



FIFTH THIRD BANK

# The Reckoning Continues

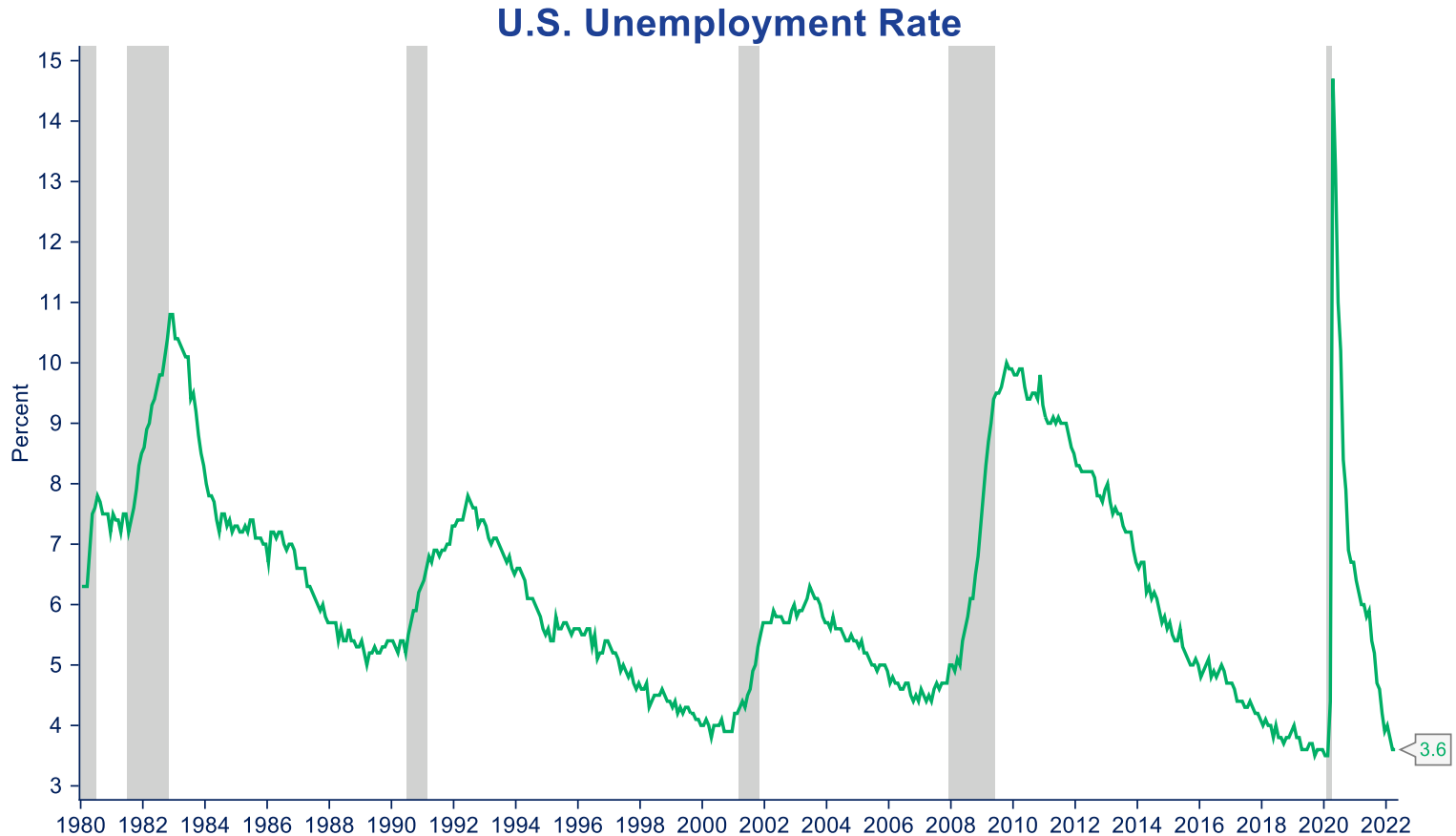
**Tom Jalics, CFA**

**Director, Chief Market Strategist**

# Executive Summary

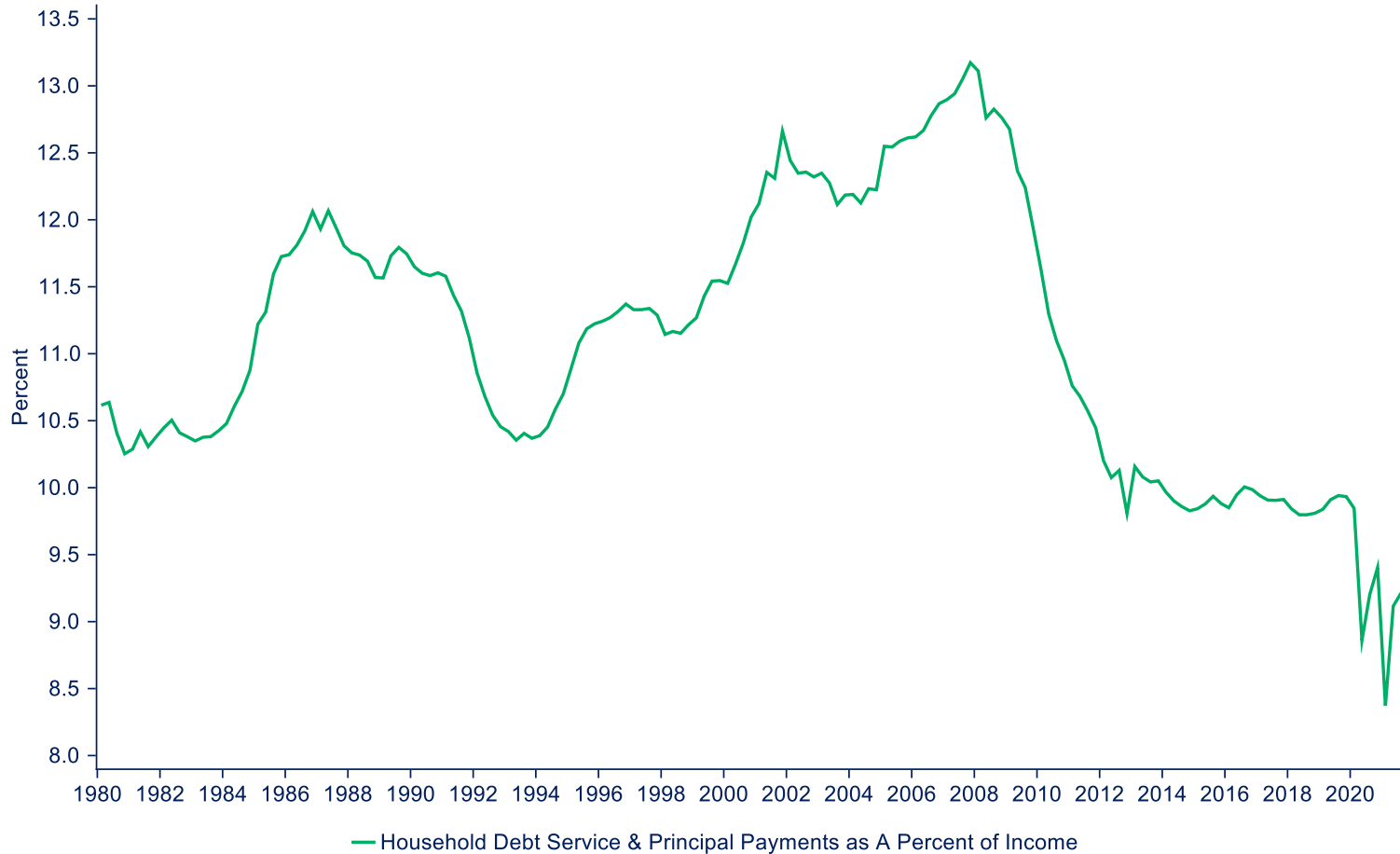
- Elements remain in place for solid, albeit slowing, domestic economic growth in 2022, driven by an empowered consumer. The business community and investors must confront the structural damage to our workforce, our supply chains, our federal balance sheet, and our expectations of price stability. This reckoning will influence economic growth, government policy, and investment outcomes.
- The economic reckoning that is underway is driven by persistent inflation, which is the biggest risk to the domestic economy. Prospective inflation rates over the next several quarters will dictate the length and strength of the domestic economic cycle. The Federal Reserve is now an inflation fighter and has a narrow path to a successful outcome.
- While far from over, we see signs that inflationary pressures and supply chain problems may have peaked. Inflation is likely to find a future steady state which is higher than the inflation experience over the past 10 years. Labor markets represent the single biggest challenge for growth and containing inflation.
- Prospective inflation rates over the next several quarters will dictate the length and strength of the domestic economic cycle. If inflation moderates, we could expect several more years of continued economic growth. If inflation doesn't moderate, risks of a domestic recession in late 2023 are a real possibility.

# Support for growth: consumer economy



Source: Macrobond, BLS, as of 5/18/2022  
Data from 1929-1947: annual unemployment rate, 14 years and over  
Data from 1948 to current: monthly unemployment rate, 16 years and over

