



Presenter:

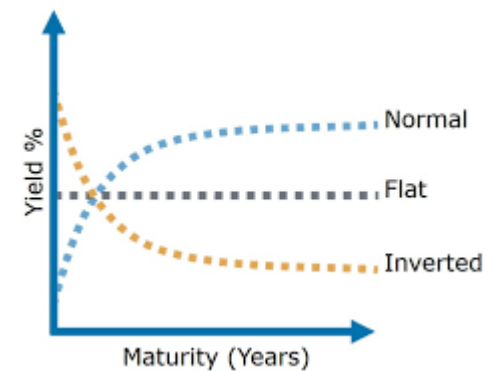
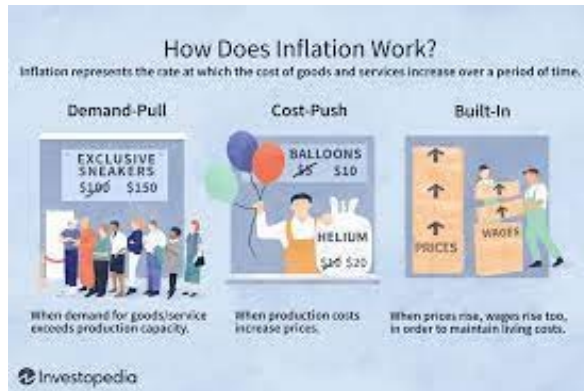
David Jang, CTP  
Managing Partner  
[david@deepblue-inv.com](mailto:david@deepblue-inv.com)  
407-618-4269

# **THE IMPACT OF HIGHER INTEREST RATES ON THE ECONOMY & BUDGET**

FGFOA Webinar Series  
January 12, 2023

# Objectives

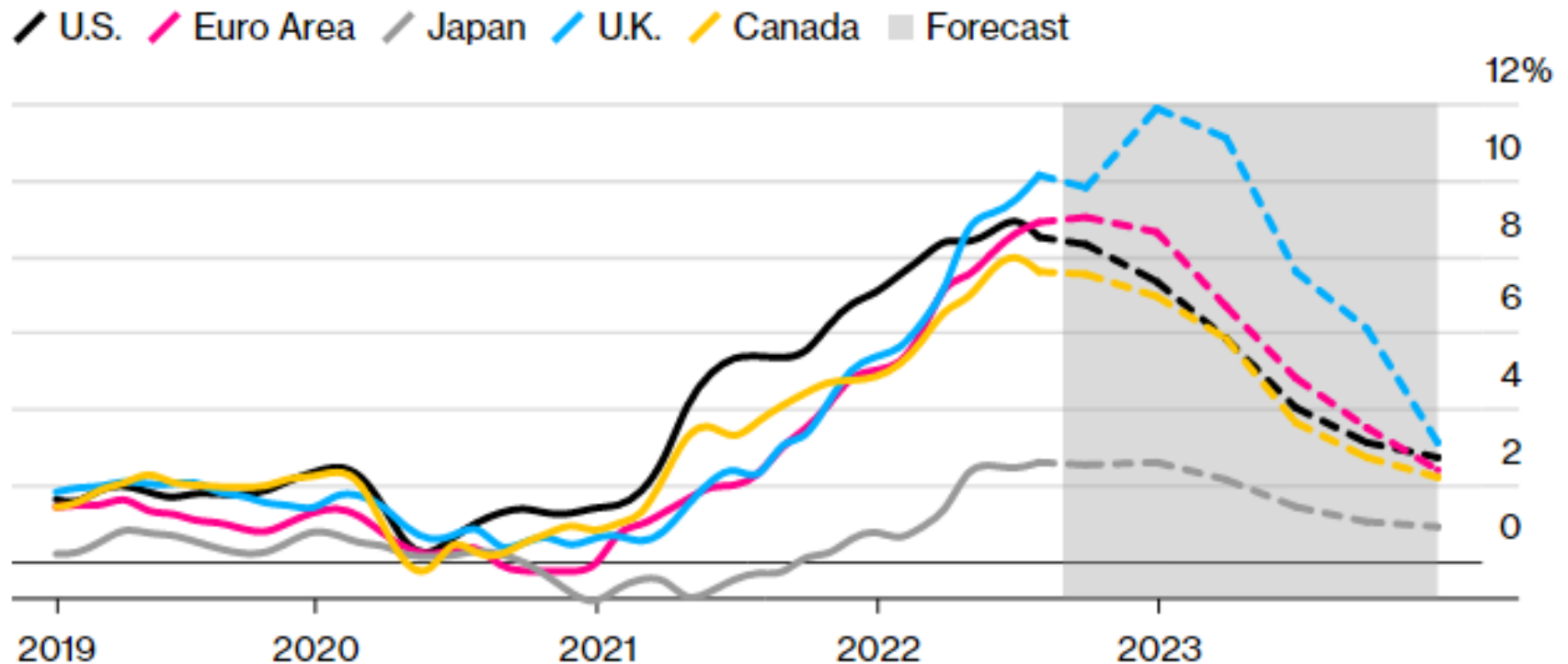
- Learn the components of inflation
- Understand why interest rates move up and down
- Assess how your revenues and expenses may be affected by current economic factors



