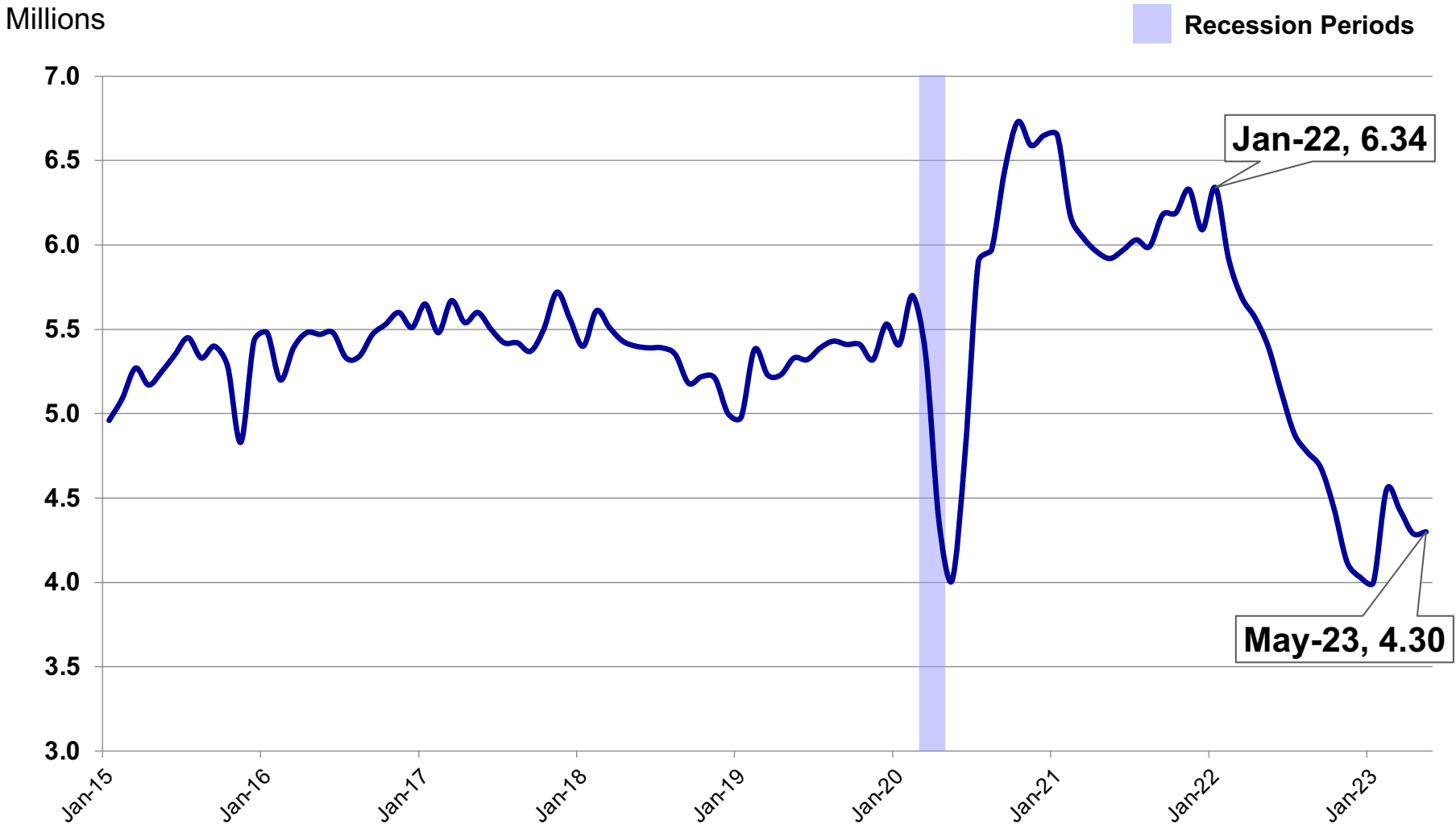


*Data through April 2023

U.S. Existing Home Sales (SAAR)

2015 – 2023*

Source: NAR



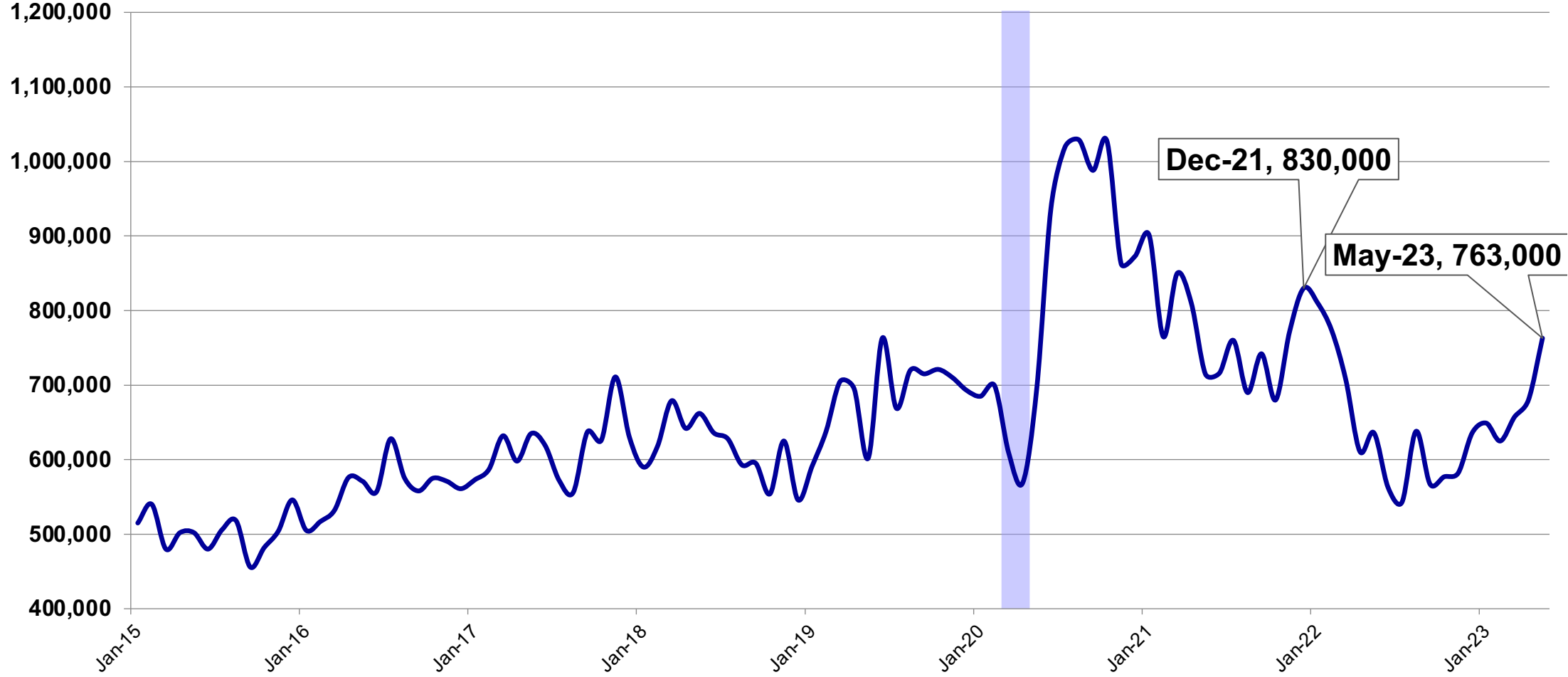
*Data through May 2023

U.S. New Home Sales

2015 – 2023*

Source: U.S. Census Bureau

Recession Periods

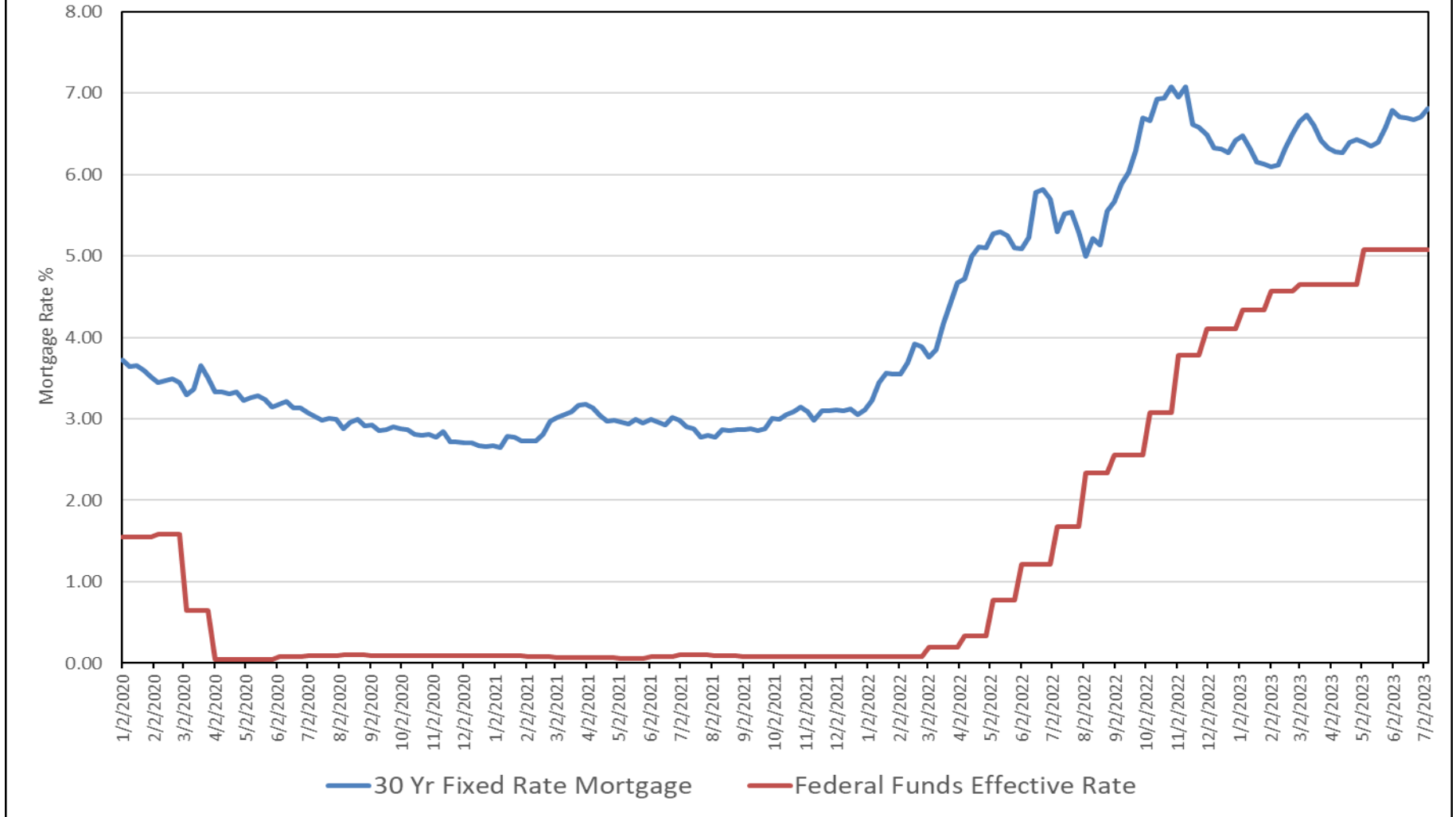


*Data through May 2023.