# Consumer resiliency despite higher rates



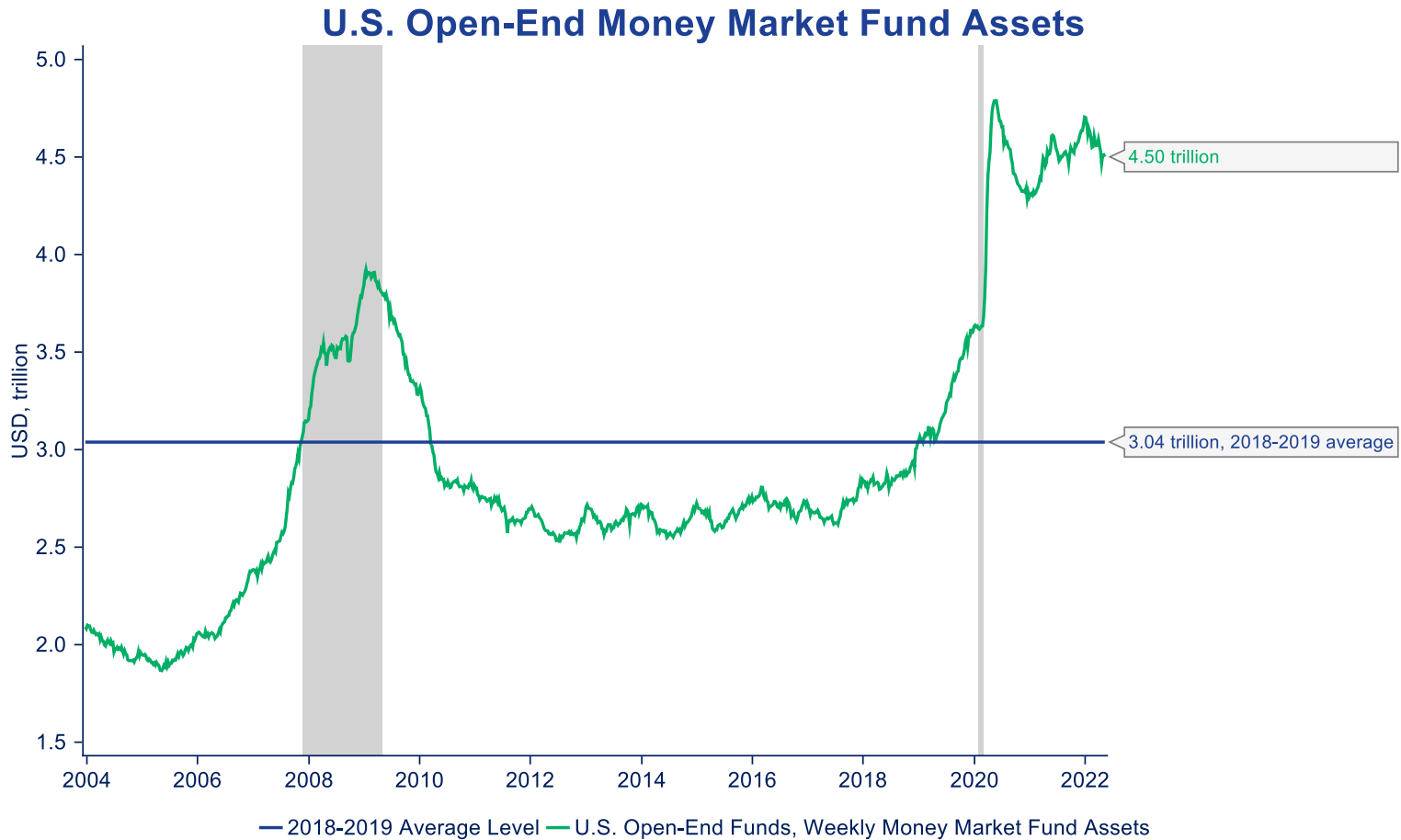
Source: Macrobond, Fed, as of 5/18/2022

# Support for growth: monetary policy shifting but still supportive



Source: Macrobond, Fed, as of 5/18/2022

# Support for growth: money on the sidelines



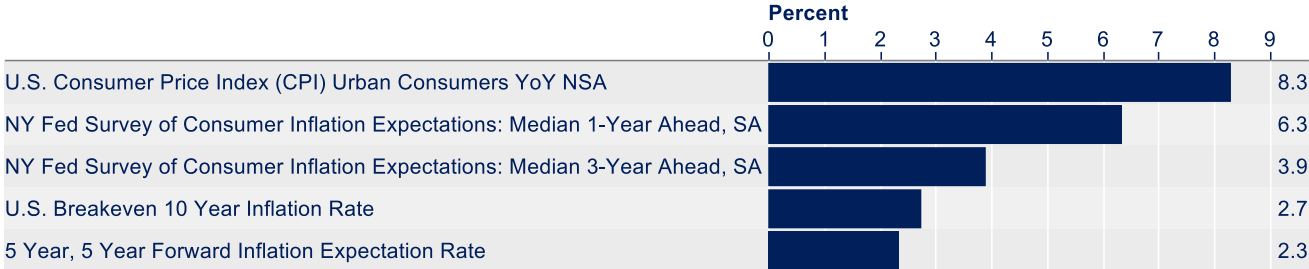
Source: Macrobond, ICI, as of 5/18/2022

# Risk to growth: inflation is persistently high



Source: Macrobond, Bloomberg, as of 5/18/2022

# The risk of inflationary psychology

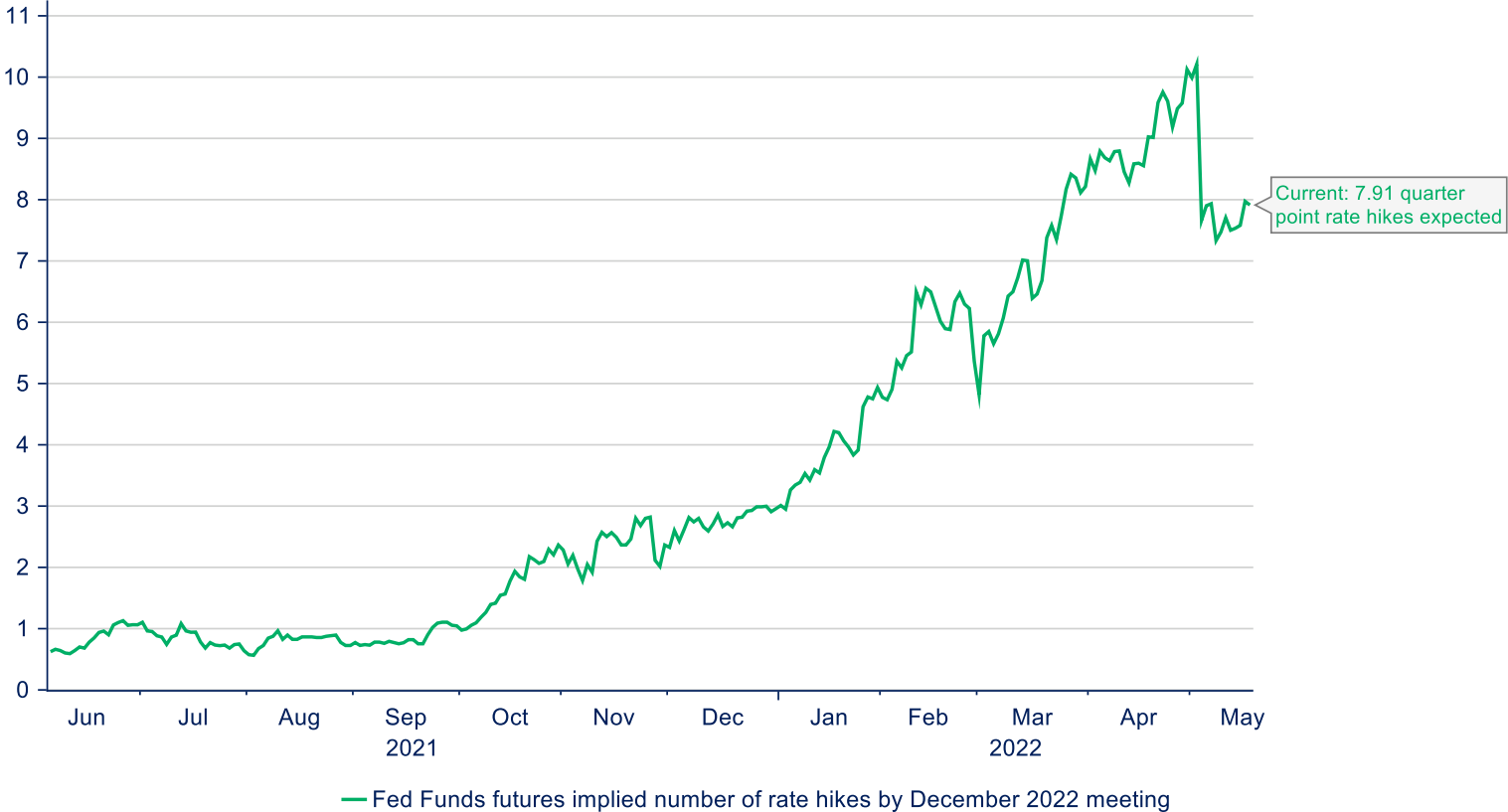