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# Global Inflation

## Actual and Forecast Inflation Rates



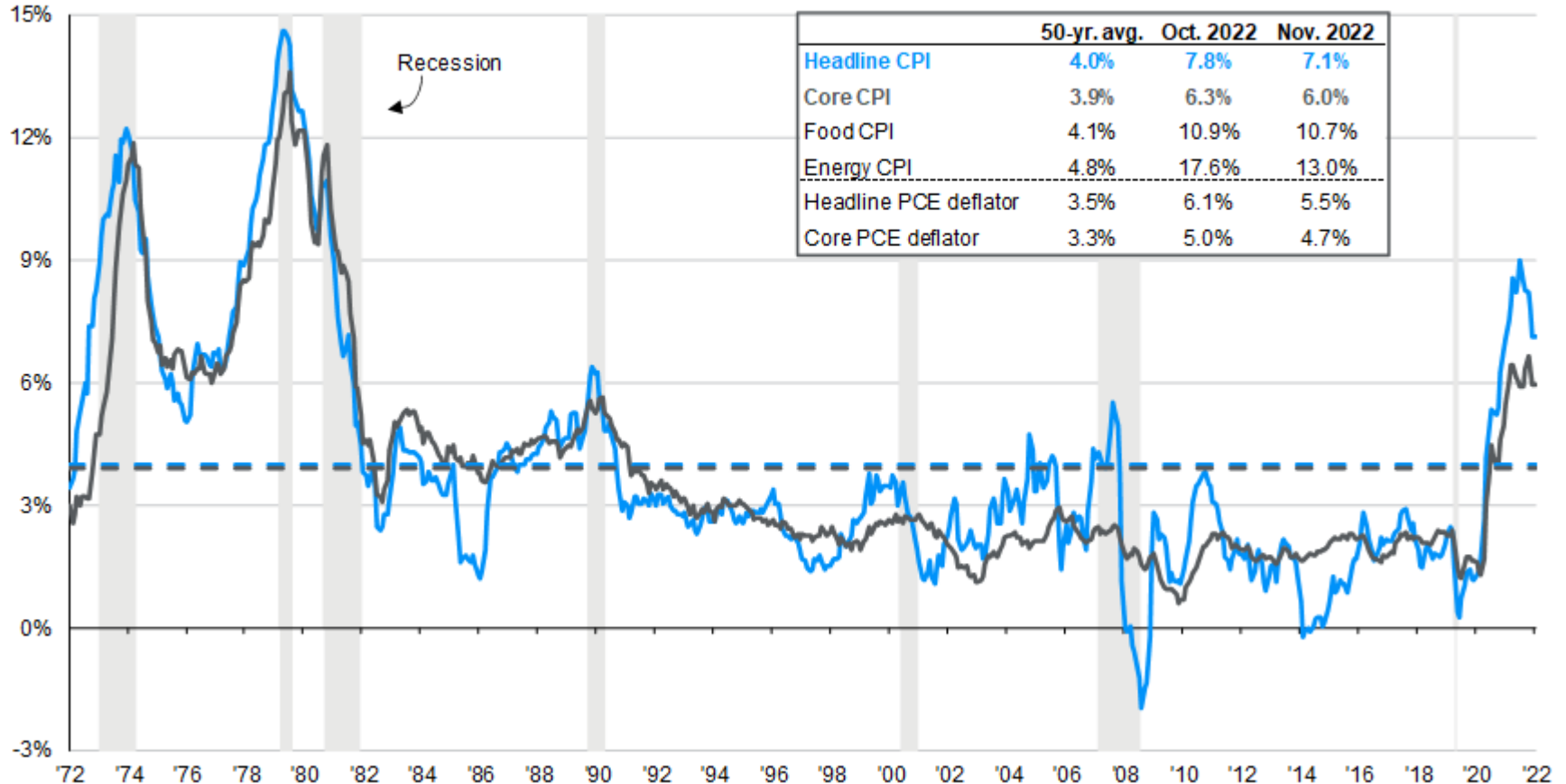
Source: Official statistics agencies, Bloomberg economist surveys

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# Inflation

## CPI and core CPI

% change vs. prior year, seasonally adjusted



Source: BLS, FactSet, J.P. Morgan Asset Management.

CPI used is CPI-U and values shown are % change vs. one year ago. Core CPI is defined as CPI excluding food and energy prices. The Personal Consumption Expenditure (PCE) deflator employs an evolving chain-weighted basket of consumer expenditures instead of the fixed-weight basket used in CPI calculations.

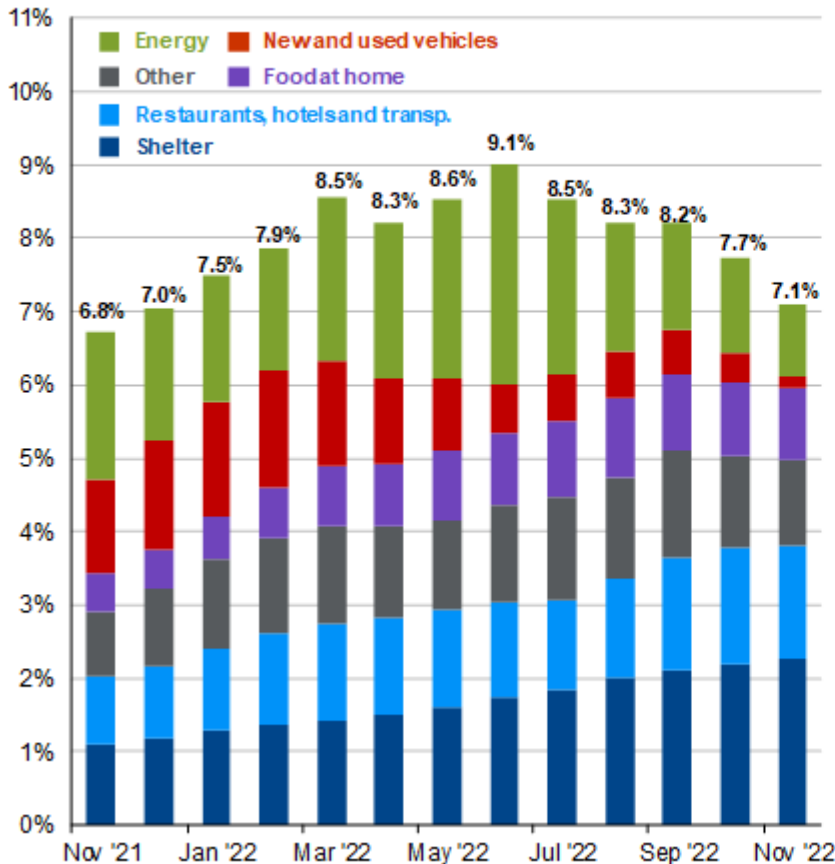
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# Inflation Components