Mortgage Rate Trends

Average 30-Year Fix Rate Mortgage Rate & Federal Funds Effective Rate 2020 - May 2023

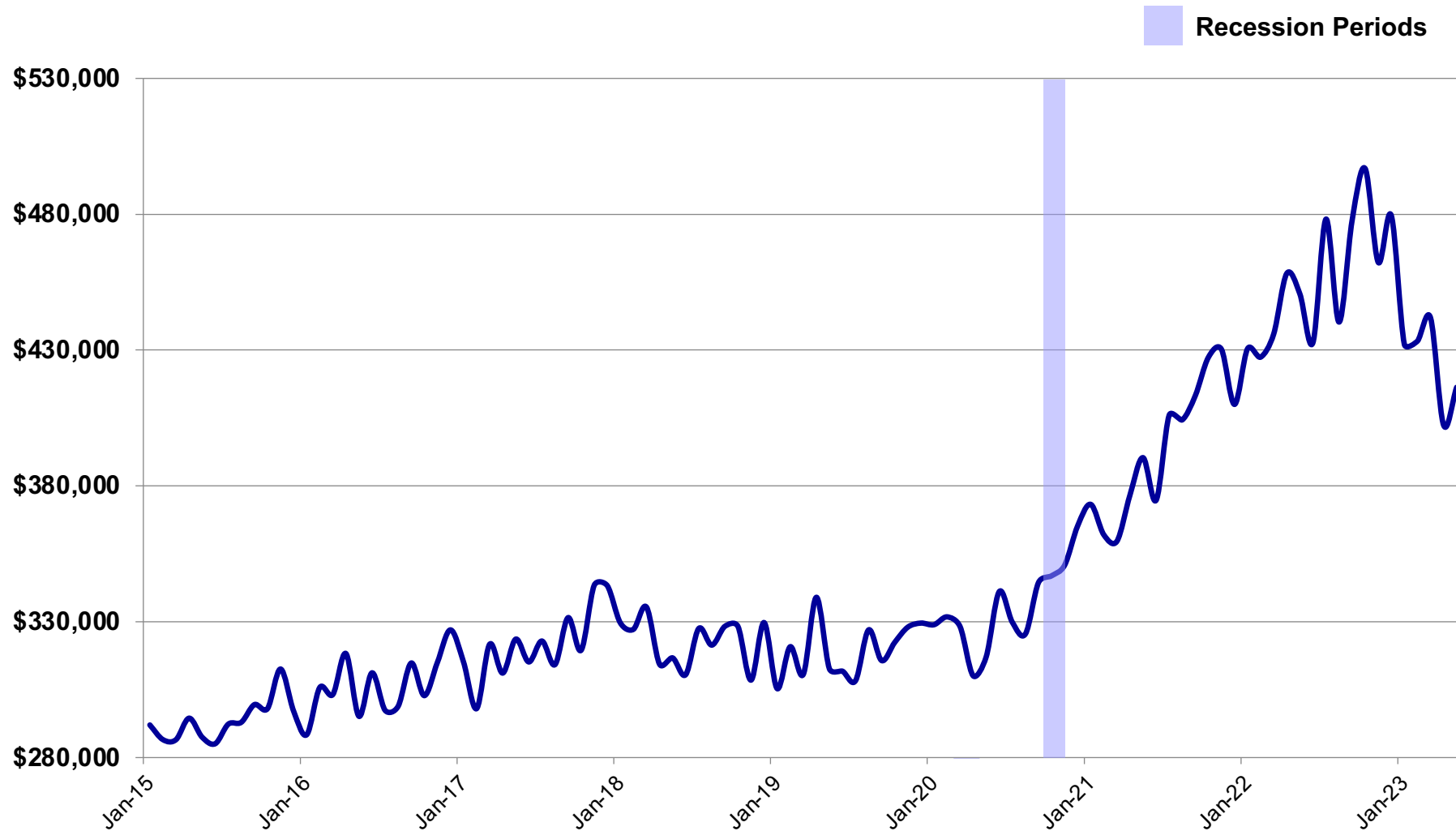
Source: Freddie Mac Primary Mortgage Market Survey, St. Louis FED