Source: Macrobond, Bloomberg, as of 5/18/2022



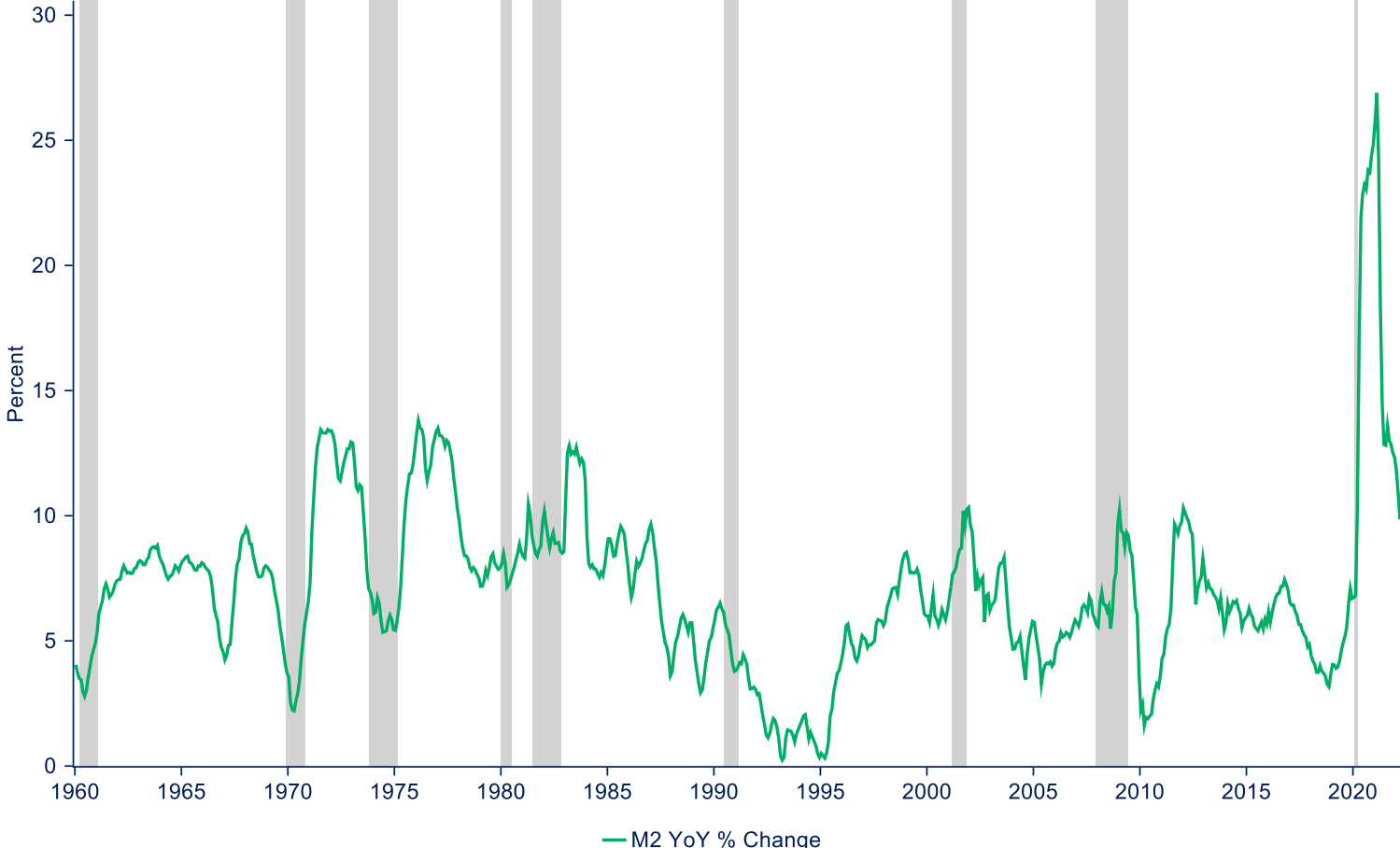
# A Fed on the warpath

## Market-implied number of 25bp rate hikes expected by year-end 2022



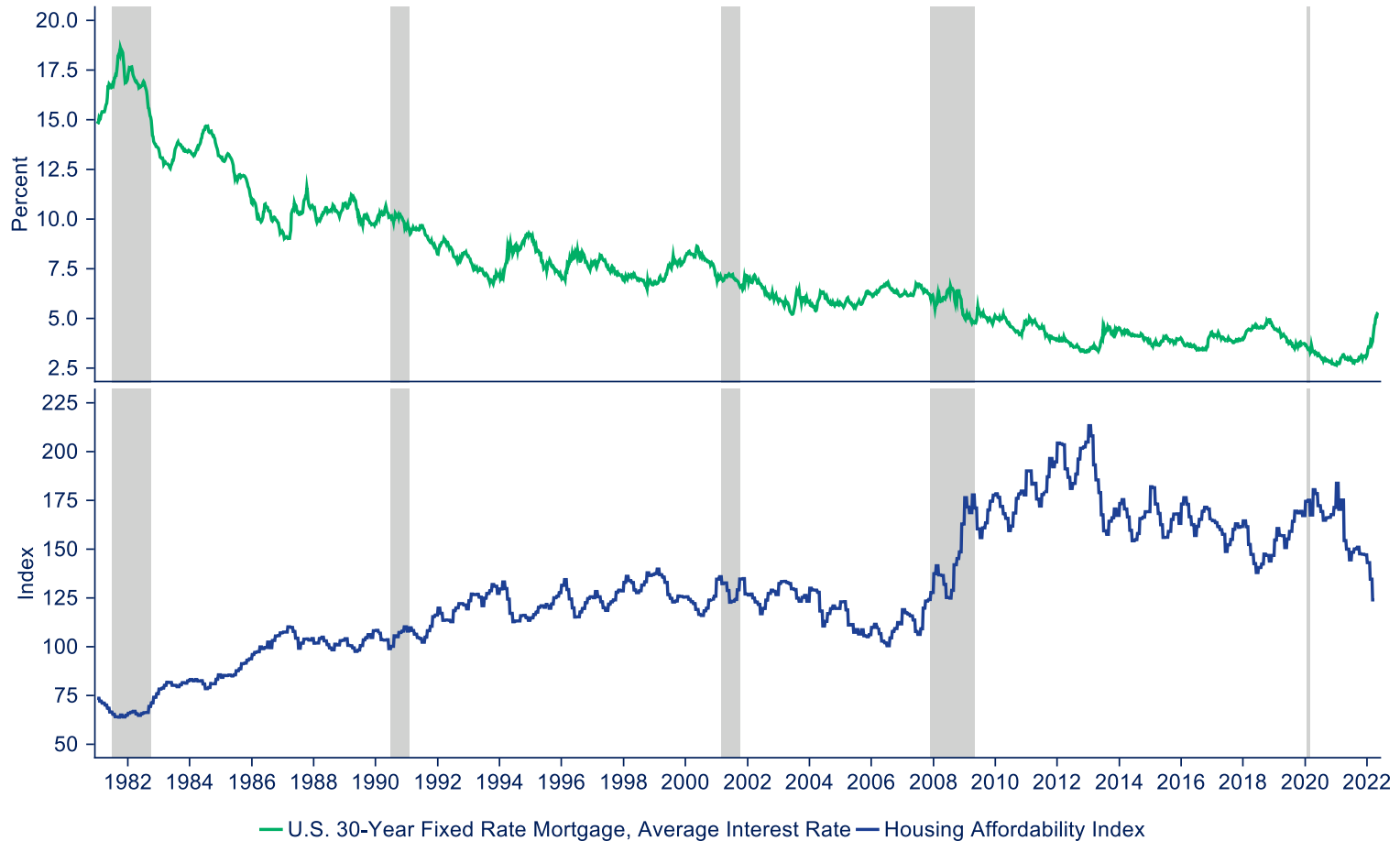
Source: Macrobond, Bloomberg, as of 5/18/2022

# The money supply surge is over



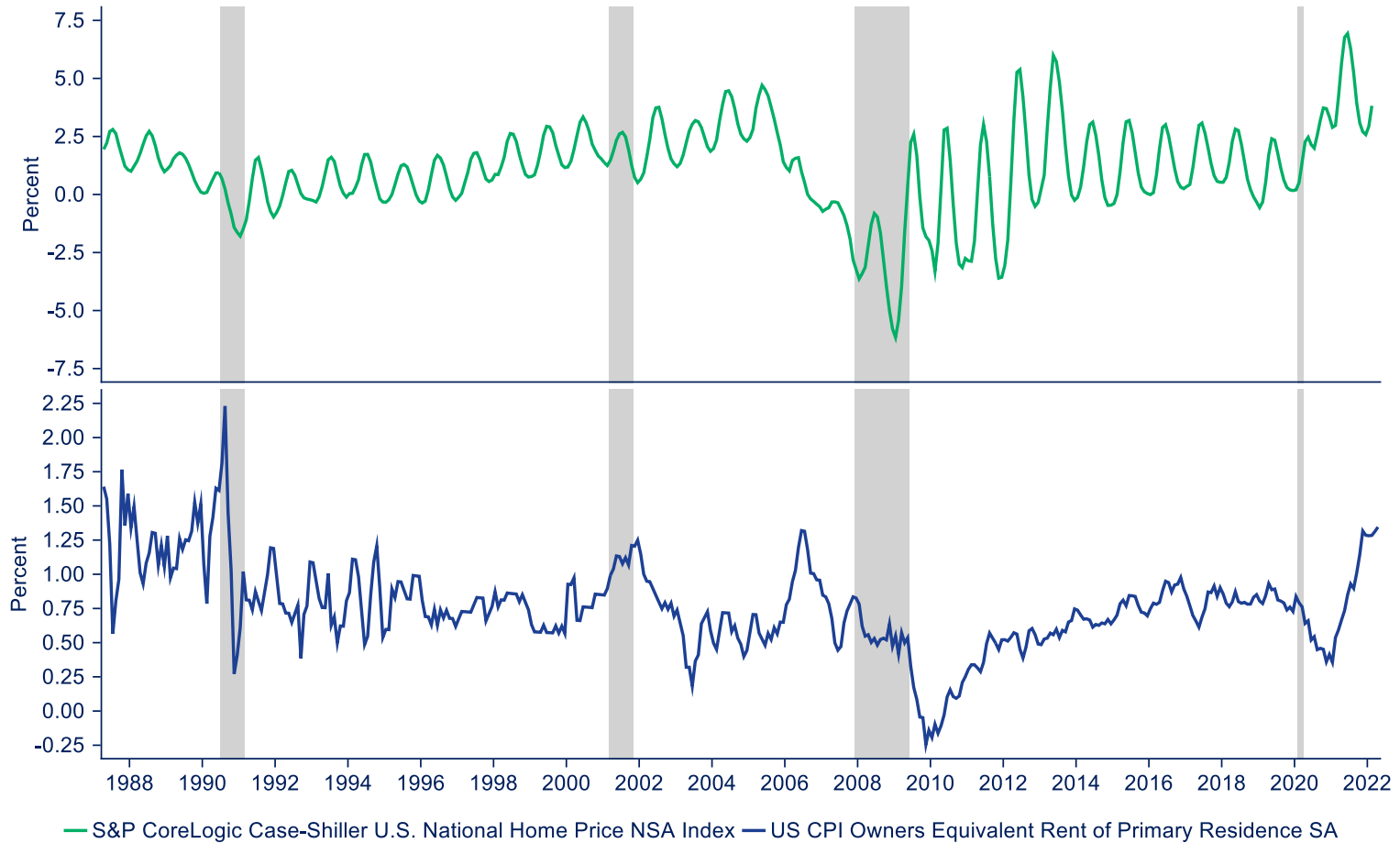
Source: Macrobond, Bloomberg, as of 5/18/2022

# Mortgage rates constrain home inflation



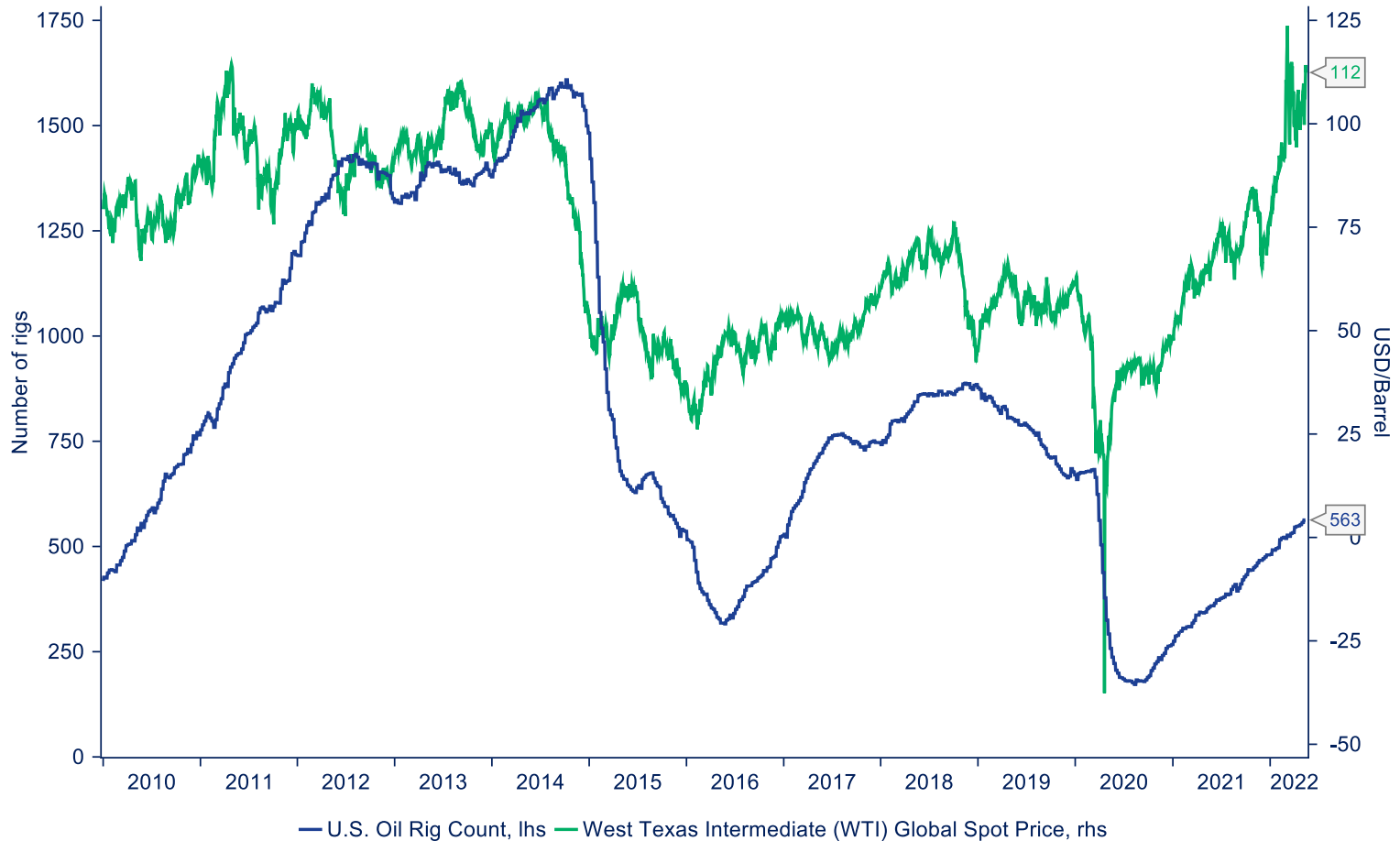
Source: Macrobond, Freddie Mac, NAR, as of 5/18/2022