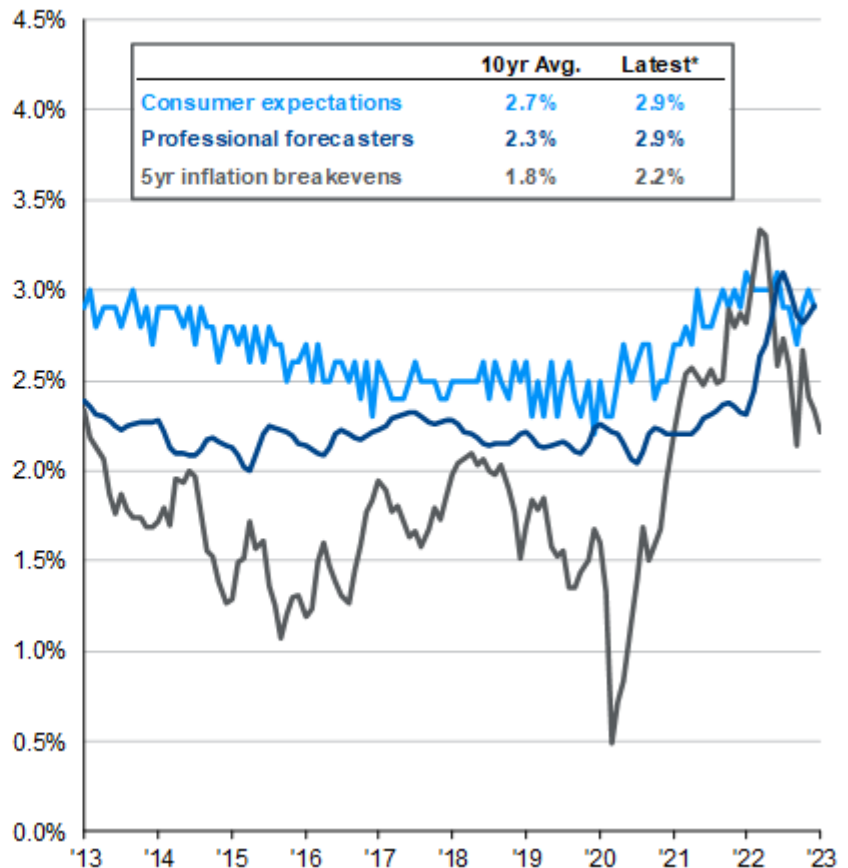
## Contributors to headline inflation

Contribution to y/y % change in CPI, not seasonally adjusted



## Inflation expectations, next 5 years

% change vs. prior year, non-seasonally adjusted



Source: Bureau of Labor Statistics, FactSet, Federal Reserve Bank of Philadelphia, University of Michigan, J.P. Morgan Asset Management. Contributions mirror the BLS methodology on Table 7 of the CPI report. Values may not sum to headline CPI figures due to rounding and underlying calculations. "Shelter" includes owner's equivalent rent and rent of primary residence. "Other" primarily reflects household furnishings, apparel, education and communication services, medical care services and other personal services. \*Reflects the latest daily 5yr/5yr breakevens, preliminary or final Consumer Sentiment survey, and the quarterly Survey of Professional Forecasters interpolated to a monthly series. The Survey of Professional Forecasters reflects the median estimate by professional forecasters of average CPI inflation over the next 5 years. The series has been adjusted by J.P. Morgan Asset Management to exclude realized inflation readings within the forecast window.

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# Question #1

The November 2021 year over year inflation rate is \_\_\_\_\_ as/than November 2022

- A. Higher
- B. Lower
- C. Same

# Wage Inflation

Wages and prices, annualized rate of three-month change



Notes: Wages measured by employment cost index, wages and salaries of civilian workers; services prices pulled from personal consumption expenditures price index

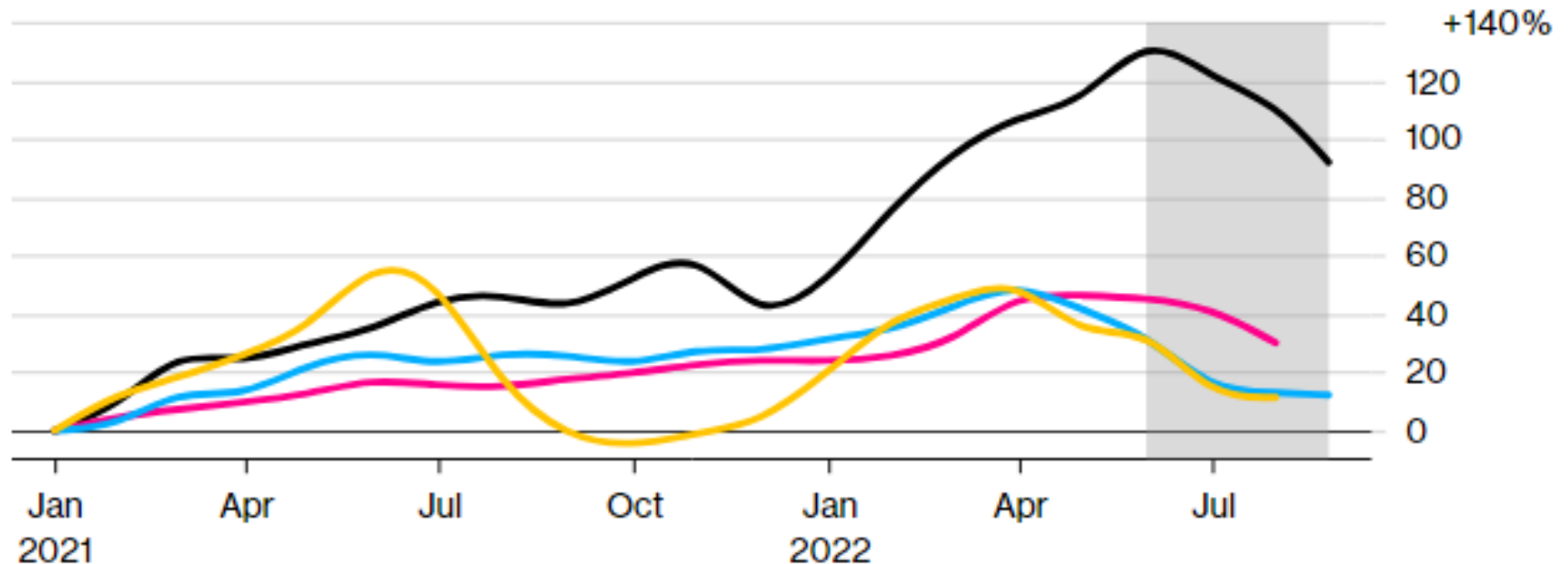
Sources: Federal Reserve Bank of St. Louis (Wages); U.S. Bureau of Economic Analysis, WSJ calculations (Services)

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# Commodity Prices are Falling

Change in prices since end of 2020

● Brent crude ● Global food ● Metals ● US Lumber



Source: Bloomberg, UNFAO, London Metal Exchange, Bureau of Labor Statistics

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# Oil Markets

## Change in production and consumption of liquid fuels

Production, consumption and inventories, millions of barrels per day

Production	2019	2020	2021	2022*	2023*	Growth since '19
U.S.	19.5	18.6	19.0	20.3	21.1	8.2%
OPEC	34.6	30.7	31.7	34.1	34.5	-0.2%
Russia	11.5	10.5	10.8	10.9	9.5	-17.3%
Global	100.3	93.9	95.7	100.0	101.1	0.8%
Consumption						
U.S.	20.5	18.2	19.9	20.4	20.5	-0.1%
China	14.0	14.4	15.3	15.2	15.8	12.5%
Global	100.8	92.0	97.6	99.8	100.8	0.0%
Inventory Change						
	-0.5	1.9	-1.9	0.2	0.2	

## U.S. crude oil inventories and rig count\*\*

Million barrels, number of active rigs



## Price of oil

WTI crude, nominal prices, USD/barrel



Source: J.P. Morgan Asset Management; (Top and bottom left) EIA; (Right) FactSet; (Bottom left) Baker Hughes.