U.S. New Home Median Sales Price

2015 – 2023*

Source: U.S. Census

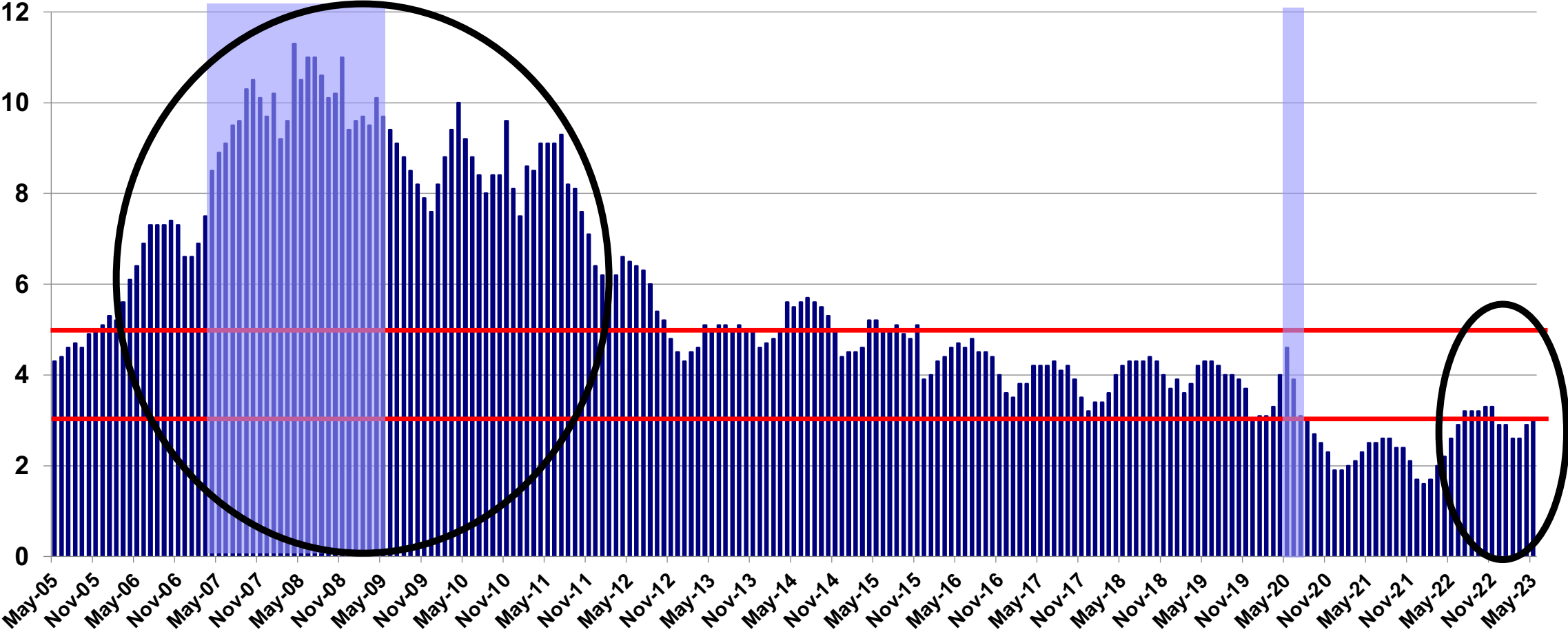


National Months Supply

2005-2023*

Source: NAR

Recession Periods

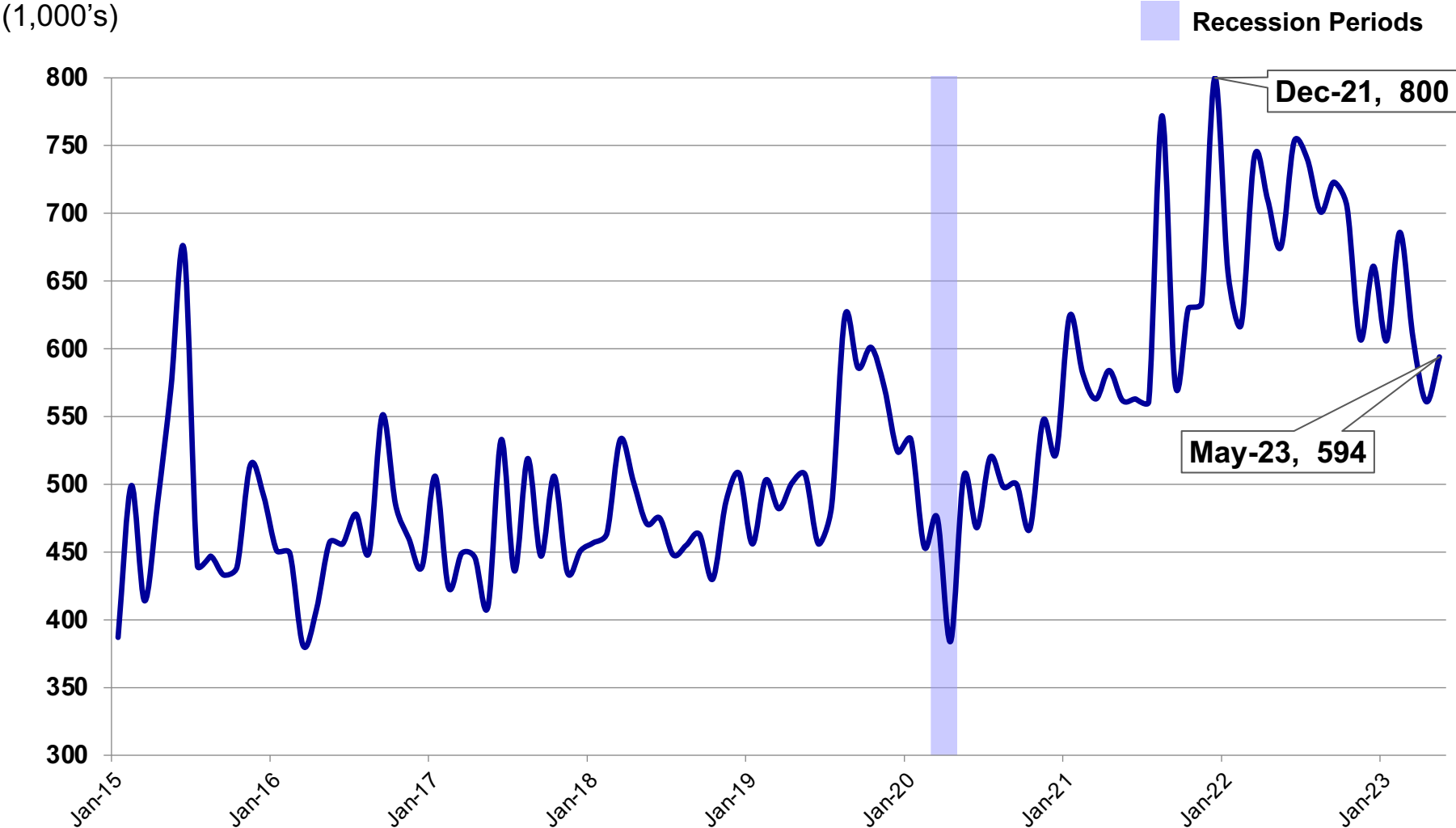


*Data through May 2023

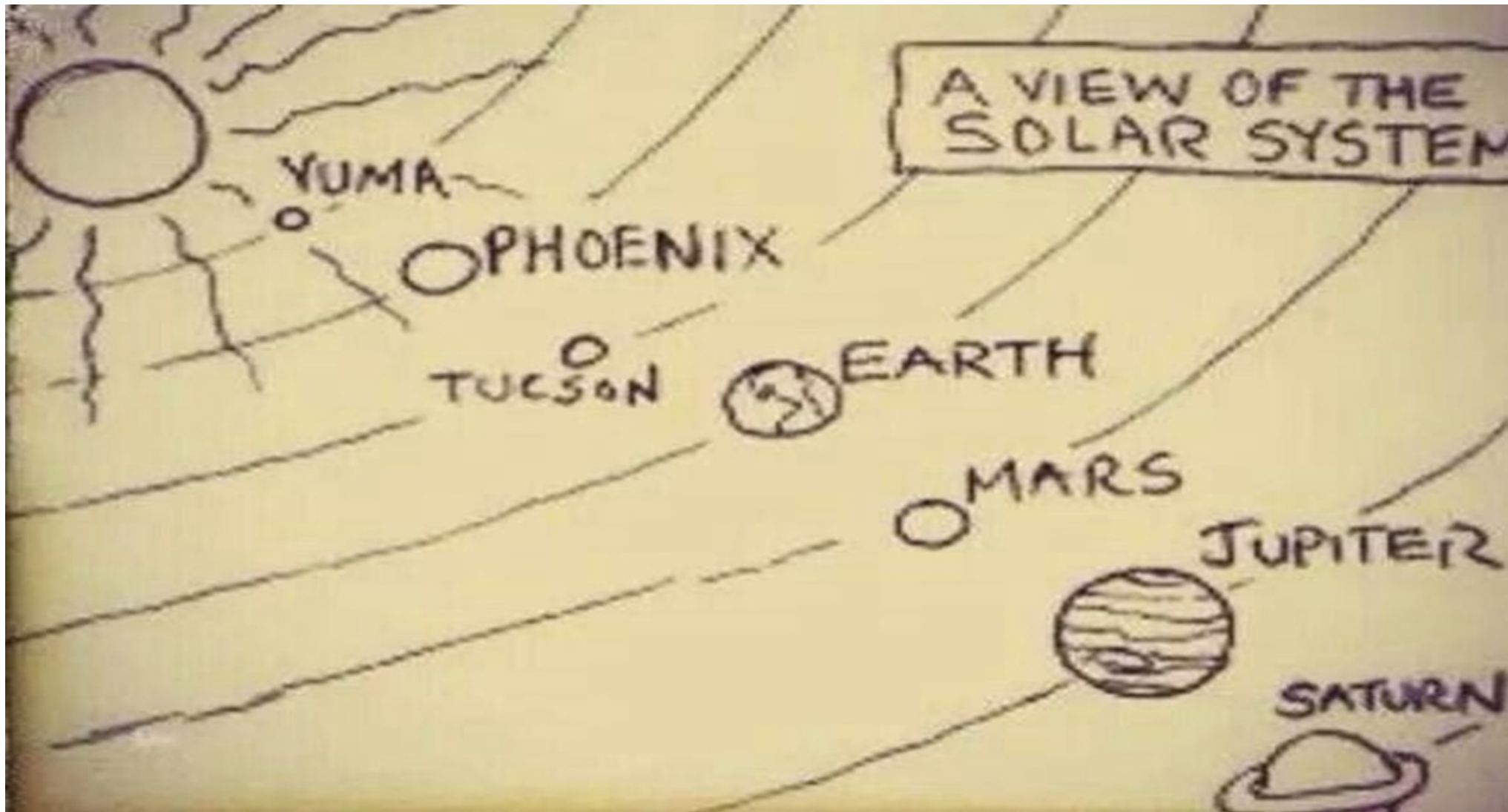
U.S. Multi-Family Permits

2015 – 2023*

Source: U.S. Bureau of Labor Statistics



State of Arizona



Arizona Rankings Among States

Source: U.S. Bureau of Census; Bureau of Labor Statistics; Bureau of Economic Analysis

DECADE	POPULATION	EMPLOYMENT	PERSONAL INCOME
1950 - 1960	4 TH	1 st	2 nd
1960 - 1970	3 RD	3 RD	4 TH
1970 - 1980	2 ND	3 RD	3 RD
1980 - 1990	3 RD	3 RD	5 TH
1980 - 1990	2 ND	2 ND	3 rd
2000 – 2010	2 nd	12 th	12 th
2010 – 2020	9 th	3 rd	6 th



Job Growth 2023 versus 2019

May 2023 vs. May 2019

Source: U.S. BLS

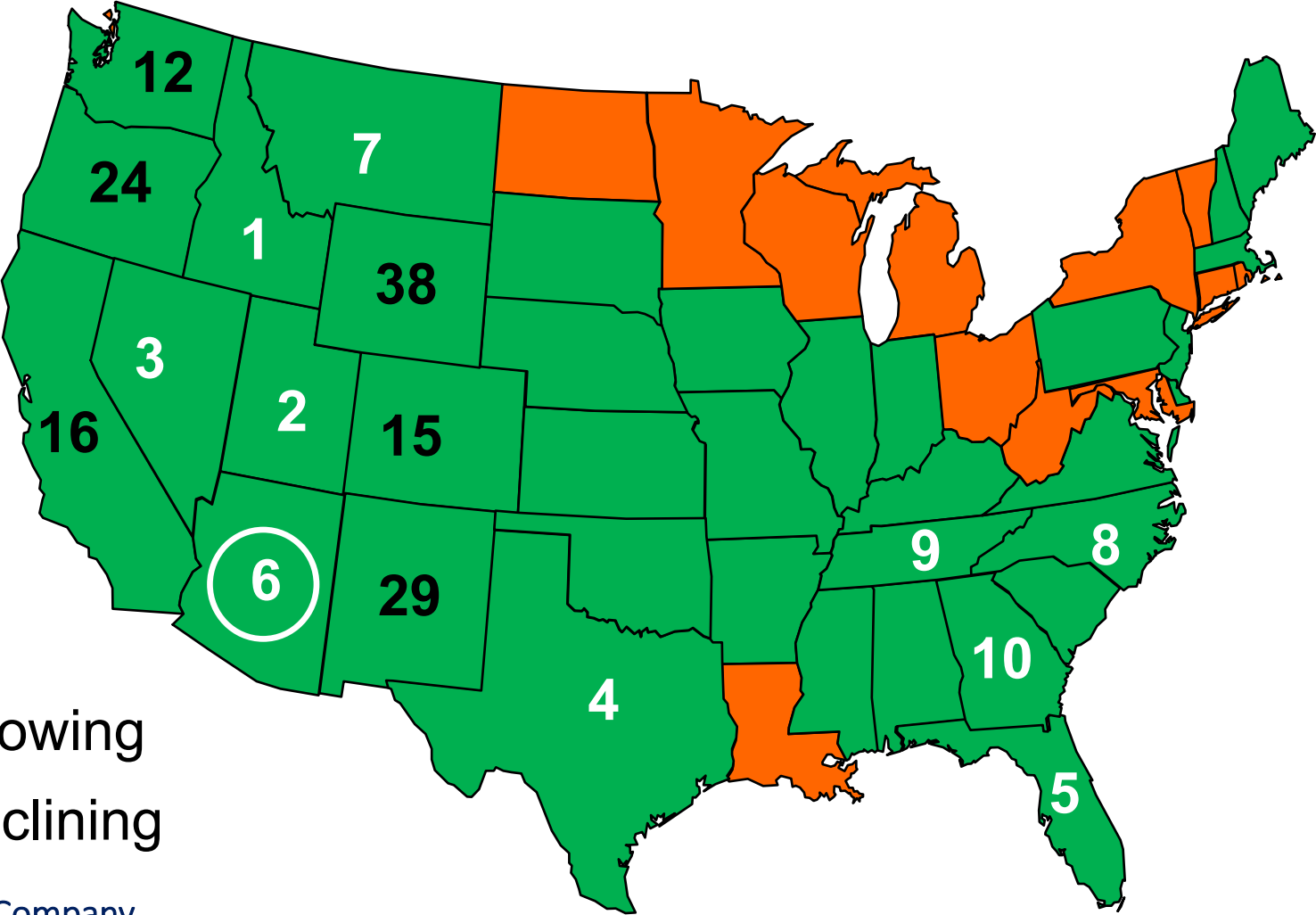
Alaska
41

50

Hawaii

● Jobs growing

● Jobs declining



Large Metro Area Employment Ranking

Metro	2023	2019	Growth	Rank
Austin-Round Rock	1,304.9	1,105.6	18.0%	1
Dallas-Fort Worth-Arlington	4,206.0	3,736.8	12.6%	2
Nashville-Davidson--Murfreesboro--Franklin	1,152.4	1,035.4	11.3%	3
Tampa-St. Petersburg-Clearwater	1,526.6	1,375.8	11.0%	4
Phoenix-Mesa-Chandler	2,360.1	2,162.7	9.1%	5
Riverside-San Bernardino-Ontario	1,667.4	1,533.5	8.7%	6
Las Vegas-Henderson-Paradise	1,114.7	1,026.7	8.6%	7
Charlotte-Concord-Gastonia	1,336.9	1,233.5	8.4%	8
Orlando-Kissimmee-Sanford	1,431.9	1,321.5	8.4%	9
San Antonio-New Braunfels	1,155.3	1,067.3	8.2%	10

Source: Bureau of Labor Statistics

Note: Metro areas with over 1,000,000 jobs

*May 2023 data

Greater Phoenix is now the 10th largest Metro in the Country (population 1970-2021)