# Housing inflation outlook: OER turning



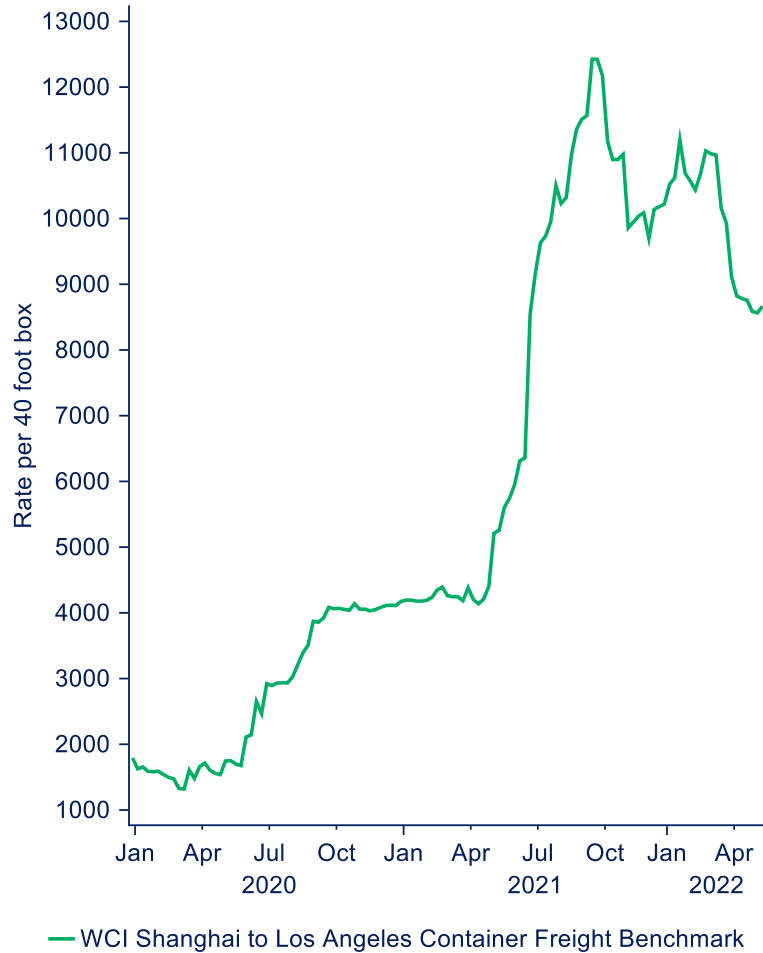
Source: Macrobond, Bloomberg, as of 5/18/2022