\*Forecasts are from the December 2022 EIA Short-Term Energy Outlook and start in 2022. \*\*U.S. crude oil inventories include the Strategic Petroleum Reserve (SPR). Liquid fuels include crude oil, natural gas, biodiesel and fuel ethanol. Active rig count includes both natural gas and oil rigs. WTI crude prices are continuous contract NYM prices in USD.

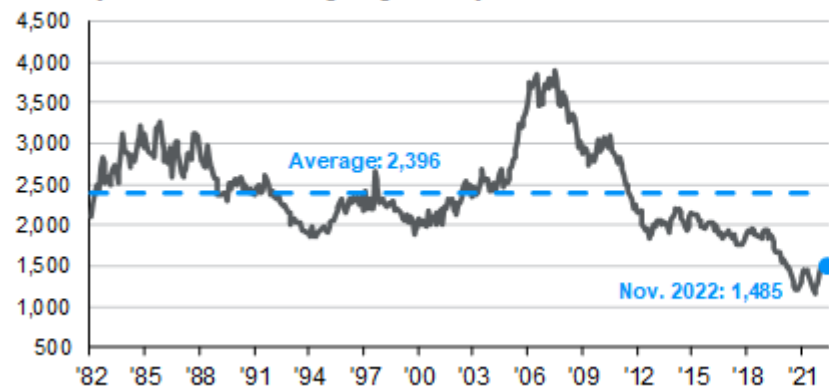
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# Residential Real Estate

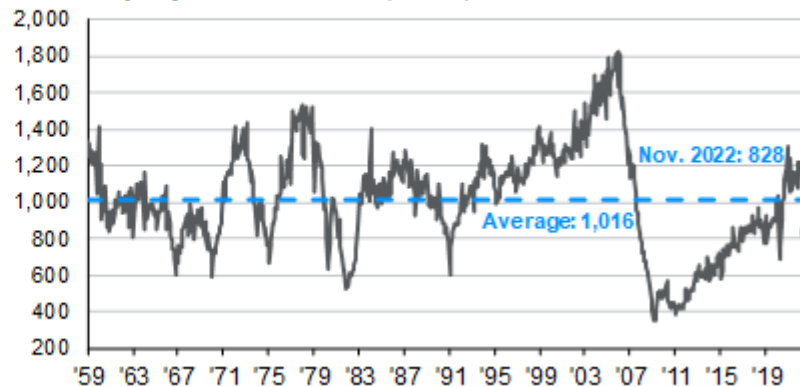
## Housing inventories

Inventory of new and existing single family homes for sale, thous, SA\*



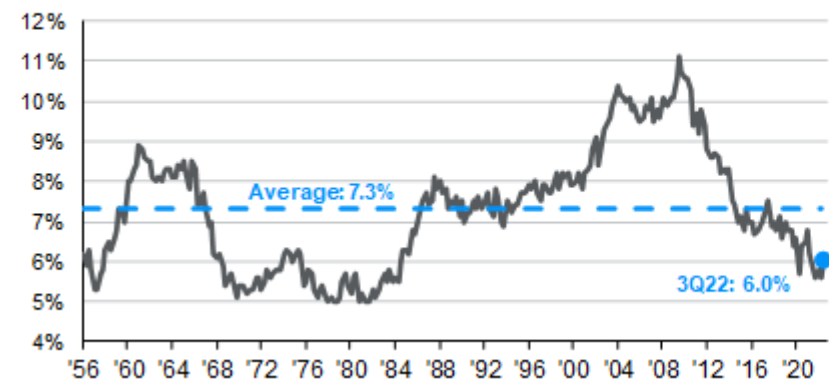
## Single-family housing starts

Seasonally adjusted annual rate (SAAR), thous houses



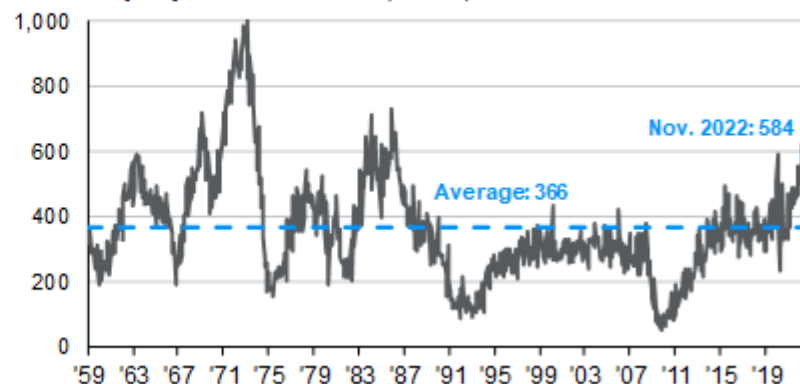
## Rental vacancy rate

Percent



## Multi-family housing starts

Seasonally adjusted annual rate (SAAR), thous houses



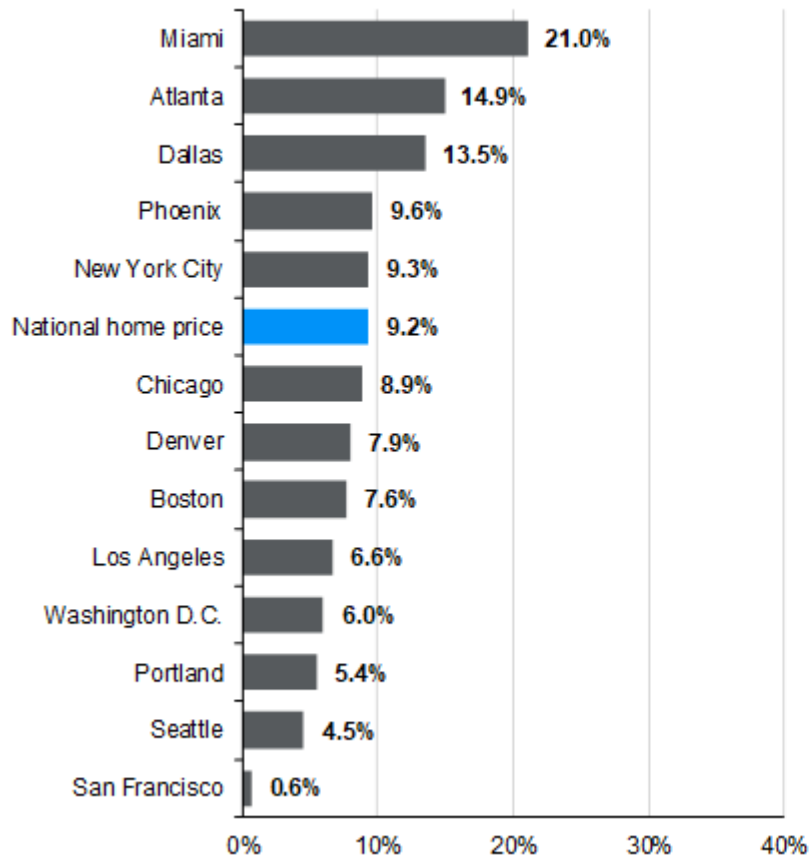
Source: U.S. Census Bureau, U.S. National Association of Realtors, J.P. Morgan Asset Management. \*Inventory of new and existing single family homes for sale is seasonally adjusted by J.P. Morgan Asset Management.  
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# Residential Real Estate