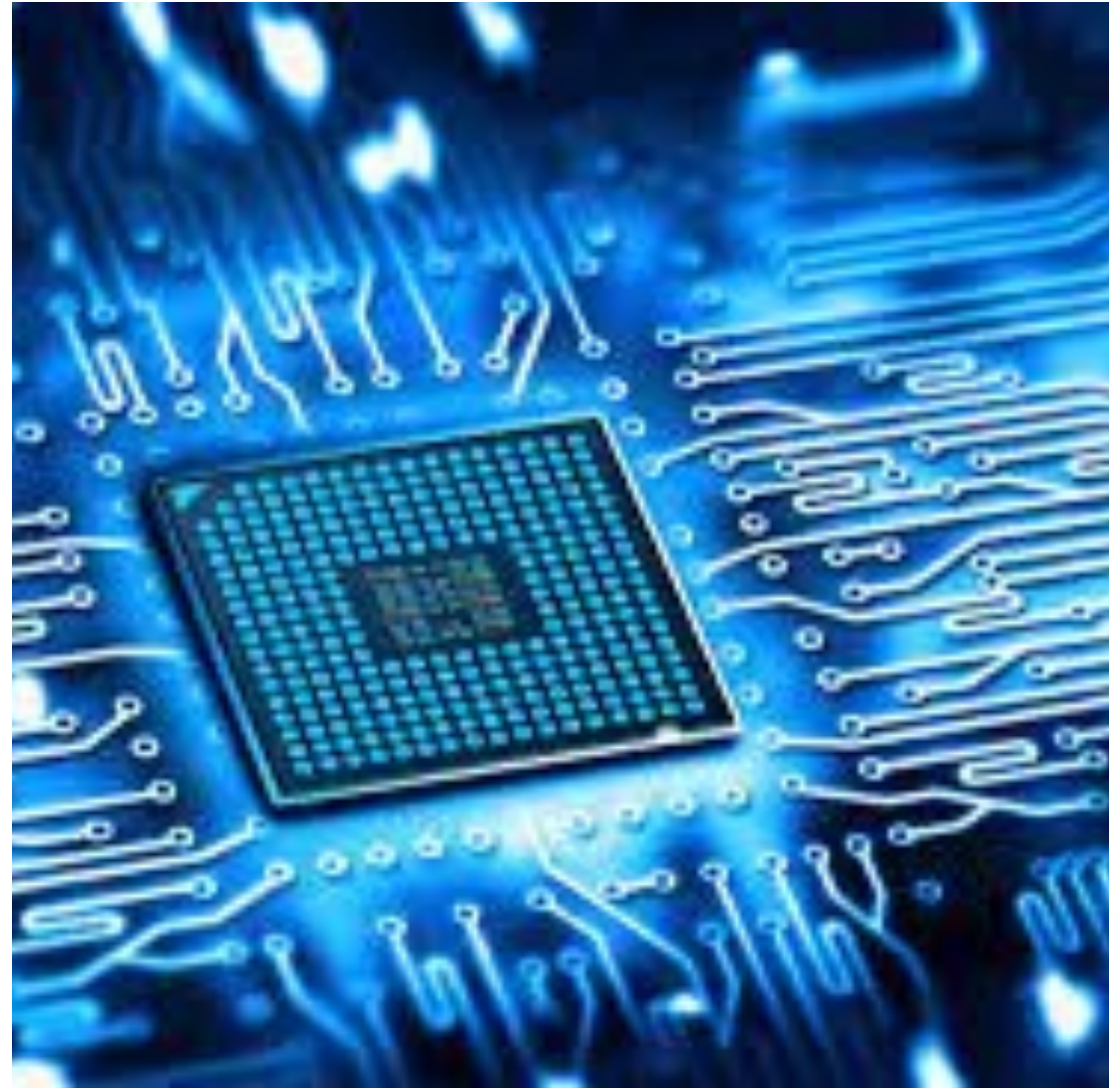
Source: U.S. Department of Commerce, Bureau of the Census)

City of Phoenix is the 5th largest city in the country

Rank	1970	1980	1990	2000	2010	2021
1	New York	New York	New York	New York	New York	New York
2	Los Angeles	Los Angeles	Los Angeles	Los Angeles	Los Angeles	Los Angeles
3	Chicago	Chicago	Chicago	Chicago	Chicago	Chicago
4	Philadelphia	Philadelphia	Washington, DC	Dallas	Dallas	Dallas
5	Detroit	Detroit	San Francisco	Philadelphia	Philadelphia	Houston
6	San Francisco	San Francisco	Philadelphia	Houston	Houston	Washington DC
7	Washington, DC	Washington, DC	Boston	Washington DC	Washington DC	Philadelphia
8	Boston	Dallas	Detroit	Miami	Miami	Atlanta
9	Pittsburgh	Houston	Dallas	Atlanta	Atlanta	Miami
10	St. Louis	Boston	Houston	Boston	Boston	Greater Phoenix
11	Baltimore	Nassau-Suffolk	Miami	San Francisco	San Francisco	Boston
12	Cleveland	St. Louis	Seattle	Detroit	Detroit	Riverside
13	Houston	Pittsburgh	Atlanta	Riverside	Riverside	San Francisco
14	Newark	Baltimore	Cleveland	Greater Phoenix	Greater Phoenix	Detroit
15	Minneapolis	Minneapolis	Minneapolis	Seattle	Seattle	Seattle
16	Dallas	Atlanta	San Diego	Minneapolis	Minneapolis	Minneapolis
17	Seattle	Newark	St. Louis	San Diego	San Diego	San Diego
18	Orange County, CA	Orange County, CA	Pittsburgh	St. Louis	St. Louis	Tampa
19	Milwaukee	Cleveland	Greater Phoenix	Tampa	Tampa	Denver
20	Atlanta	San Diego	Tampa	Baltimore	Baltimore	Baltimore
21	Cincinnati	Miami	Denver	Denver	Denver	St. Louis
22	Paterson	Denver	Cincinnati	Pittsburgh	Pittsburgh	Charlotte
23	San Diego	Seattle	Portland	Portland	Portland	Orlando
24	Buffalo	Tampa	Milwaukee	Sacramento	Sacramento	San Antonio
25	Miami	Riverside	Kansas City	San Antonio	San Antonio	Portland
26	Kansas City	Greater Phoenix	Sacramento	Orlando	Orlando	Sacramento
27	Denver	Cincinnati	Norfolk	Cincinnati	Cincinnati	Pittsburgh
28	Riverside	Milwaukee	Indianapolis	Cleveland	Cleveland	Austin
29	Indianapolis	Kansas	Columbus	Kansas City	Kansas City	Las Vegas
30	San Jose	San Jose	San Antonio	San Jose	San Jose	Cincinnati
31	New Orleans	Buffalo	New Orleans	Columbus	Columbus	Kansas City
32	Tampa	Portland	Orlando	Charlotte	Charlotte	Columbus
33	Portland	New Orleans	Buffalo	Indianapolis	Indianapolis	Indianapolis
34	Greater Phoenix	Indianapolis	Charlotte	Virginia Beach	Virginia Beach	Cleveland
35	Columbus	Columbus	Hartford	Providence	Providence	Nashville

Arizona & Greater Phoenix

- Most of the growth is in Greater Phoenix
- Strong job growth likely to slow in 2023.
- Economic development successes (semiconductors, electrical car & battery manufacturers and suppliers)
- Single family housing is under lots of pressure.
- Rental housing still positive.
- Continued but slower population growth



Arizona:

Phoenix and the Rest of the State

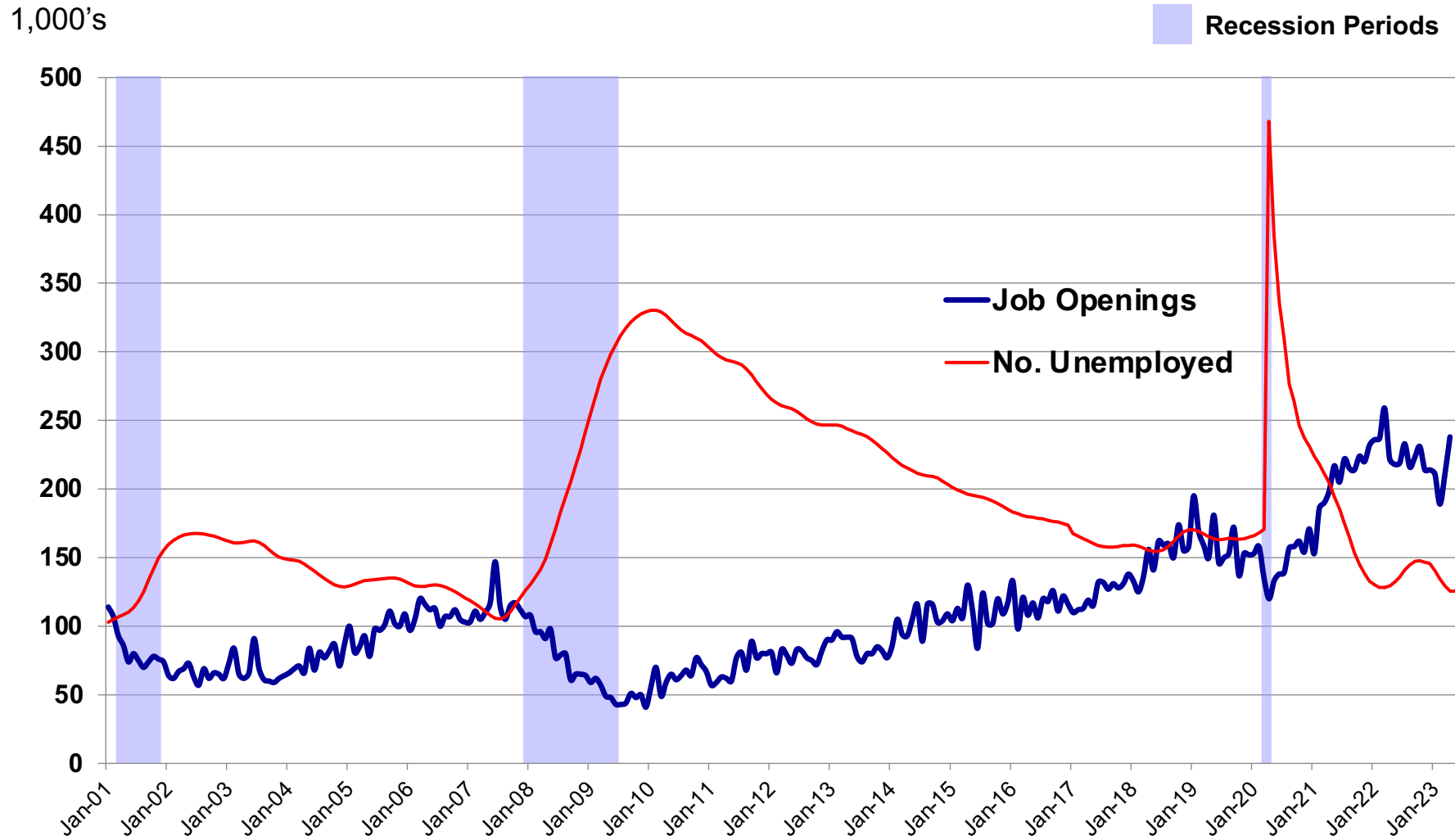
April 2022 - May 2023

Area	% Change	% of Arizona Job Growth	2022 (p) Annual Wages
Arizona	18.7%	100.0%	\$64,721
Greater Phoenix	19.9%	79.3%	\$67,584
Greater Tucson	14.2%	10.0%	\$57,135
Balance of State	15.9%	10.7%	\$50,154