# Energy inflation outlook: rising production

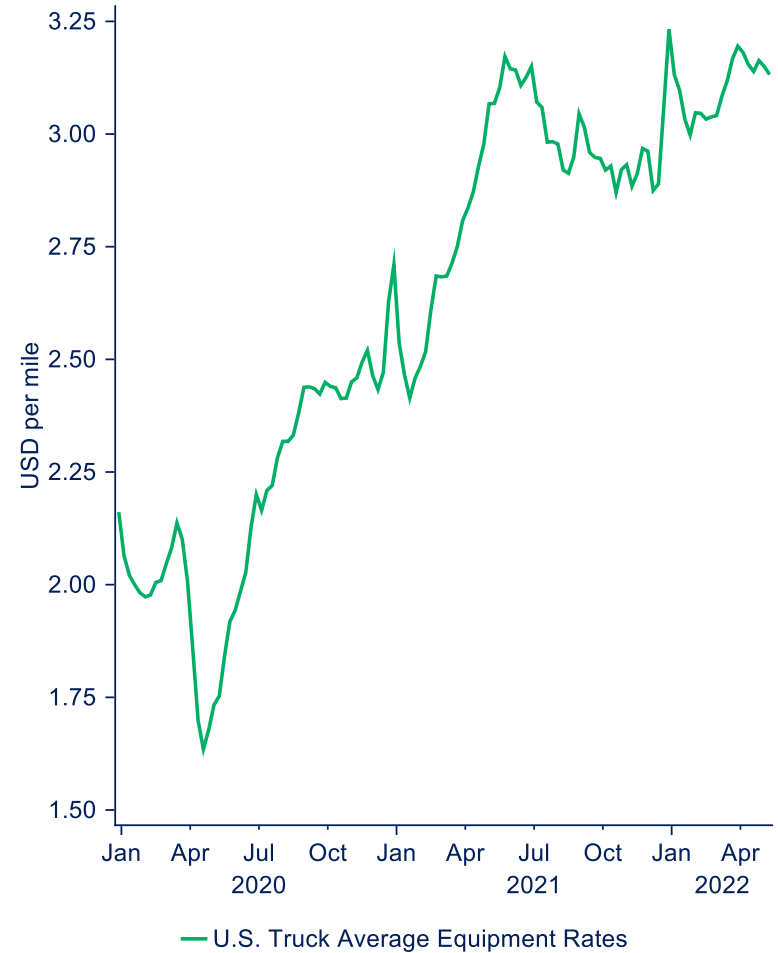


Source: Macrobond, Baker Hughes, as of 5/18/2022

# Inflation outlook: supply chain stabilization

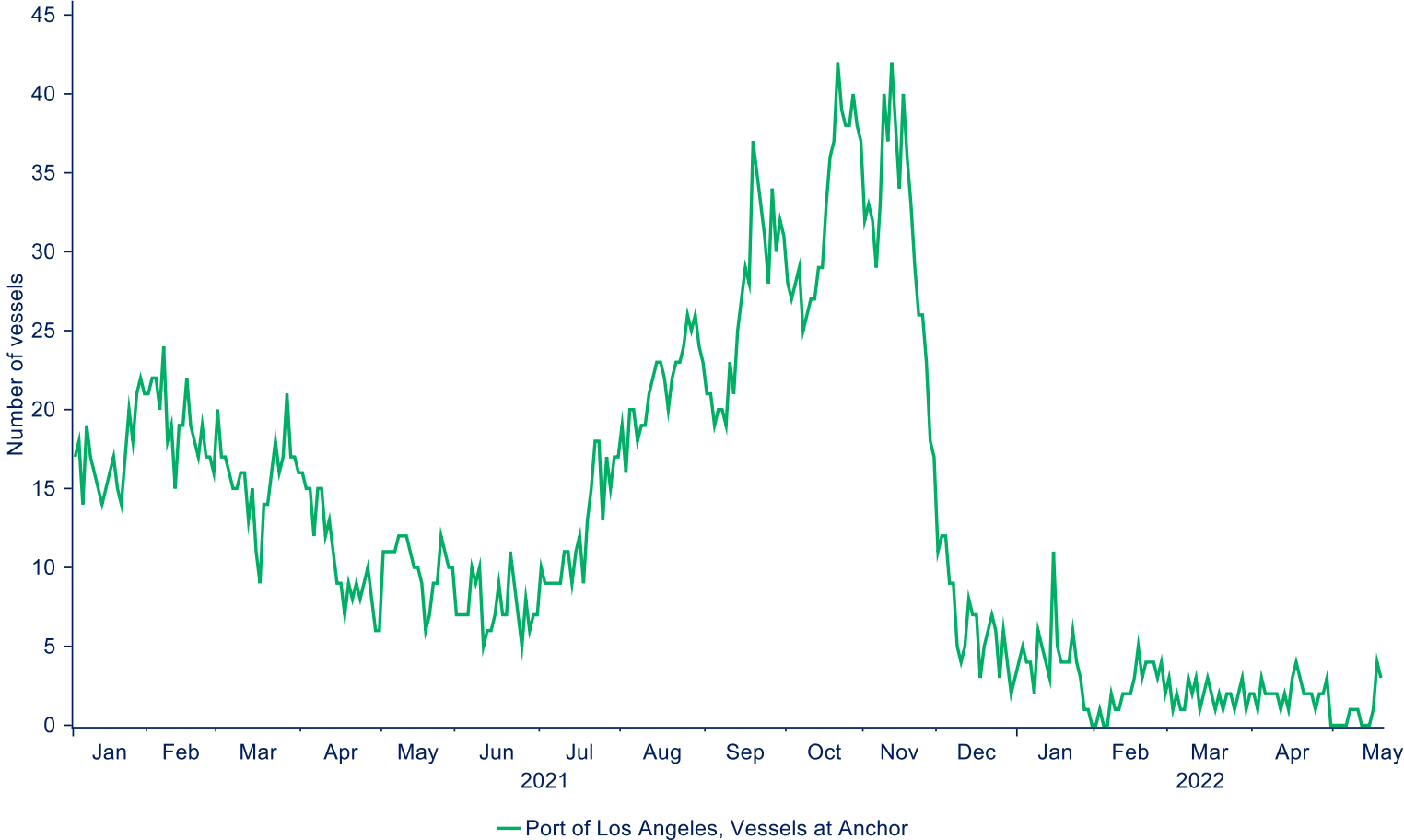


Source: Macrobond, Bloomberg, Cornerstone Macro Research as of 5/18/2022



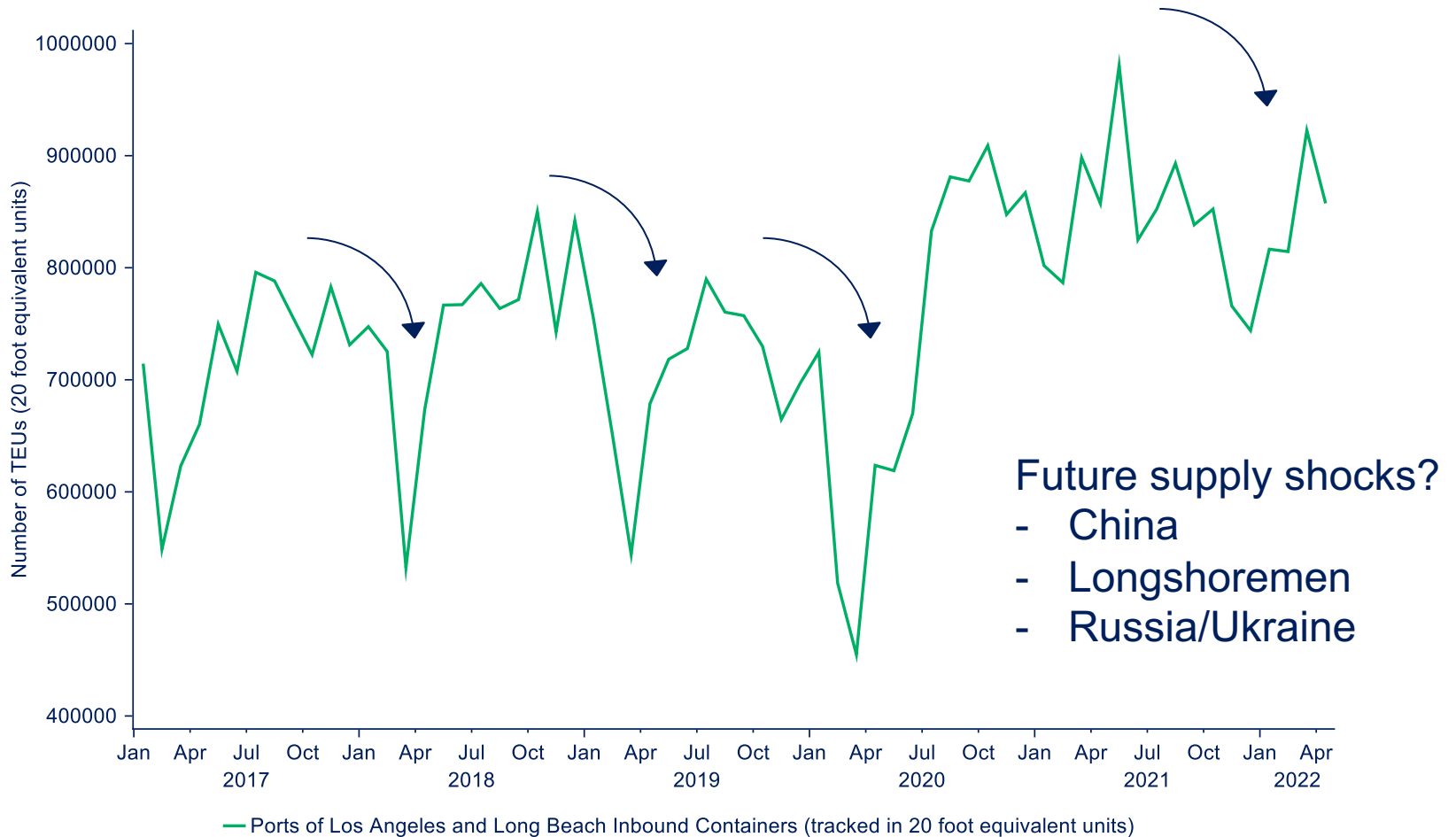
Source: Macrobond, Bloomberg, Truckstop.com, Cornerstone Macro as of 5/18/2022

# Inflation outlook: supply chain stabilization



Source: Macrobond, Port of Los Angeles, as of 5/18/2022

# Supply chain: not out of the woods yet



Source: Macrobond, Bloomberg, Ports of Los Angeles and Long Beach, Cornerstone Macro, as of 5/18/2022



# Inflation outlook: inventories building



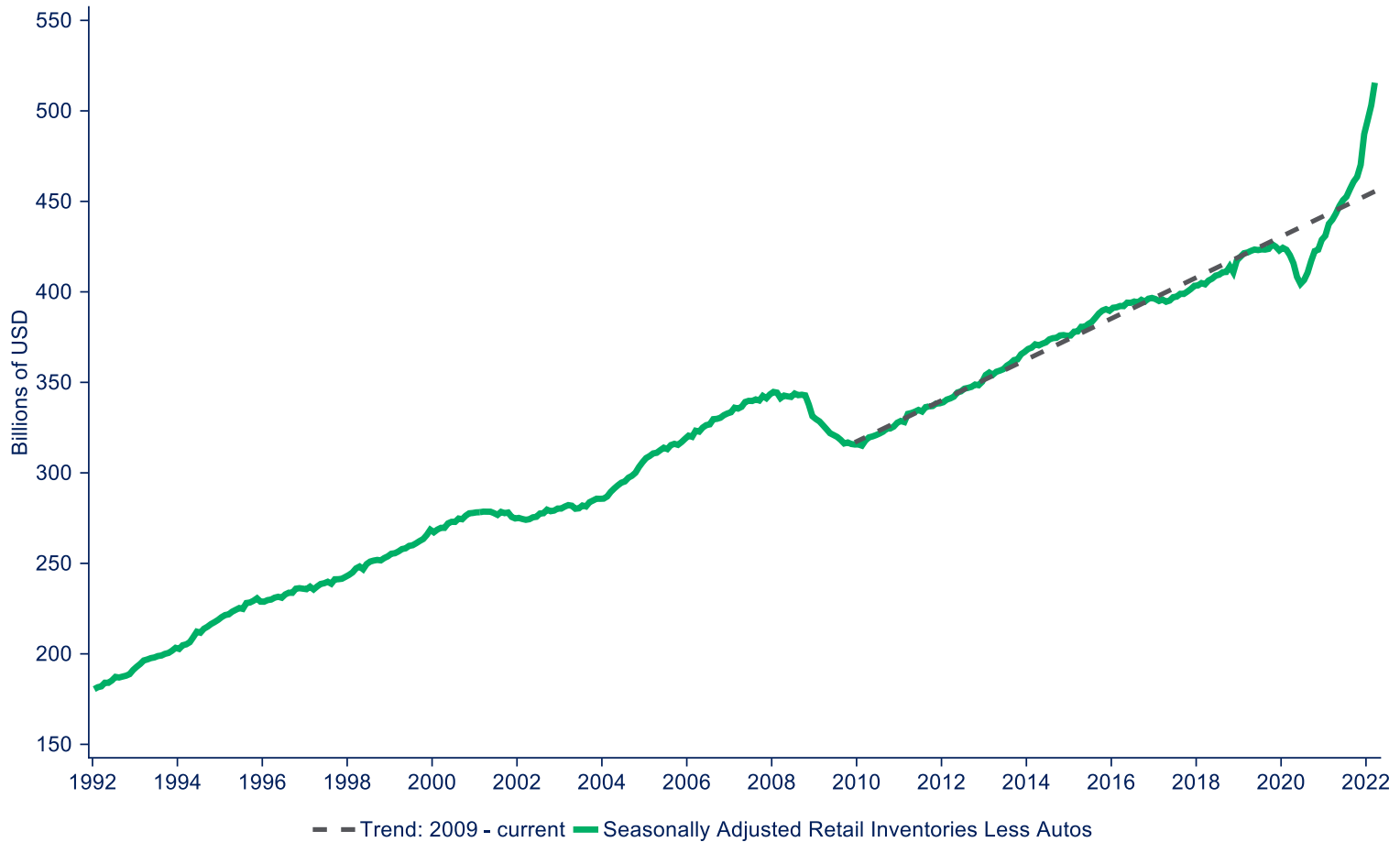
Source: Macrobond, U.S. Census Bureau, as of 5/18/2022

# Inflation outlook: inventory/sales ratio bottoming



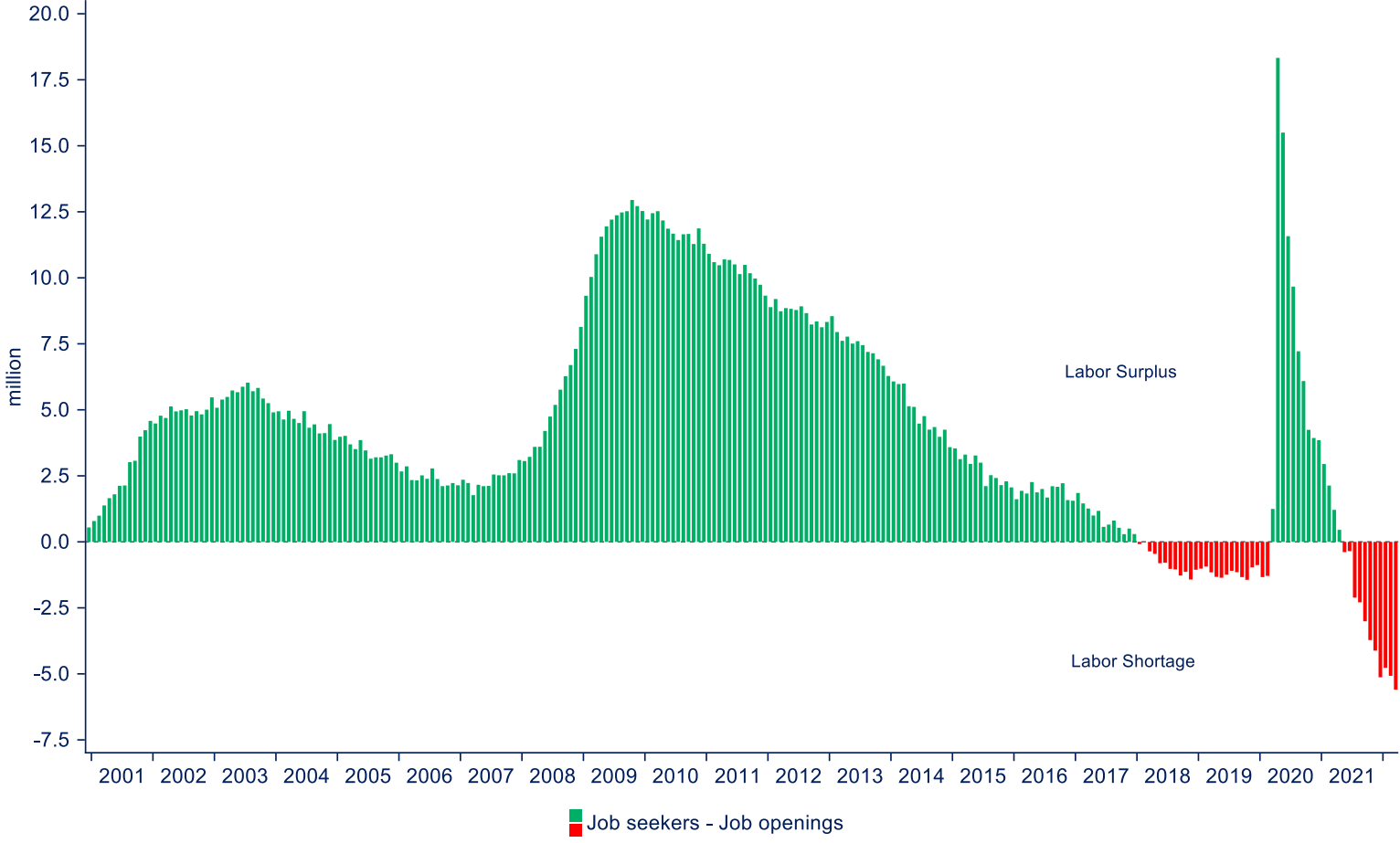
Source: Macrobond, U.S. Census Bureau, as of 5/18/2022