## U.S. home price growth by city

S&P Case-Shiller Home Price Index, Oct. 2022, y/y % change



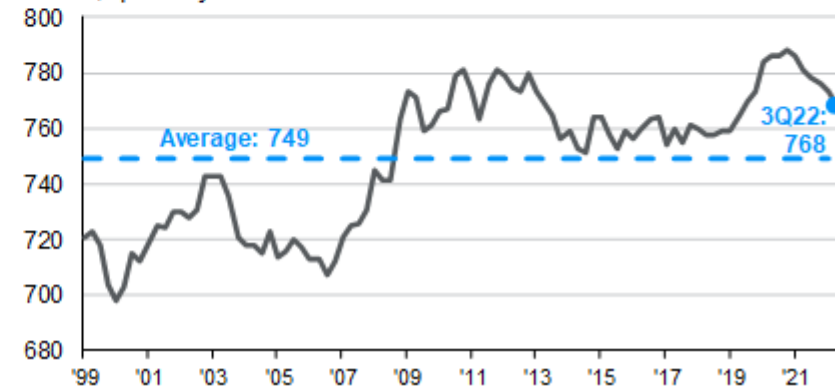
## Housing affordability index\*

Index



## Credit score at mortgage origination

Median, quarterly



Source: J.P. Morgan Asset Management. (Left) FactSet, Robert Shiller, Standard & Poor's; (Top right) U.S. National Association of Realtors; (Bottom right) New York Fed Consumer Credit Panel/Equifax. \*Based on the National Association of Realtors methodology, an index value above 100 signifies that a family earning the median income has more than enough income to qualify for a mortgage loan on a median-priced home. The calculation assumes a down payment of 20% of the home price and it assumes a qualifying ratio of 25%.

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# Question #2

The October year over year national home price change is \_\_\_\_\_ than Miami, FL