Greater Phoenix accounts for **68%**
of the States's Population

Arizona Job Openings and No. Unemployed 2001 – 2023*

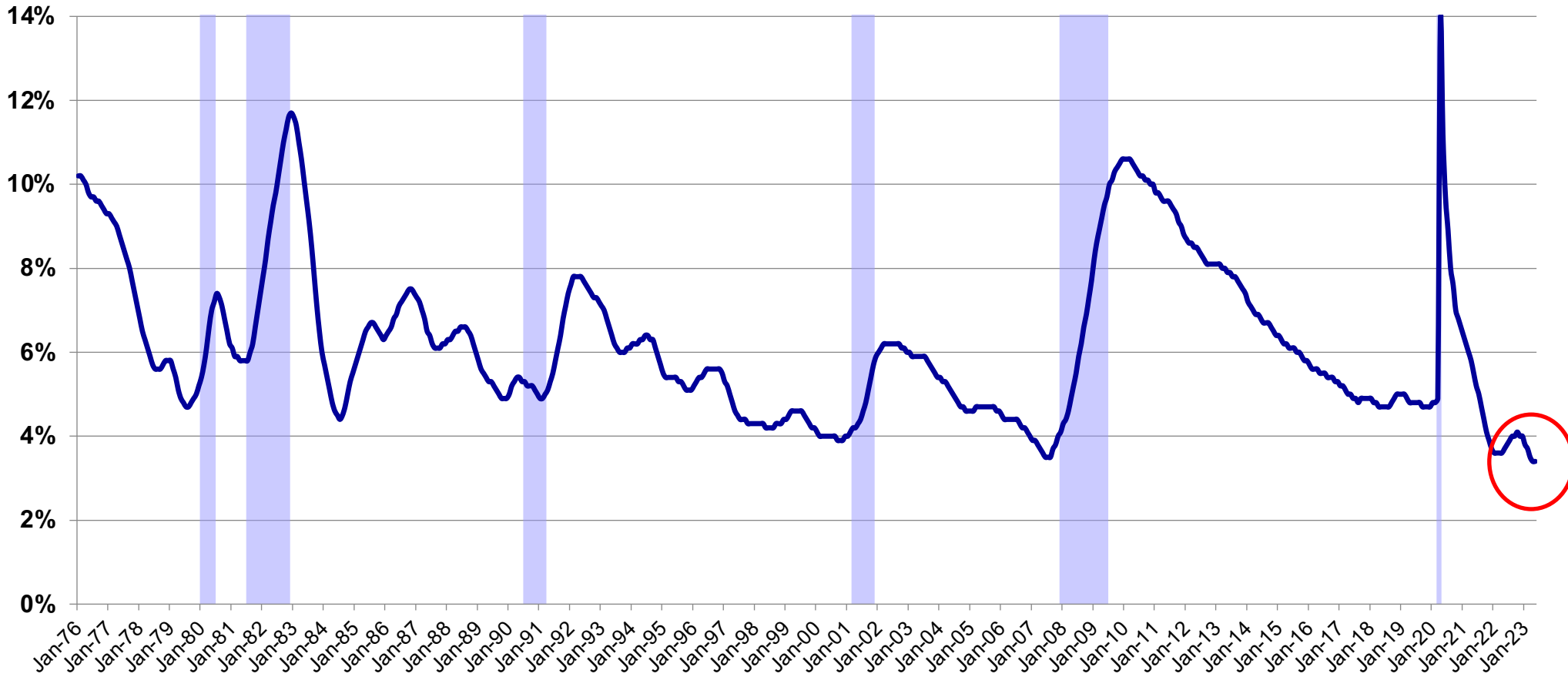
Source: U.S. Bureau of Labor Statistics



Arizona Unemployment Rate

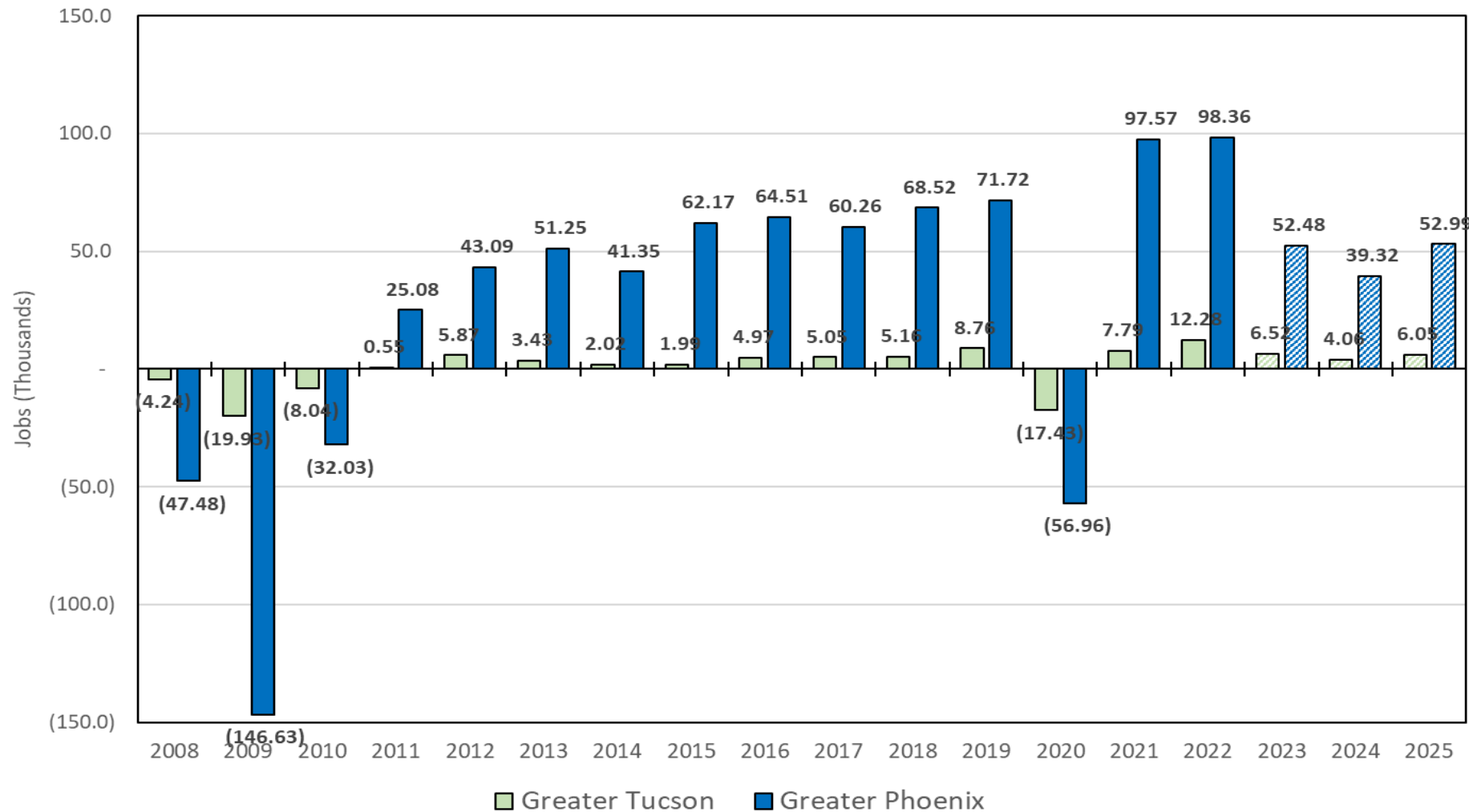
1976-2023

Source: BLS; AOEO



Historic & Future Job Growth Greater Tucson & Greater Phoenix

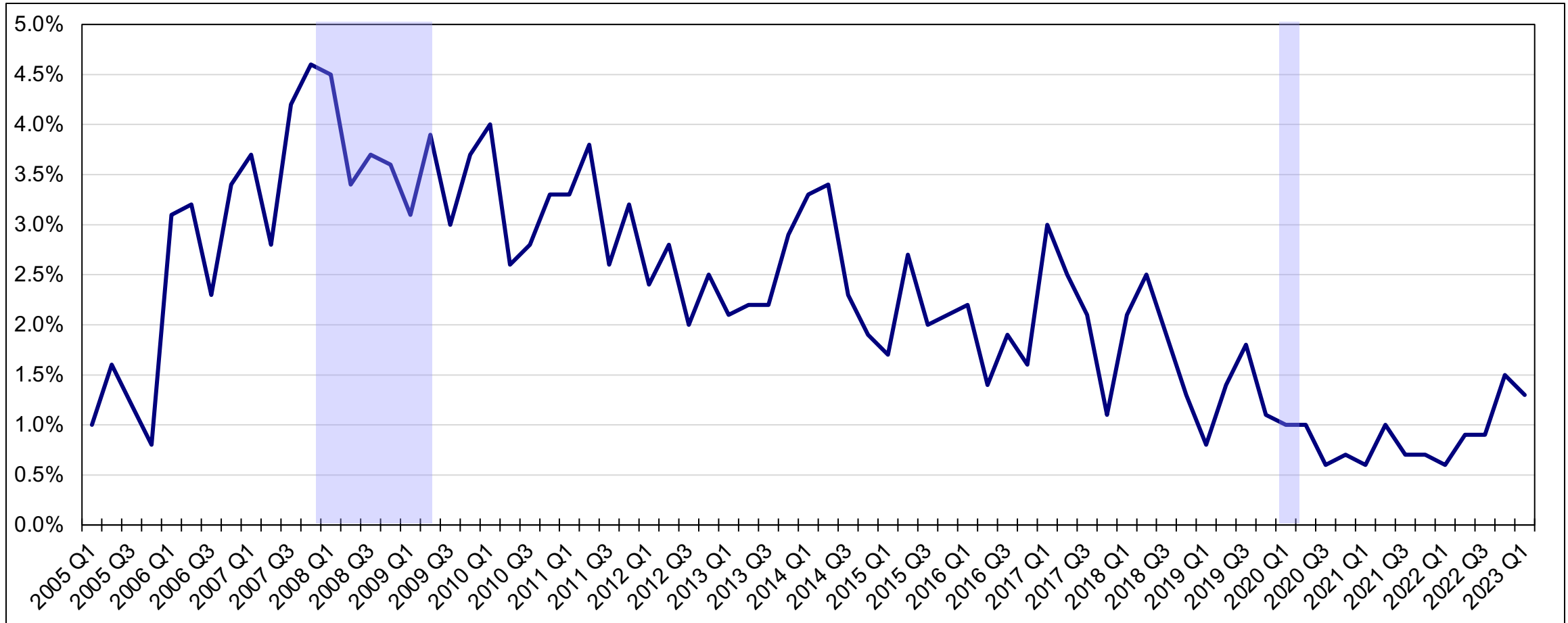
Source: AZ OEO, U of A



Job Growth

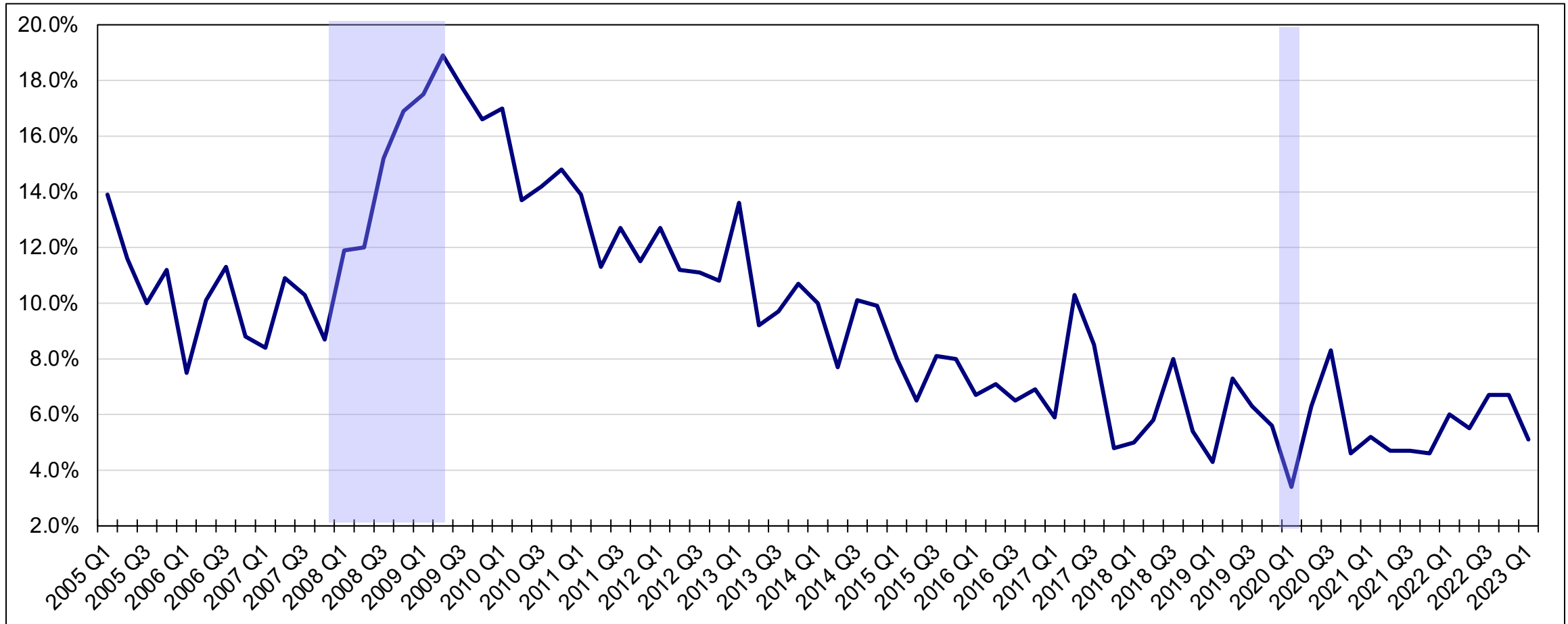
AZ Homeowner Vacancy Rate

Source: U.S. Census Bureau



AZ Rental Vacancy Rate

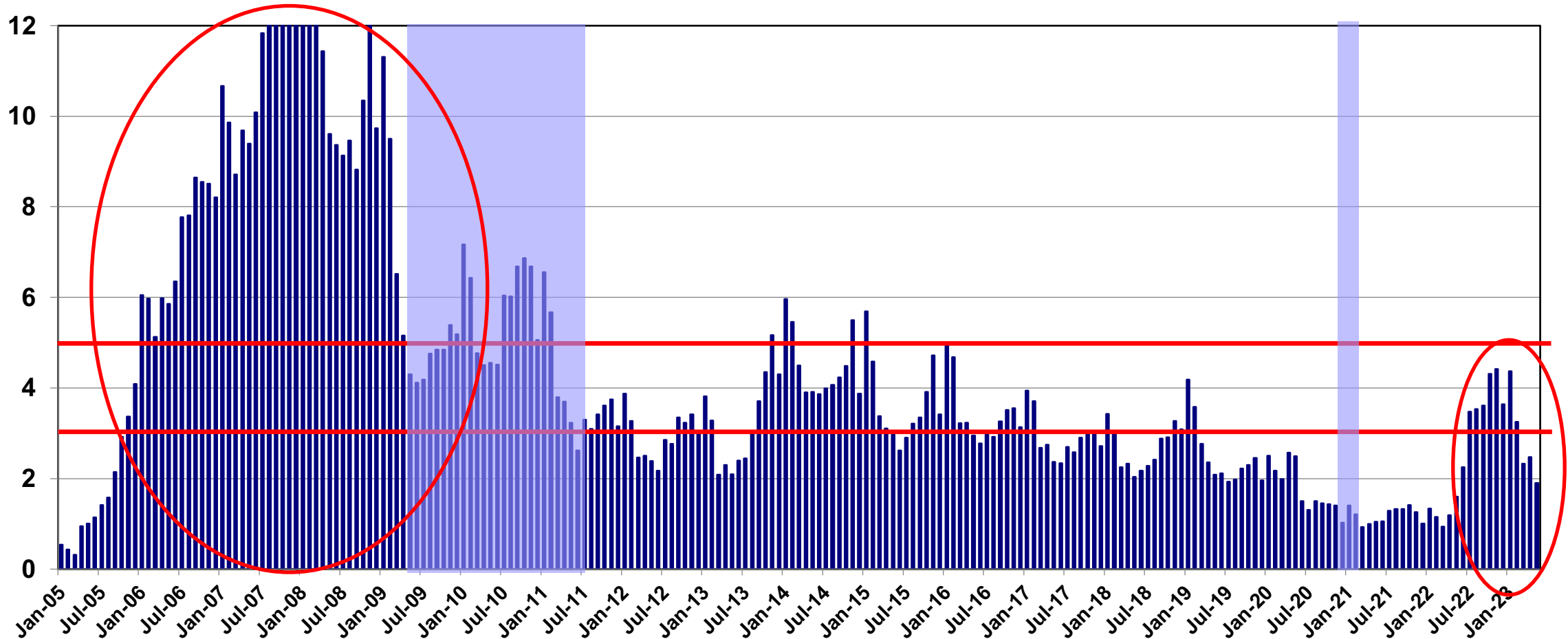
Source: U.S. Census Bureau



Greater Phoenix Months Supply of For Sale Housing

Source: ARMLS; Cromford Report

Recession Periods



Arizona Undersupplied Housing Market