# Ex-auto inventories support disinflation



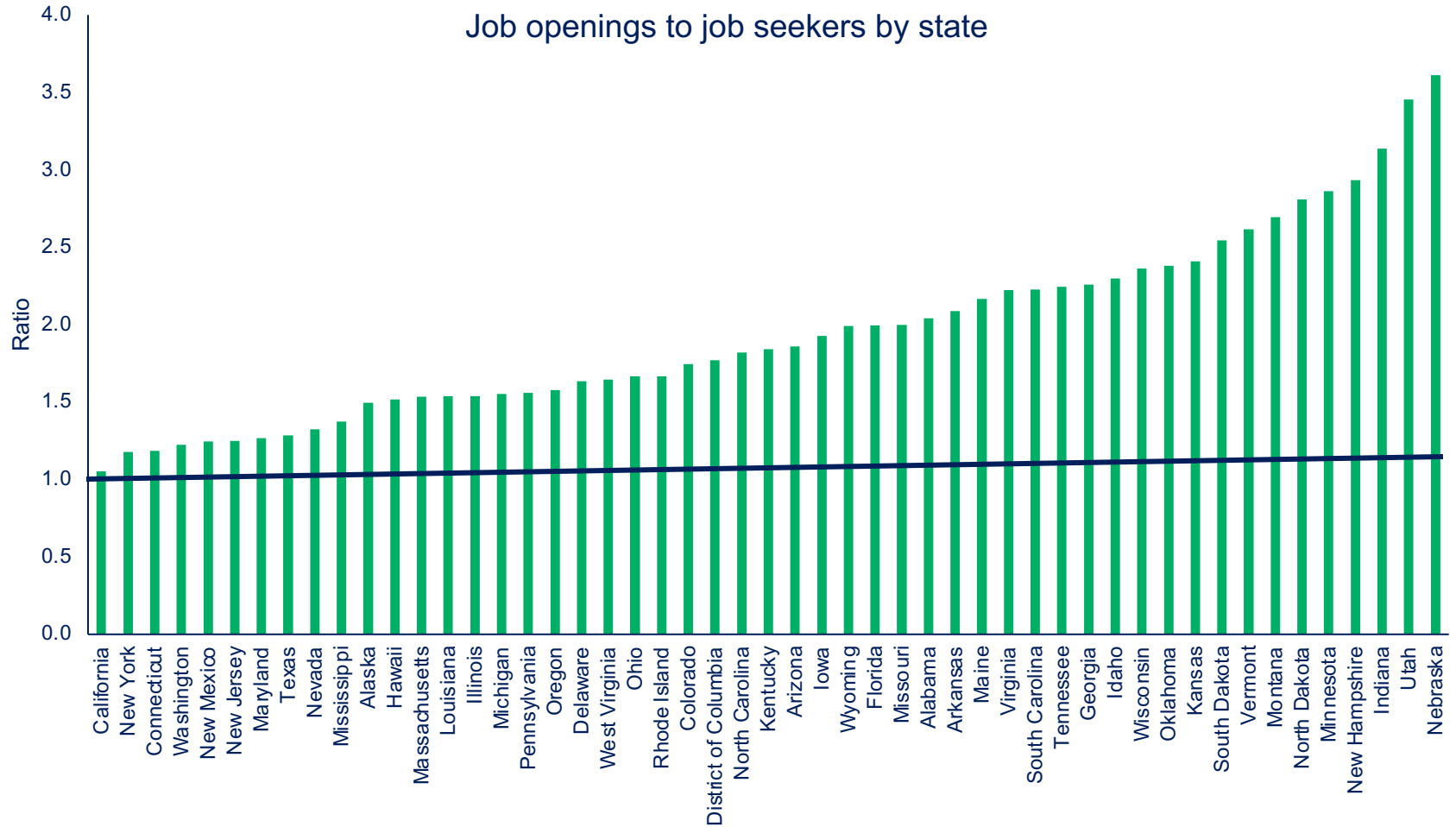
Source: Macrobond, Bloomberg, as of 5/18/2022