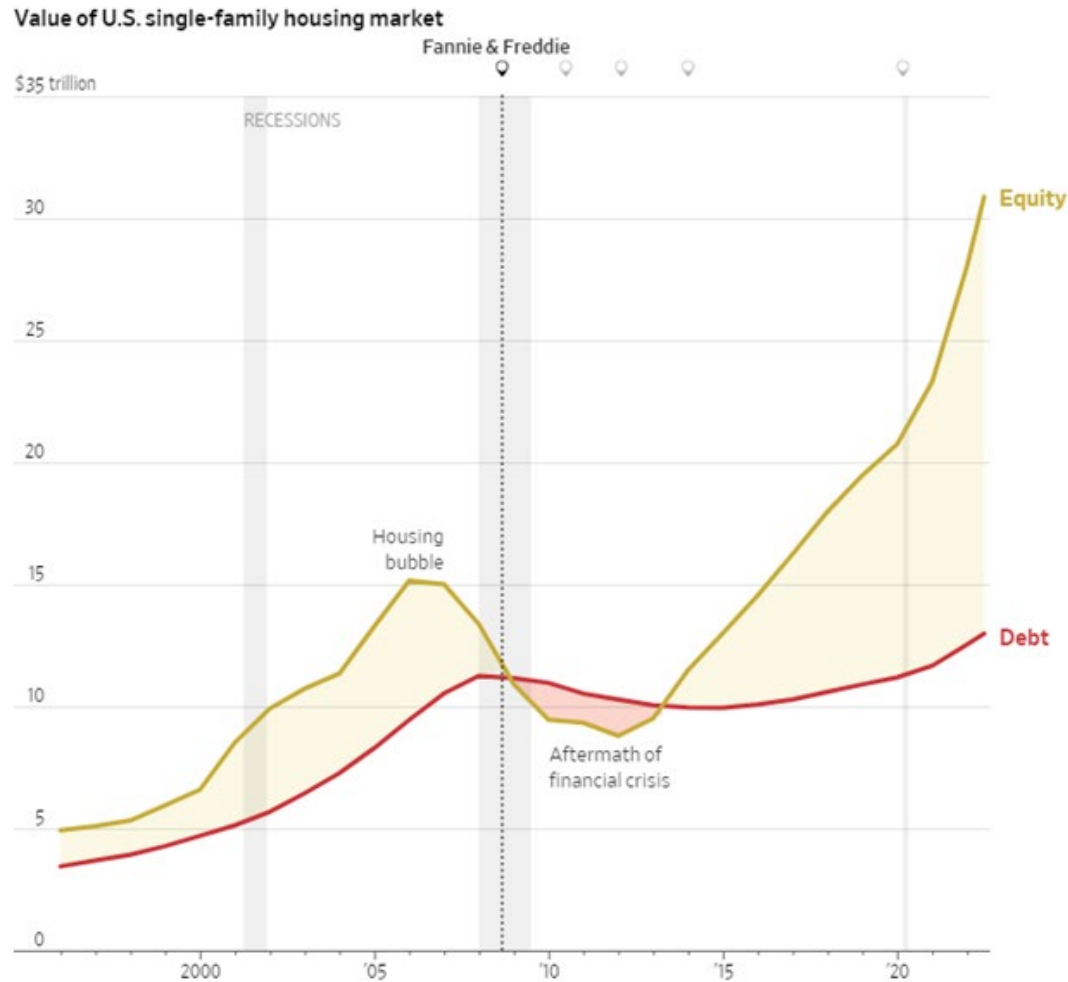
- A. Higher
- B. Lower
- C. Same

# Cost of Living by State

State	Annual Mean Wage (All Occupations)	Average Monthly Rent	Value of \$100	*Rental Affordability
Hawaii	\$59,760	\$1,880.08	\$80.70	19.63
California	\$68,510	\$1,777.67	\$83.60	16.19
New York	\$70,460	\$1,431.58	\$83.70	12.68
New Jersey	\$67,120	\$1,541.08	\$84.00	14.33
Massachusetts	\$72,940	\$1,553.75	\$89.60	13.29
Washington	\$68,740	\$1,487.58	\$91.60	13.50
Maryland	\$65,900	\$1,505.33	\$92.30	14.25
New Hampshire	\$59,270	\$1,213.50	\$93.50	12.78
Alaska	\$63,480	\$1,288.42	\$94.90	12.66
Connecticut	\$66,130	\$1,315.42	\$95.00	12.41
Vermont	\$55,450	<i>Not provided</i>	\$96.90	<i>N/A</i>
Oregon	\$59,070	\$1,226.58	\$97.80	12.96
Colorado	\$62,900	\$1,404.33	\$98.10	13.93
Rhode Island	\$62,120	\$1,178.08	\$98.70	11.83
Virginia	\$62,330	\$1,351.33	\$98.70	13.53
<b>Florida</b>	<b>\$51,950</b>	<b>\$1,329.92</b>	<b>\$99.00</b>	<b>15.97</b>
Alabama	\$48,110	\$914.08	\$114.20	11.86
Arkansas	\$46,500	\$778.92	\$115.30	10.45
Mississippi	\$42,700	\$868.42	\$115.60	12.69
Source: Patriot Software, Deep Blue Investment Advisors				
* Number of weeks work to pay annual rent cost				

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# Value of Single-Family Housing Market



Note: Single-family data includes one- to four-family homes with mortgages. Home equity is calculated from value of household and nonfinancial business sector.

Source: Urban Institute

Peter Santilli/THE WALL STREET JOURNAL

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# Dollar Drivers

## The U.S. dollar

U.S. Dollar Index



## The U.S. trade balance

Current account balance, % of GDP



## Developed markets interest rate differentials

Difference between U.S. and international 10-year yields\*



Source: J.P. Morgan Asset Management; (Left) FactSet, ICE; (Top right) Bureau of Economic Analysis, FactSet; (Bottom right) Tullett Prebon. Currencies in the DXY Index are: British pound, Canadian dollar, euro, Japanese yen, Swedish krona and Swiss franc. \*Interest rate differential is the difference between the 10-year U.S. Treasury yield and a basket of the 10-year yields of each major trading partner (Australia, Canada, Europe, Japan, Sweden, Switzerland and UK). Weights in the basket are calculated using the 10-year average of total government bonds outstanding in each region. Europe is defined as the 19 countries in the euro area. *Guide to the Markets – U.S.* Data are as of January 5, 2022.

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# Question #3

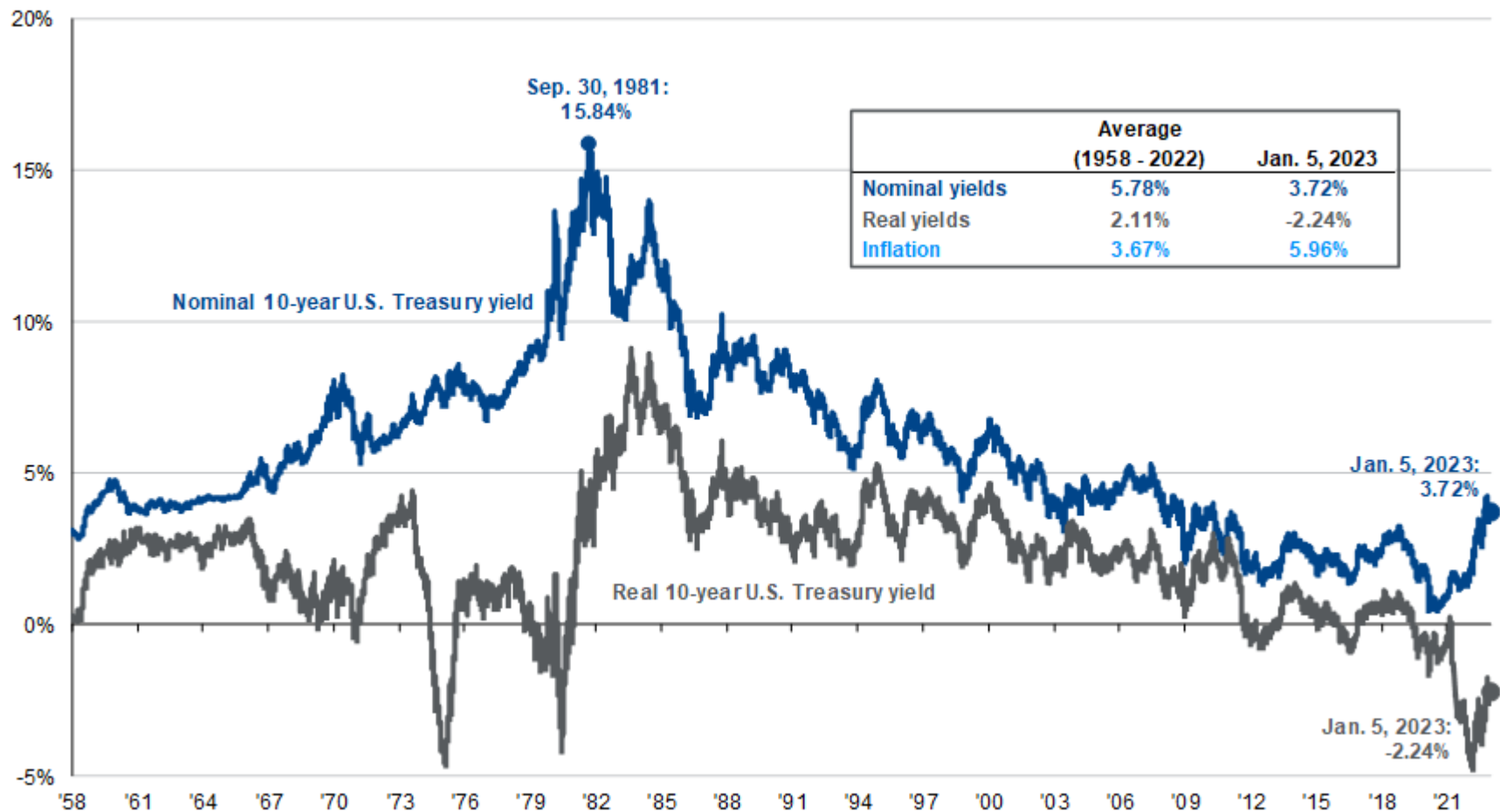
The USD index on January 5, 2022 is  
\_\_\_\_\_ as/than June 2007

- A. Higher
- B. Lower
- C. Same



# Interest Rates and Inflation

## Nominal and real U.S. 10-year Treasury yields



Source: BLS, FactSet, Federal Reserve, J.P. Morgan Asset Management.