- Arizona Department of Housing analysis estimates that 270,000 housing units are needed statewide just to meet current demand.
- Greater Phoenix ranked 4th most undersupplied market in U.S. based on vacancy rates by John Burns Real Estate Consulting.
- City of Phoenix market is undersupplied by 163,000 units

If this is not addressed now, the problem will worsen. The only way to fix this properly is to build more and build now.

What's Different in the Housing Market Compared to 2008?

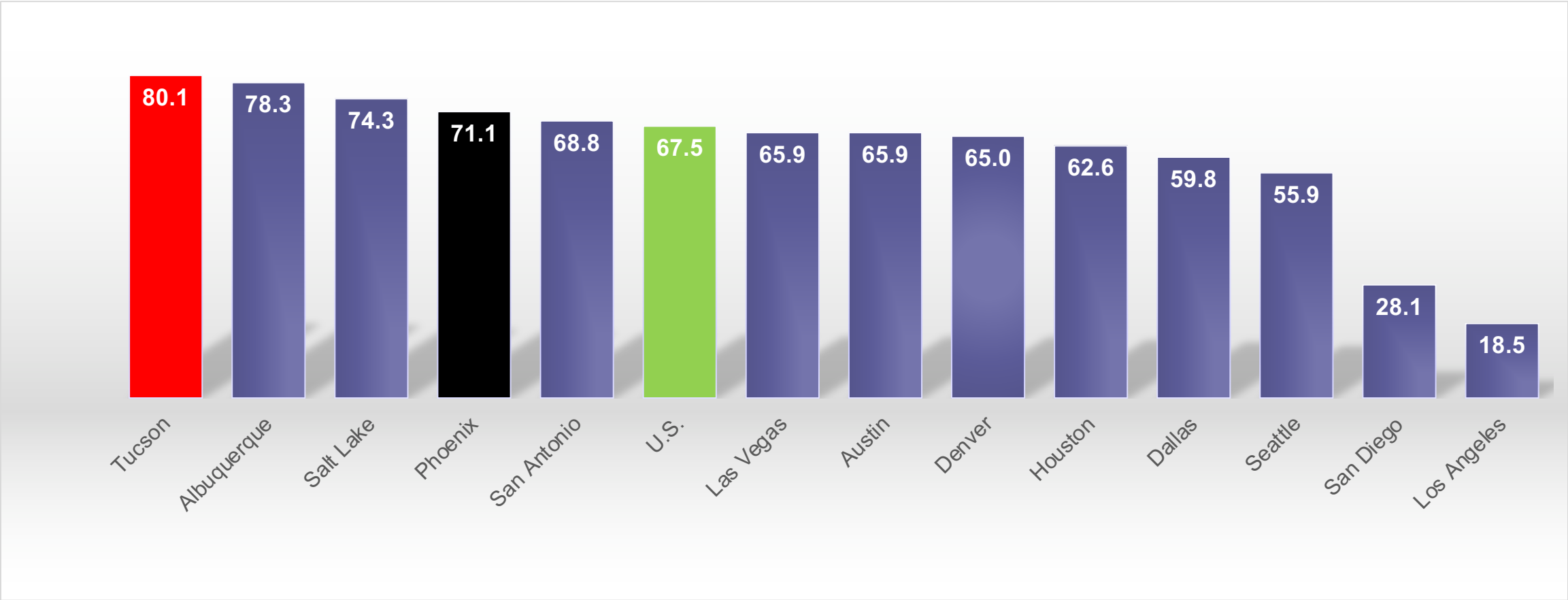
- People underwater is much lower
- Credit is much more stringent
 - No Subprime mortgages
 - FICO Scores are higher
 - Regulation is not as lax
- Demographic demand is much higher
- Amount of supply is much lower