# A historic labor gap



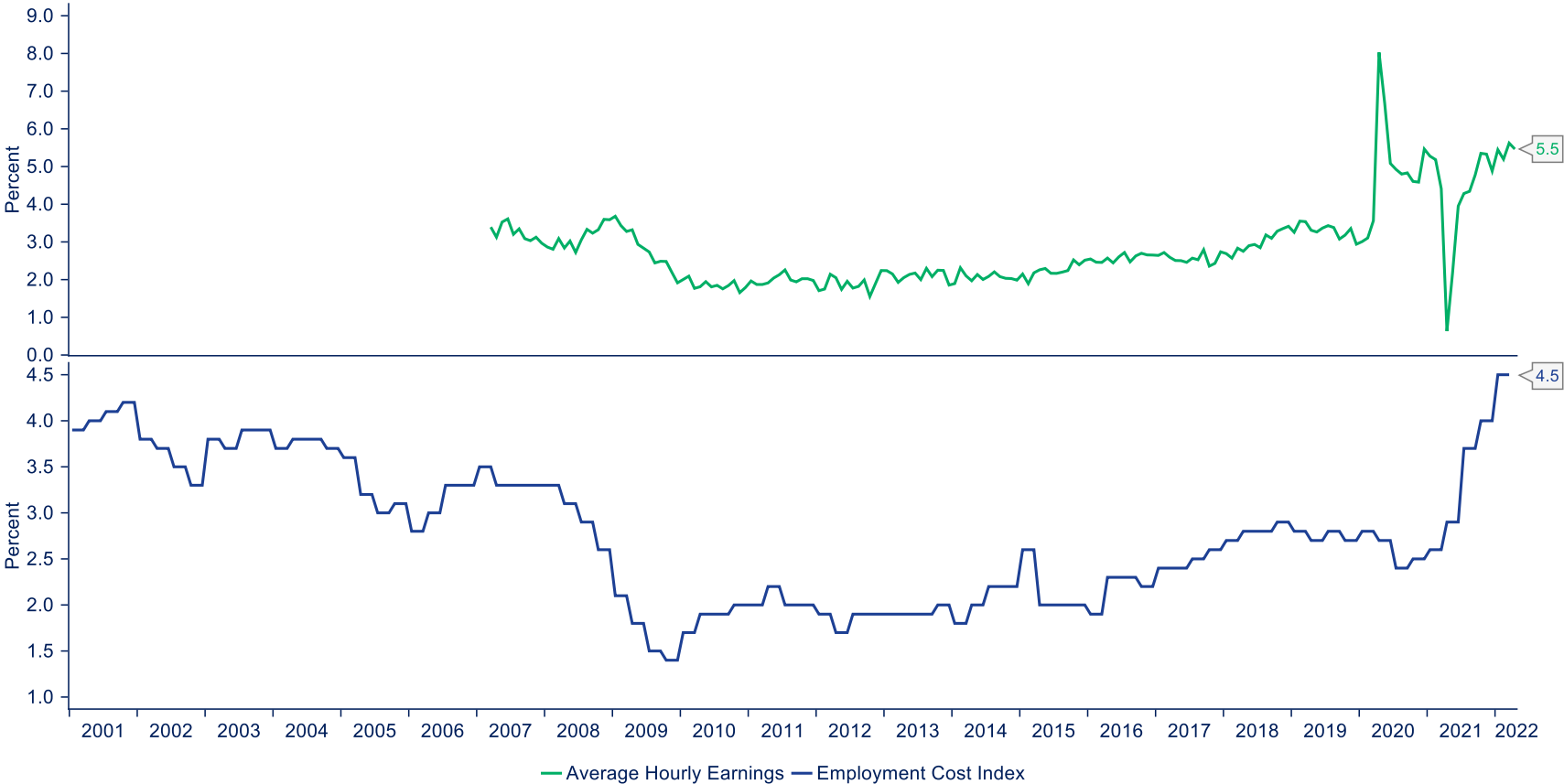
Source: Macrobond, BLS, as of 5/18/2022

# No relief for employers



Source: Bureau of Labor Statistics, as of 1/31/22

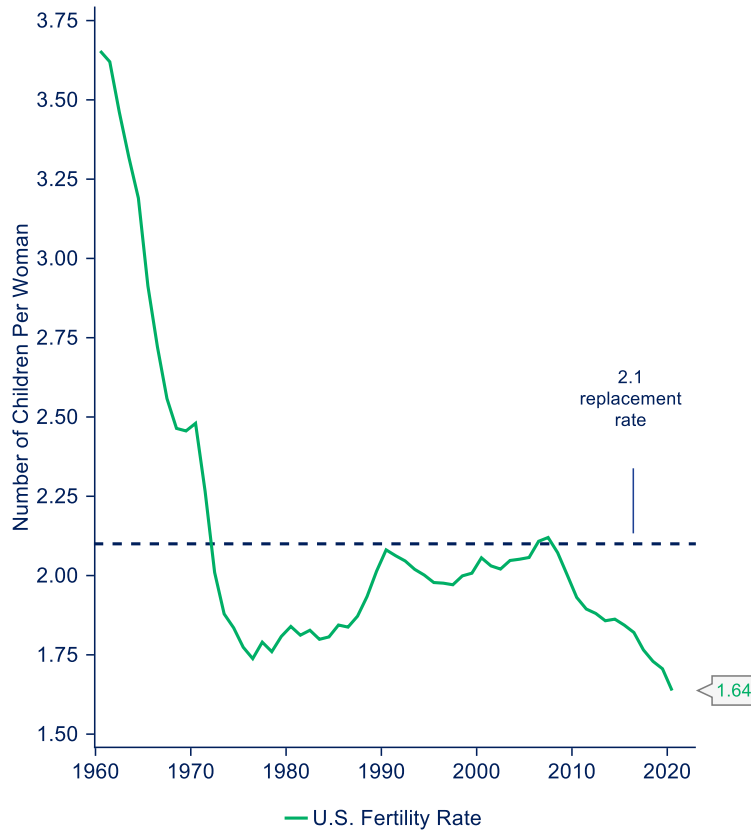
# Wage growth vs. compensation cost



Source: Macrobond, Bloomberg BLS, as of 5/18/2022

# Labor: the multi-decade challenge

## Structural issues

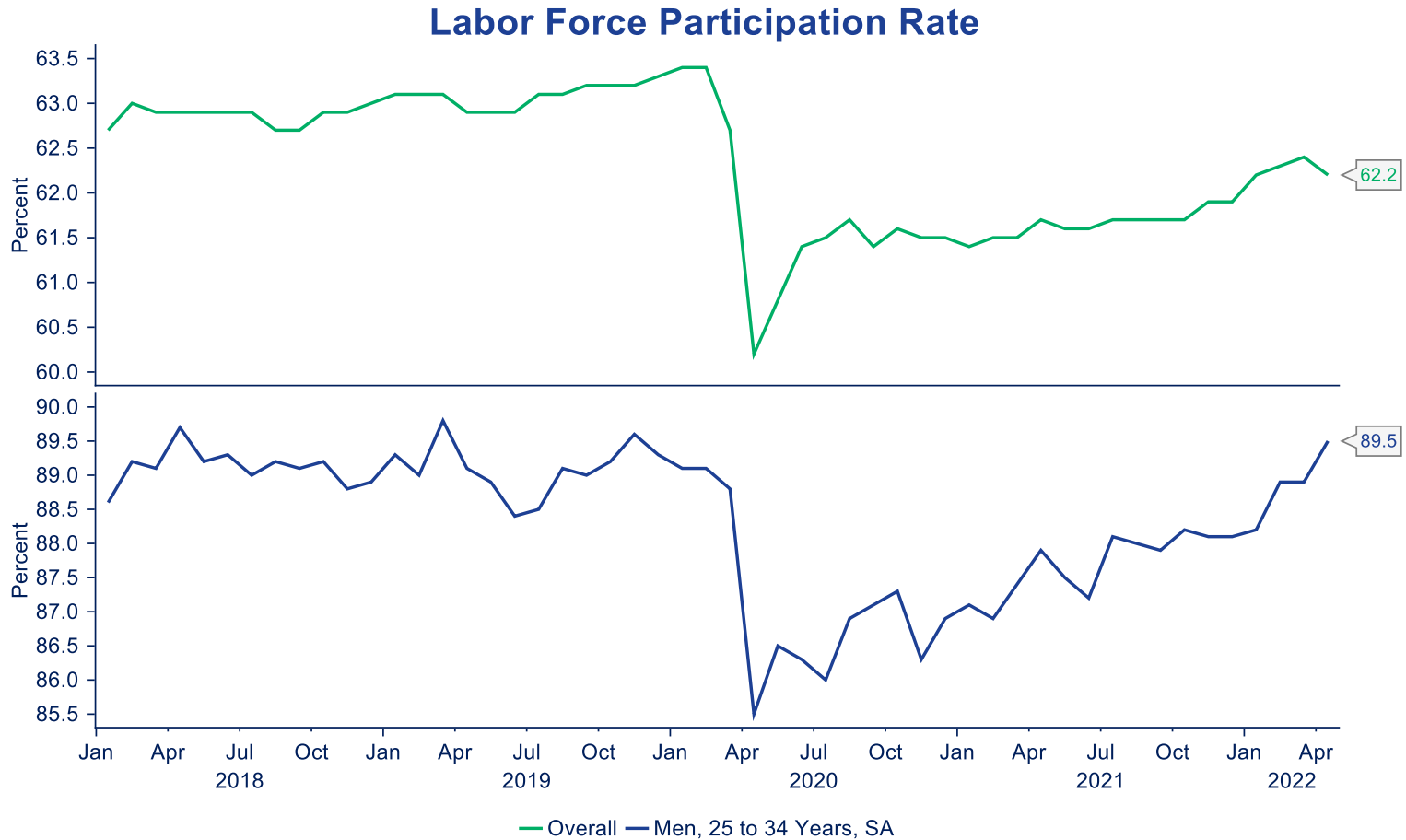


Source: Macrobond, World Bank, as of 5/18/2022

## Employers can help themselves

- Eliminate unnecessary barriers
- Flexibility for working parents
- Pathways for older workers
- Establish non-traditional talent pipelines