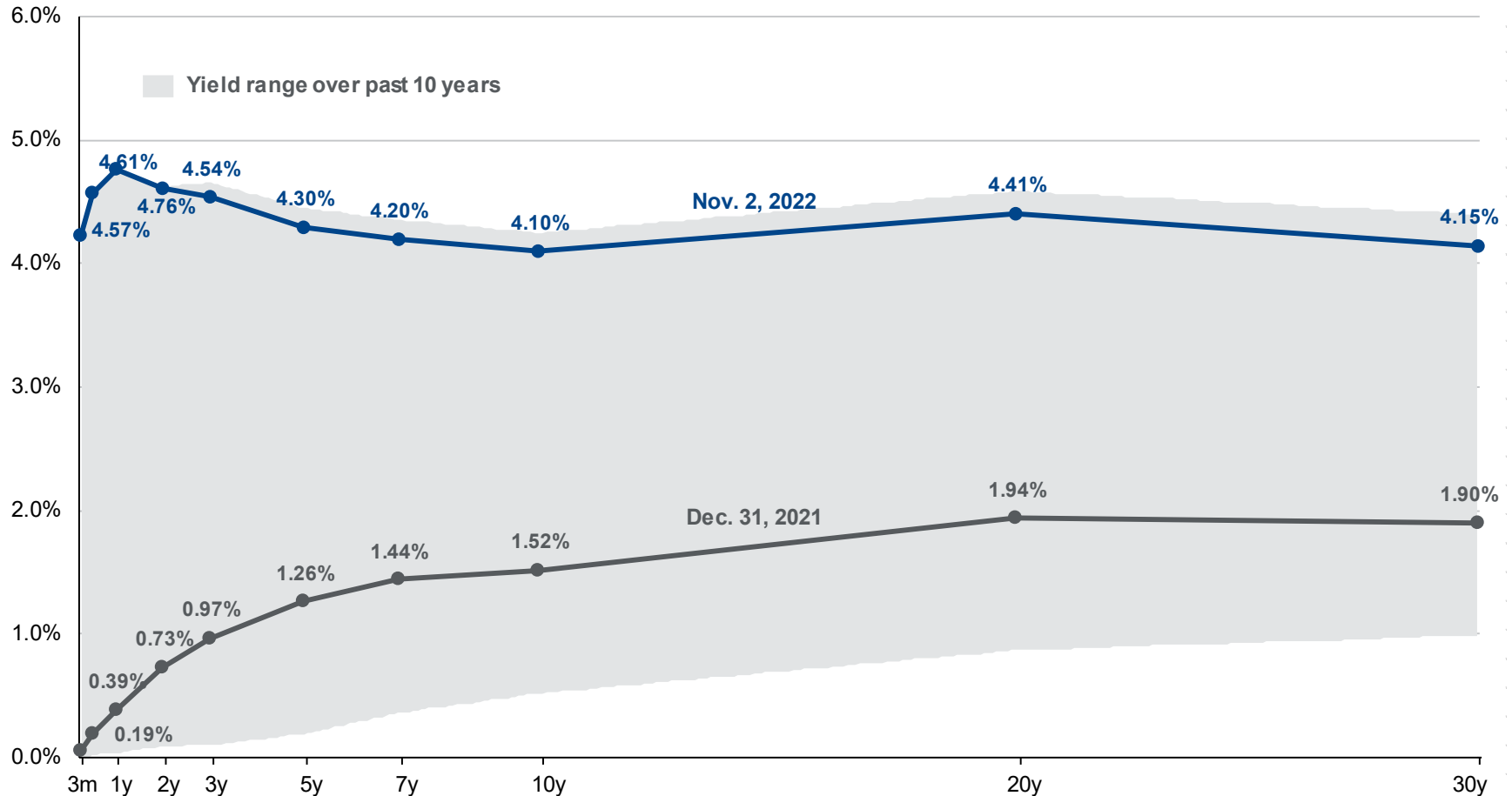
Real 10-year Treasury yields are calculated as the daily Treasury yield less year-over-year core CPI inflation for that month. For the current month, we use the prior month's core CPI figures until the latest data is available.

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# Yield Curve (11/2/22)