Housing Opportunity Index

2015 Q1

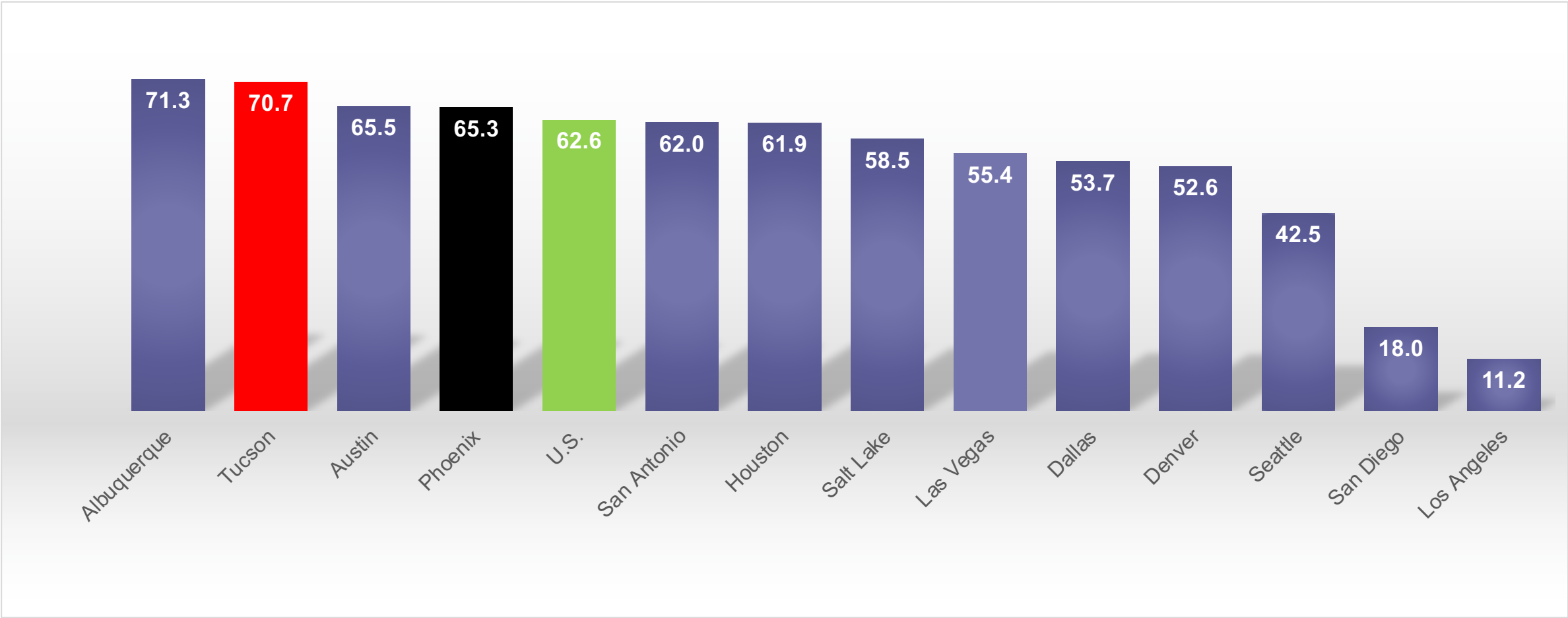
Source: NAHB/Wells Fargo



Housing Opportunity Index

2019 Q1

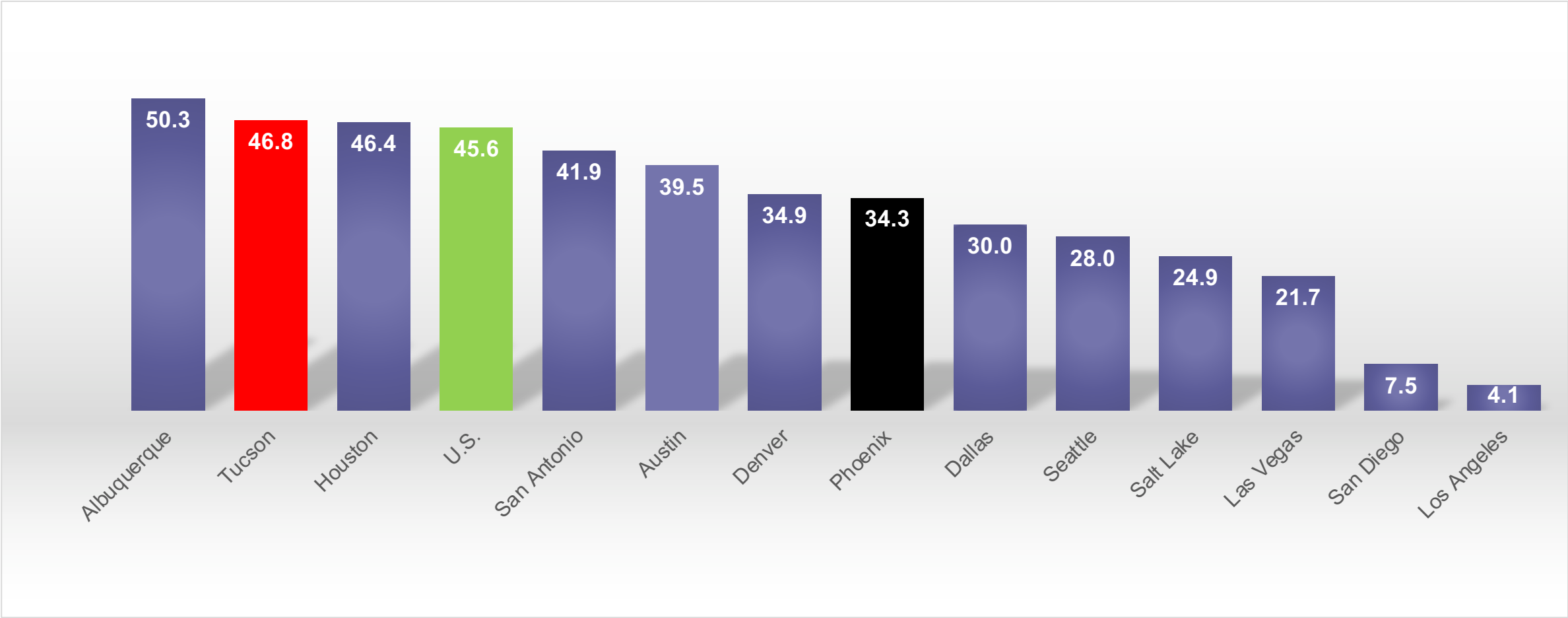
Source: NAHB/Wells Fargo



Housing Opportunity Index

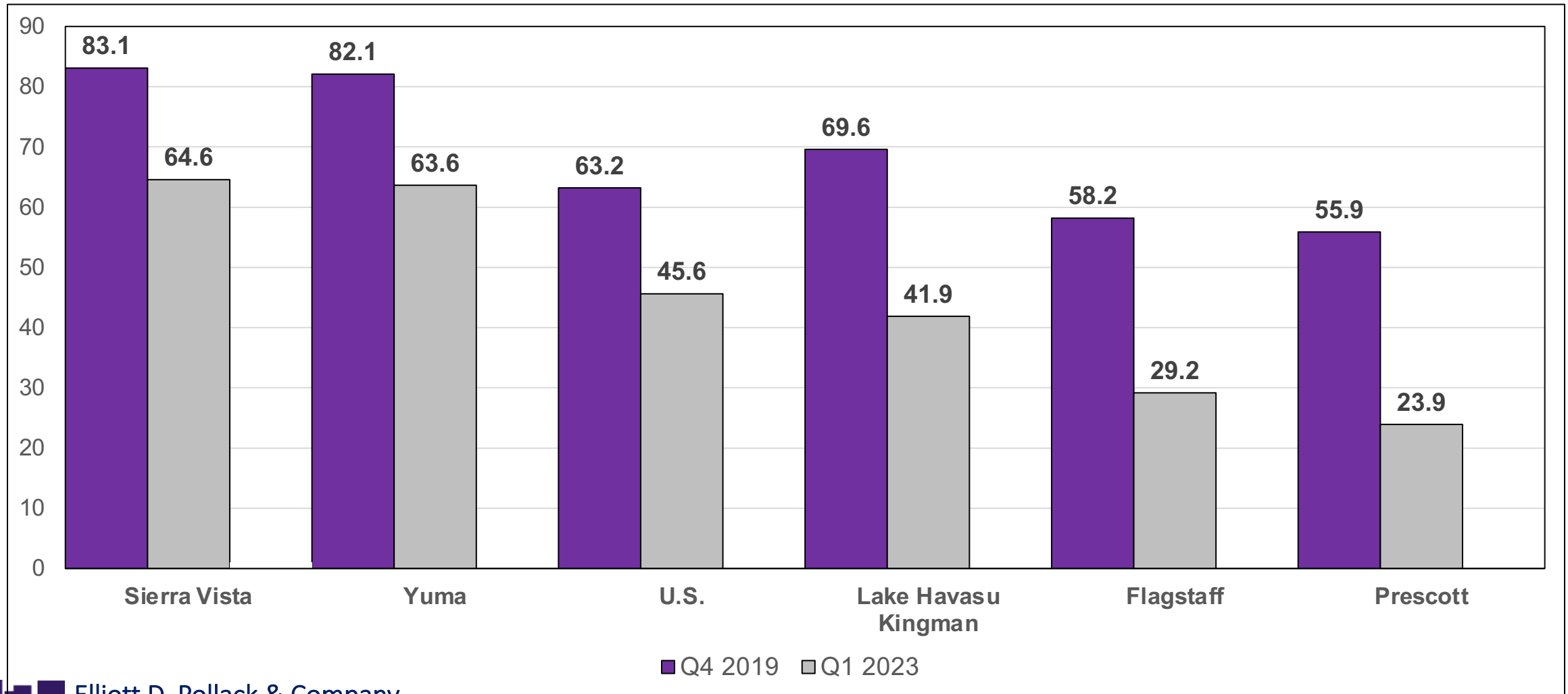
2023 Q1

Source: NAHB/Wells Fargo



Housing Opportunity Index – AZ Metro Areas

Source: NAHB/Wells Fargo

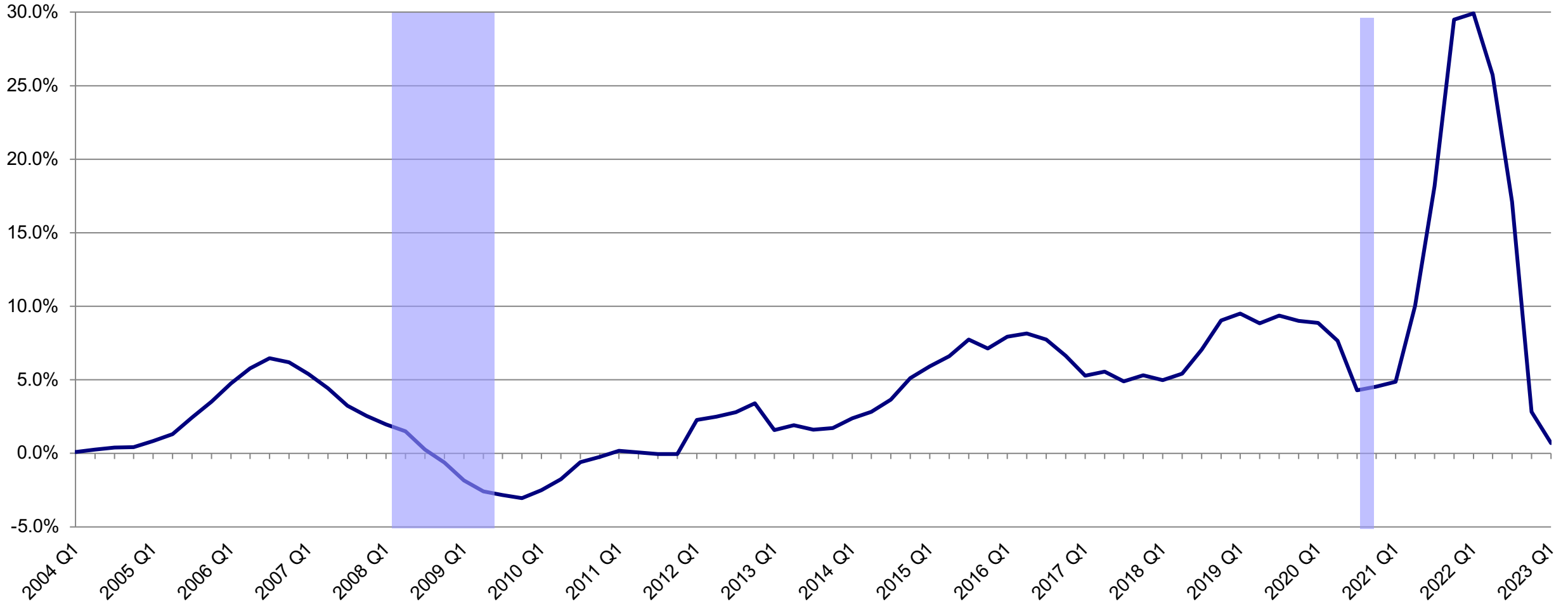


Greater Phoenix Multi-Family Average Rent Percent Change a Year Ago

2004 – 2023*

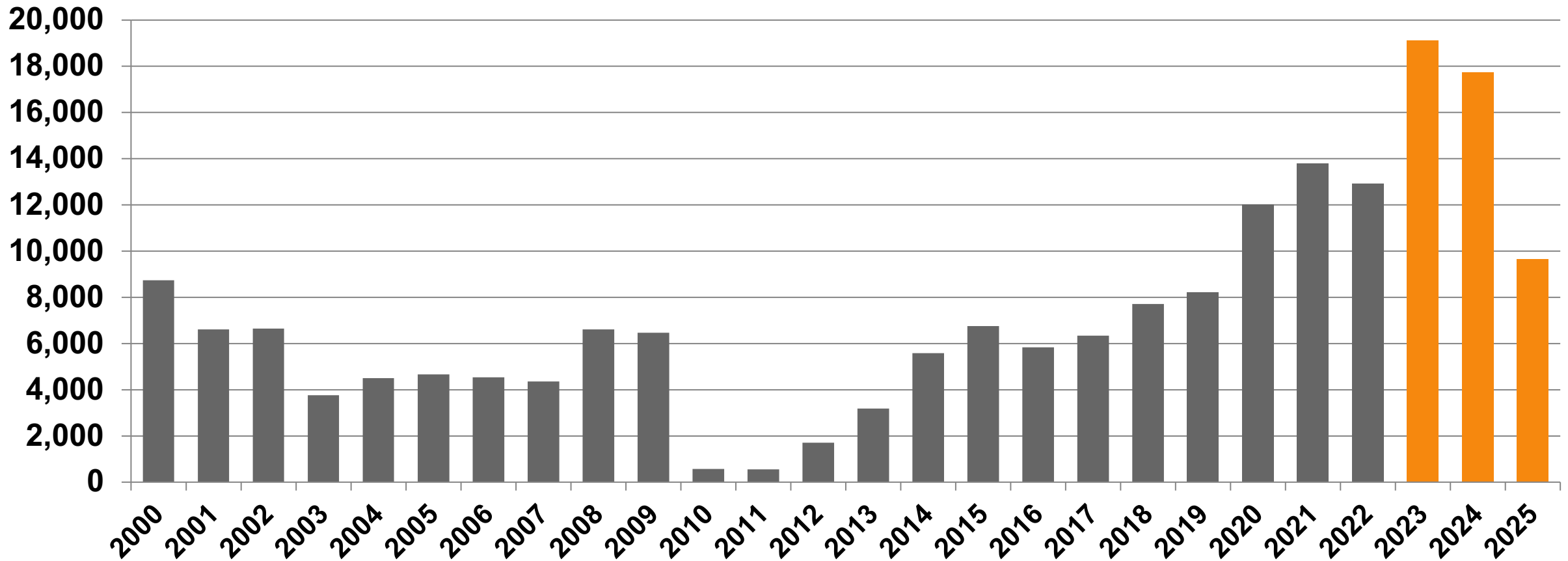
Source: RealData

 **Recession Periods**



Greater Phoenix Apartment Deliveries 2000-2022; Forecast 2023-2025

Source: RealData; Commercial Brokers; Elliott D. Pollack & Company



Top 7 Things That Can Be Done to End The Housing Shortage

1. **Build more housing units**
2. **Build more housing units**
3. **Build more housing units**
4. **Build more housing units**
5. **Build more housing units**
6. **Build more housing units**