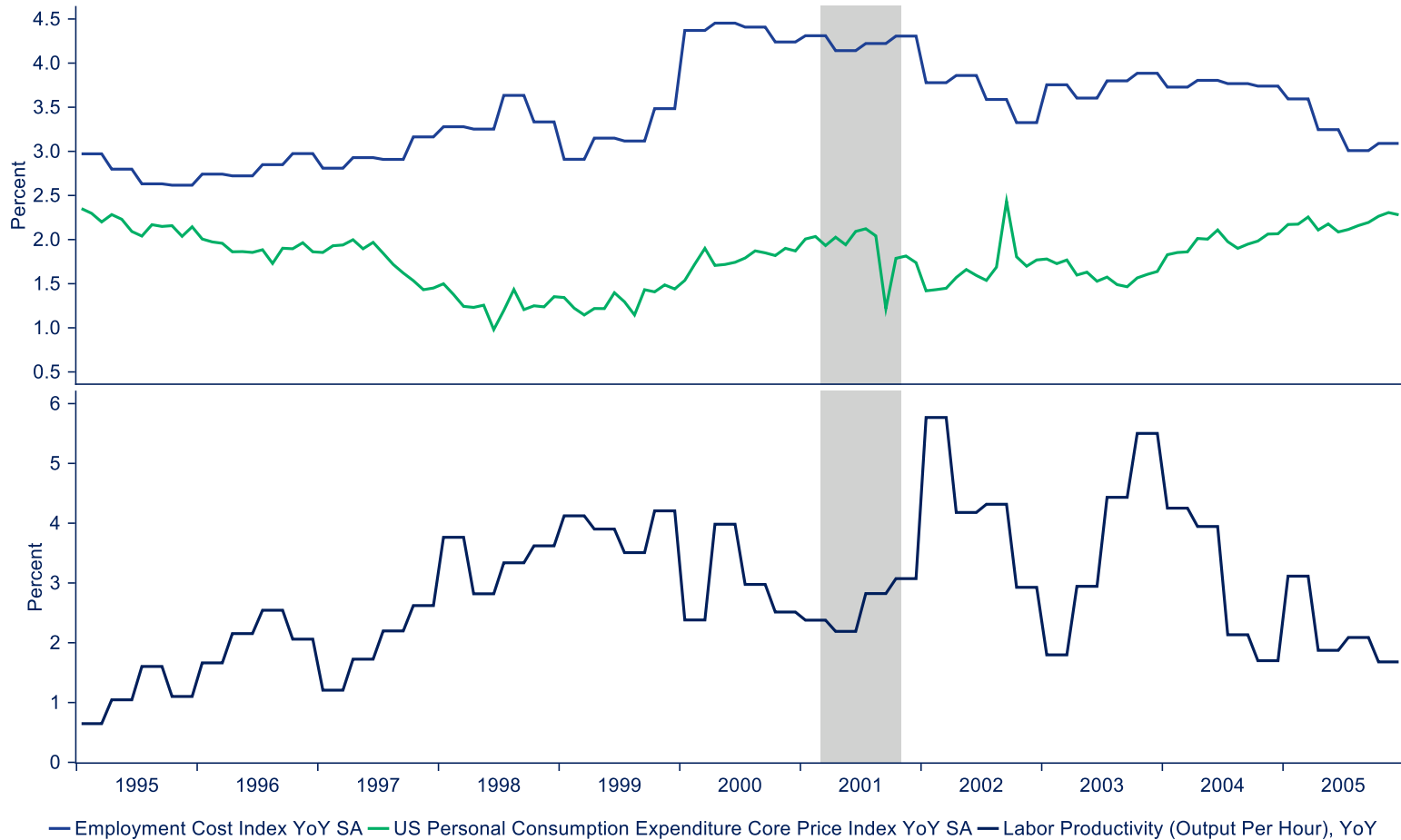
# Labor market healing



Source: Macrobond, BLS, as of 5/18/2022

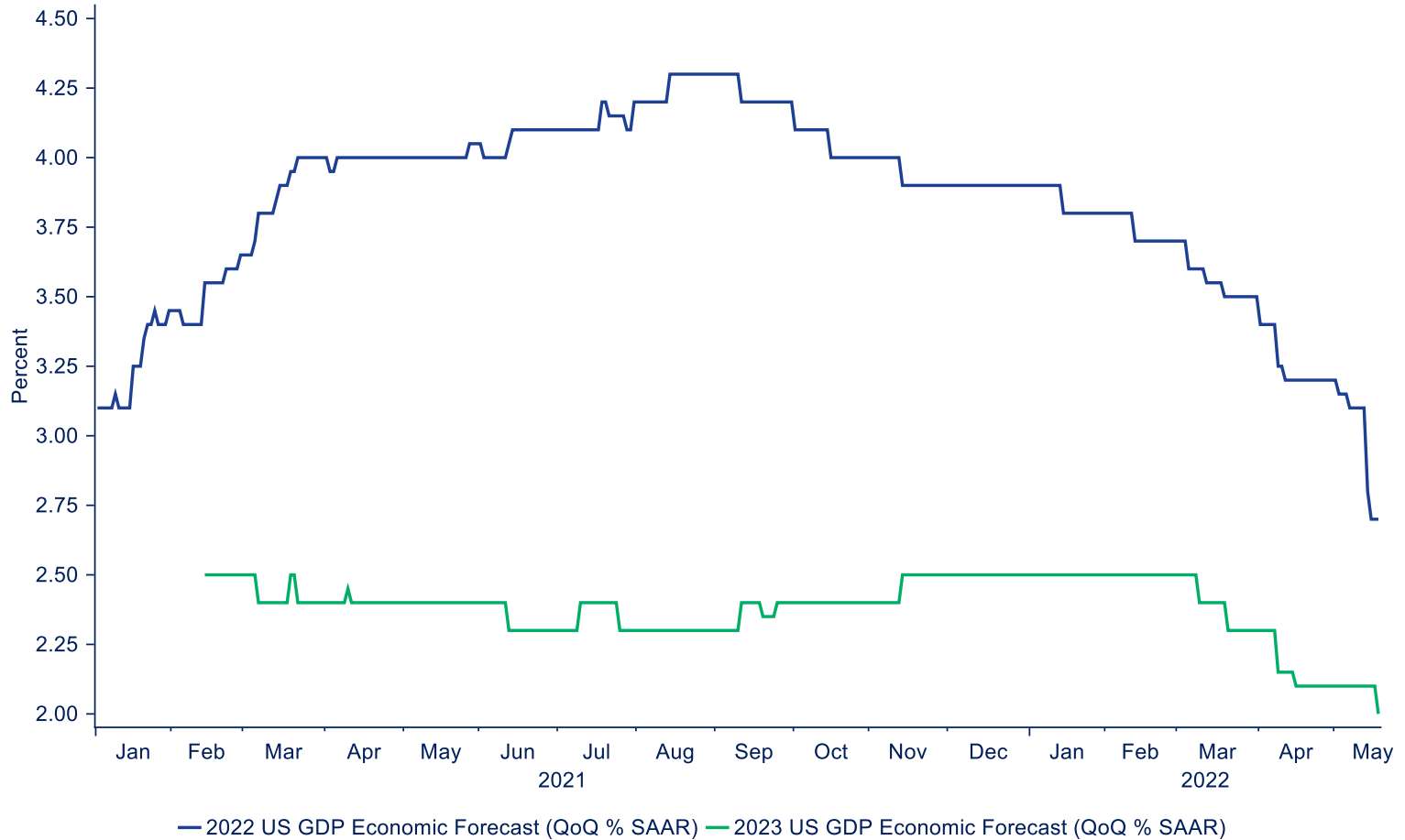


# Productivity offsets labor costs



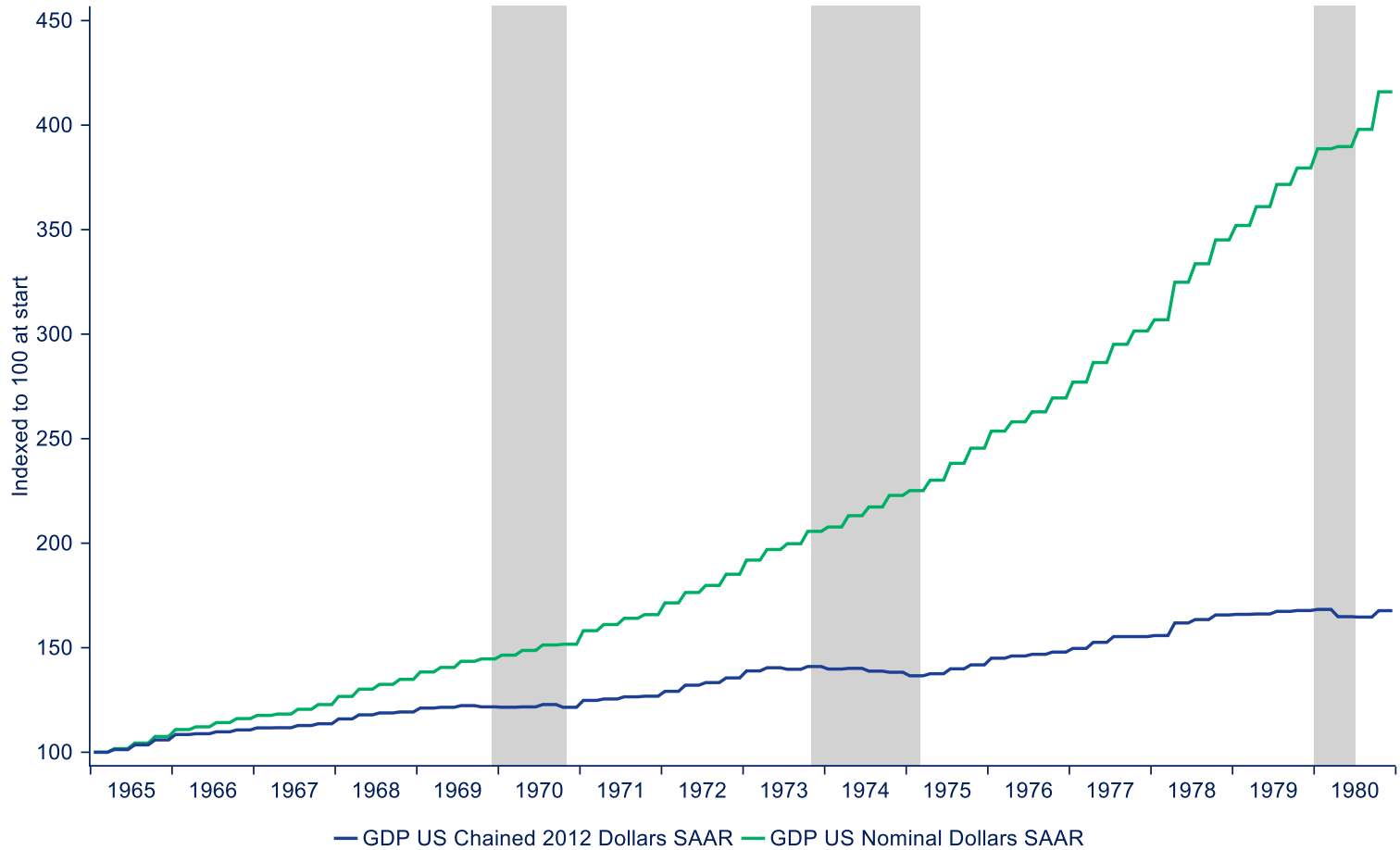
Source: Macrobond, BLS, as of 5/18/2022

# Forward growth expectations falling



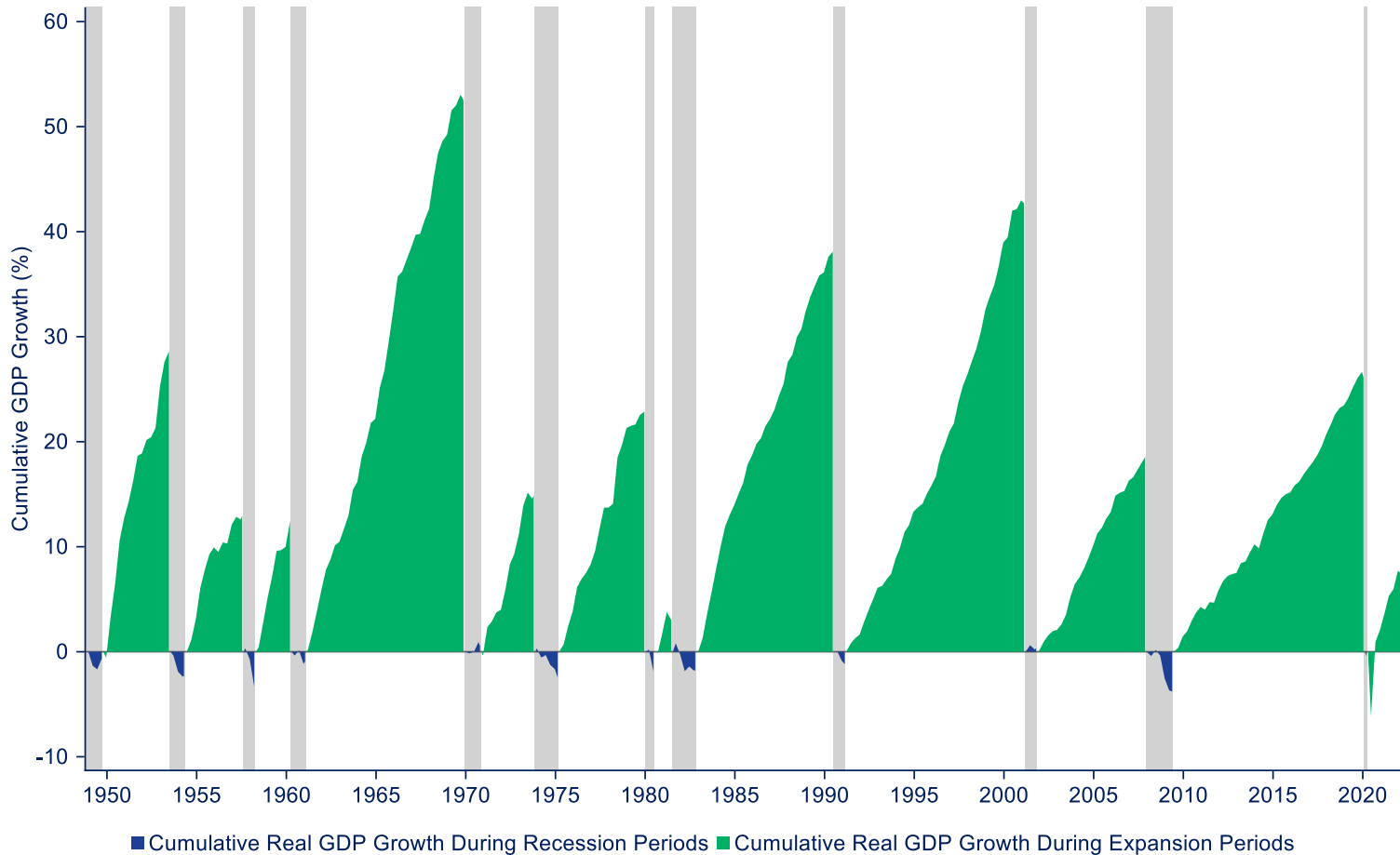
Source: Macrobond, Bloomberg, as of 5/18/2022

# Real versus nominal growth



Source: Macrobond, BLS, as of 5/18/2022

# The big question: Is it 1982? Or is it 1994?



Source: Macrobond, NBER, BEA, as of 3/31/2022

# Questions?

Thank you

# Definitions

**Fed Funds futures implied number of rate hikes** represents the estimated number of moves priced into the current forward-curve structure for the United States using the futures model. **The Federal Funds Rate (Fed funds)** is the short-term interest rate targeted by the Federal Reserve's Federal Open Market Committee (FOMC) as part of its monetary policy.

**The Consumer Price Index** is a measure of prices paid by consumers for a basket of consumer goods and services. The yearly (or monthly) growth rates represent the inflation rate.

**The New York Federal Reserve Survey of Consumer Expectations** is a nationally representative, Internet-based survey of a rotating panel of approximately 1,300 household heads. The inflation expectations measure tracks the median one-year and three-year ahead expected inflation rates.

**The Breakeven 10-Year inflation rate** is calculated by subtracting the real yield of the inflation-linked maturity curve from the yield of the closest nominal Treasury maturity. The result is the implied inflation rate for the term of the stated maturity.

**The 5-Year, 5-Year Forward Inflation Expectation Rate** measures expected inflation (on average) over the five-year period that begins five years from today.

**M2** is a measure of the money supply that includes cash, checking deposits, and easily-convertible near money.

**The Housing Affordability Index** – when the index measures 100, a family earning the median income has exactly the amount needed to purchase a median-price resale home using conventional financing. An increase in the home affordability index means that a family is more likely to be able to afford the median priced house.

**The S&P CoreLogic Case-Shiller U.S. National Home Price Index** tracks the value of a single-family housing within the United States. The index is a composite of single-family home price indices for the nine U.S. Census divisions.

**Owners Equivalent Rent of Primary Residence** is the amount of rent that would have to be paid in order to substitute a currently owned house as a rental property. Within the Consumer Price Index (CPI), this measures the change in the shelter cost consumers receive from their primary residences.

**West Texas Intermediate (WTI) crude** is a light crude oil that serves as one of the main global oil benchmarks.

**Average hourly earnings** tracks total hourly remuneration (in cash or in kind) paid to employees in return for work done (or paid leave).

**The employment cost index** measures changes in employee compensation costs (or labor costs). These costs include both direct costs (such as wages, bonuses or in-kind benefits) as well as indirect costs (such as social security contributions, training costs, medical benefits, taxes, etc.).

**The fertility rate** represents the number of children that would be born to a woman if she were to live to the end of her childbearing years and bear children in accordance with current age-specific fertility rates.

**The labor force participation rate** is a measure of the economy's active workforce. It is the sum of all workers who are employed or actively seeking employment divided by the total noninstitutionalized, civilian working-age population.

**Personal consumption expenditure deflators** track overall price changes for goods and services purchased by consumers.

**Labor productivity (output per hour)** tracks the total output that can be produced with a given input of labor. Generally, it is measured by dividing total real gross domestic product by either total employment or total hours worked.

**Household debt service and principal payments as a percent of income** is calculated using household debt service payments as the numerator and gross disposable income over the same period as the denominator. It measures the capacity of households to cover their debt payments (interest and principal).

**Money market funds** are mutual funds that invest in highly liquid, near-term instruments including cash and cash equivalents.

**GDP (Gross Domestic Product)** is the total market value of all final goods and services produced in a country in a given year, equal to total consumer, investment and government spending, plus the value of exports, minus the value of imports. The **Bloomberg GDP Economic Forecasts** provides contributor forecasts from economists.

# Disclosures

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