7. **Build more housing units**



INDUSTRIAL

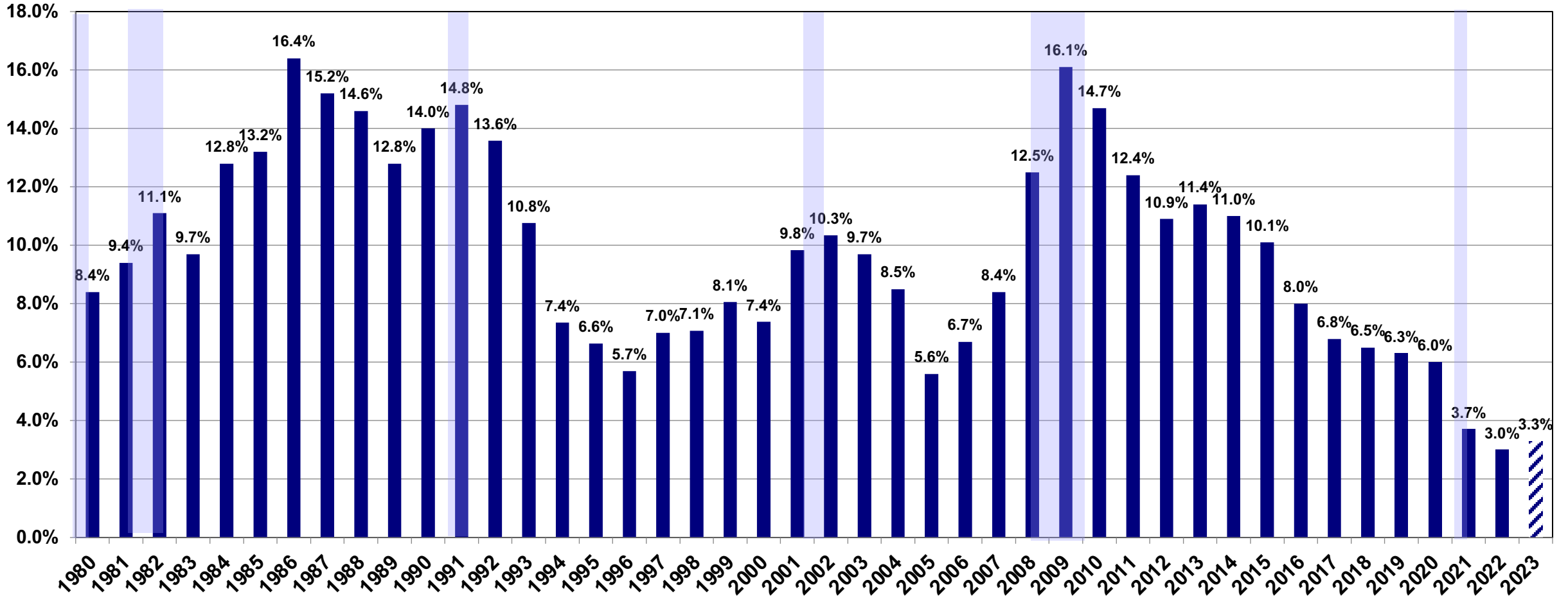


Industrial Space Vacancy Rates

Greater Phoenix 1980 – 2023*

Source: CBRE

Recession Periods



Greater Phoenix Industrial Market

Source: CBRE

2023 First Quarter.

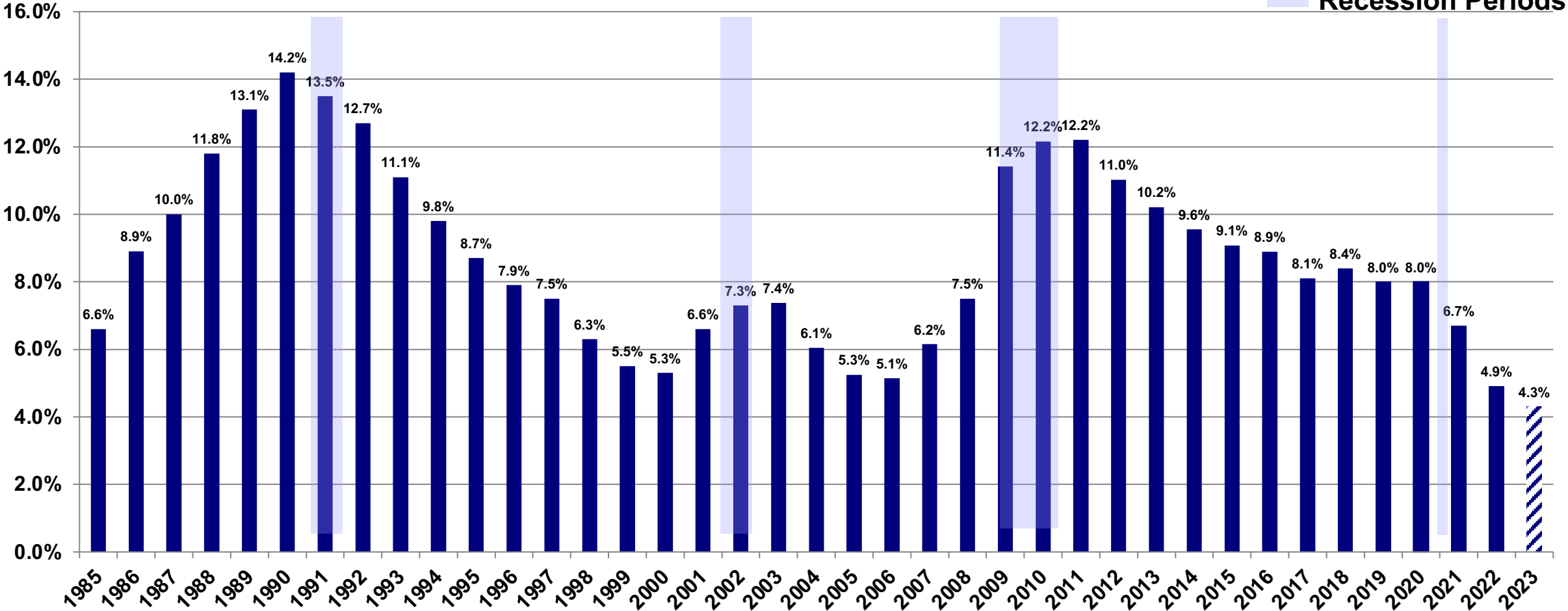
- Vacancy Rate 3.3%
- 1Q 2022 Asking Rate: \$0.99
- 1Q 2023 Asking Rate: \$1.14
- Under Construction 45.9 million sq. ft.
- YTD Net Absorption 4.0 million sq. ft.

RETAIL



Retail Space Vacancy Rates Greater Phoenix 1985–2023*

Source: CBRE**



What to Expect This Year & Next?



Arizona Summary

- The near term will be difficult, but absolutely necessary. The Fed needs to stay the course.
- Easing but tightening labor markets.
- Slower retail sales (temporarily).
- Inflation higher than U.S.
- Housing Affordability remains an issue.
- The long-term outlook is very good. The short term.....not so much.

Have a nice day!





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