## U.S. Treasury yield curve

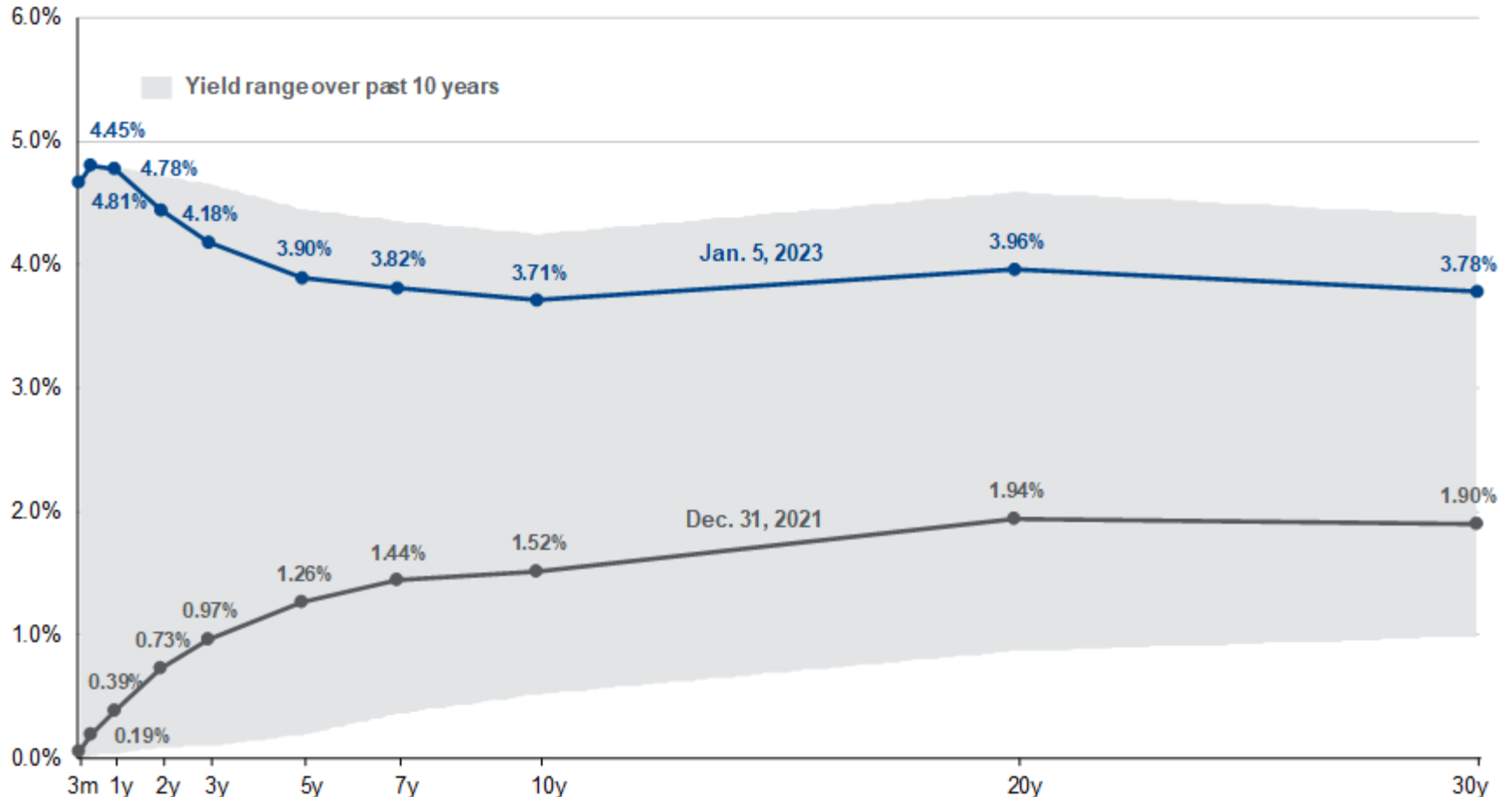


Source: FactSet, Federal Reserve, J.P. Morgan Asset Management.  
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# Yield Curve (1/5/23)

## U.S. Treasury yield curve



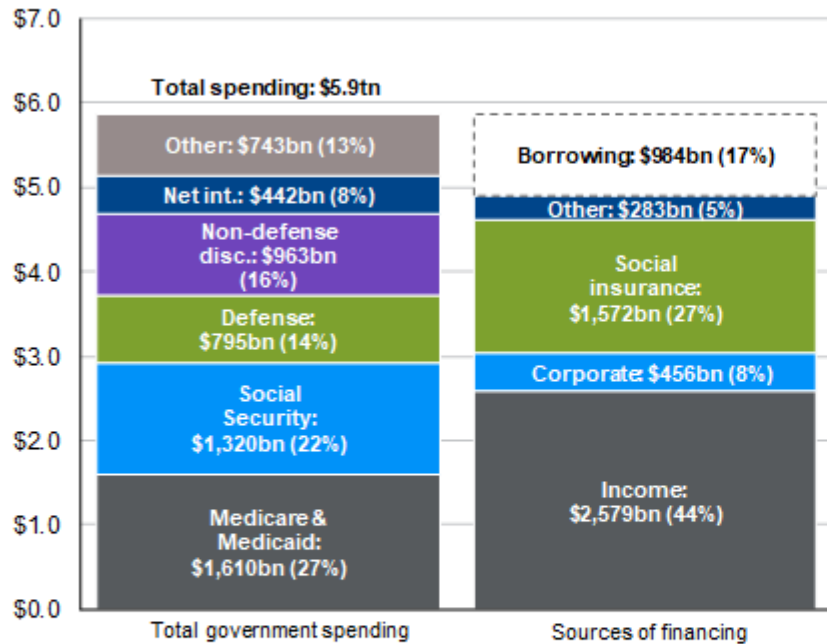
Source: FactSet, Federal Reserve, J.P. Morgan Asset Management.  
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# Federal Finances

## The 2023 federal budget

CBO Baseline forecast, USD trillions

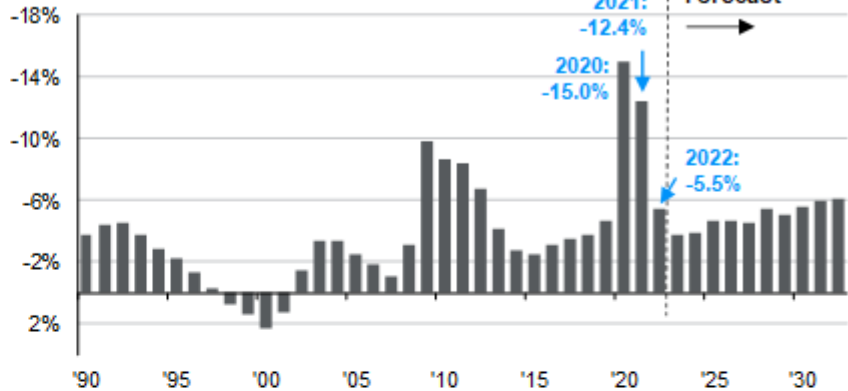


## CBO's Baseline economic assumptions

	2023	'24-'25	'26-'27	'28-'32
Real GDP growth	3.0%	1.6%	1.5%	1.7%
10-year Treasury	2.8%	3.1%	3.5%	3.8%
Headline inflation (CPI)	3.6%	2.4%	2.3%	2.4%
Unemployment	3.6%	3.7%	4.1%	4.5%

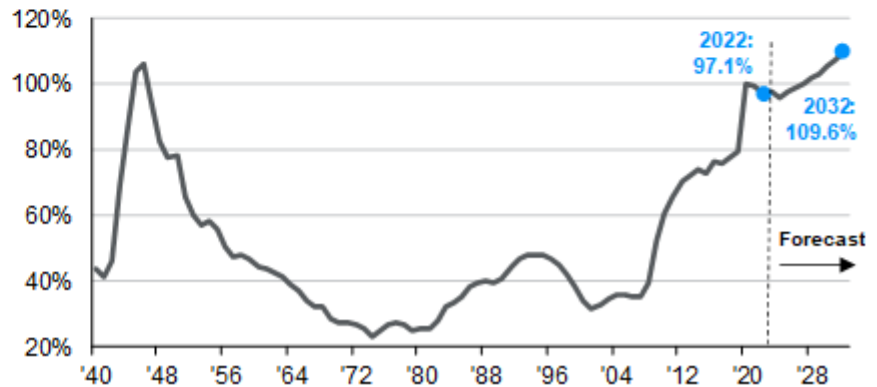
## Federal budget surplus/deficit

% of GDP, 1990 – 2032, CBO Baseline Forecast



## Federal net debt (accumulated deficits)

% of GDP, 1940 – 2032, CBO Baseline Forecast, end of fiscal year



Source: CBO, J.P. Morgan Asset Management; (Top and bottom right) BEA, Treasury Department.

Estimates are based on the Congressional Budget Office (CBO) May 2022 Update to the Budget and Economic Outlook. Data for fiscal year 2022 is from the CBO's Monthly Budget Review. Other spending includes, but is not limited to, health insurance subsidies, income security and federal civilian and military retirement. Note: Years shown are fiscal years. Forecasts are not a reliable indicator of future performance. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated.

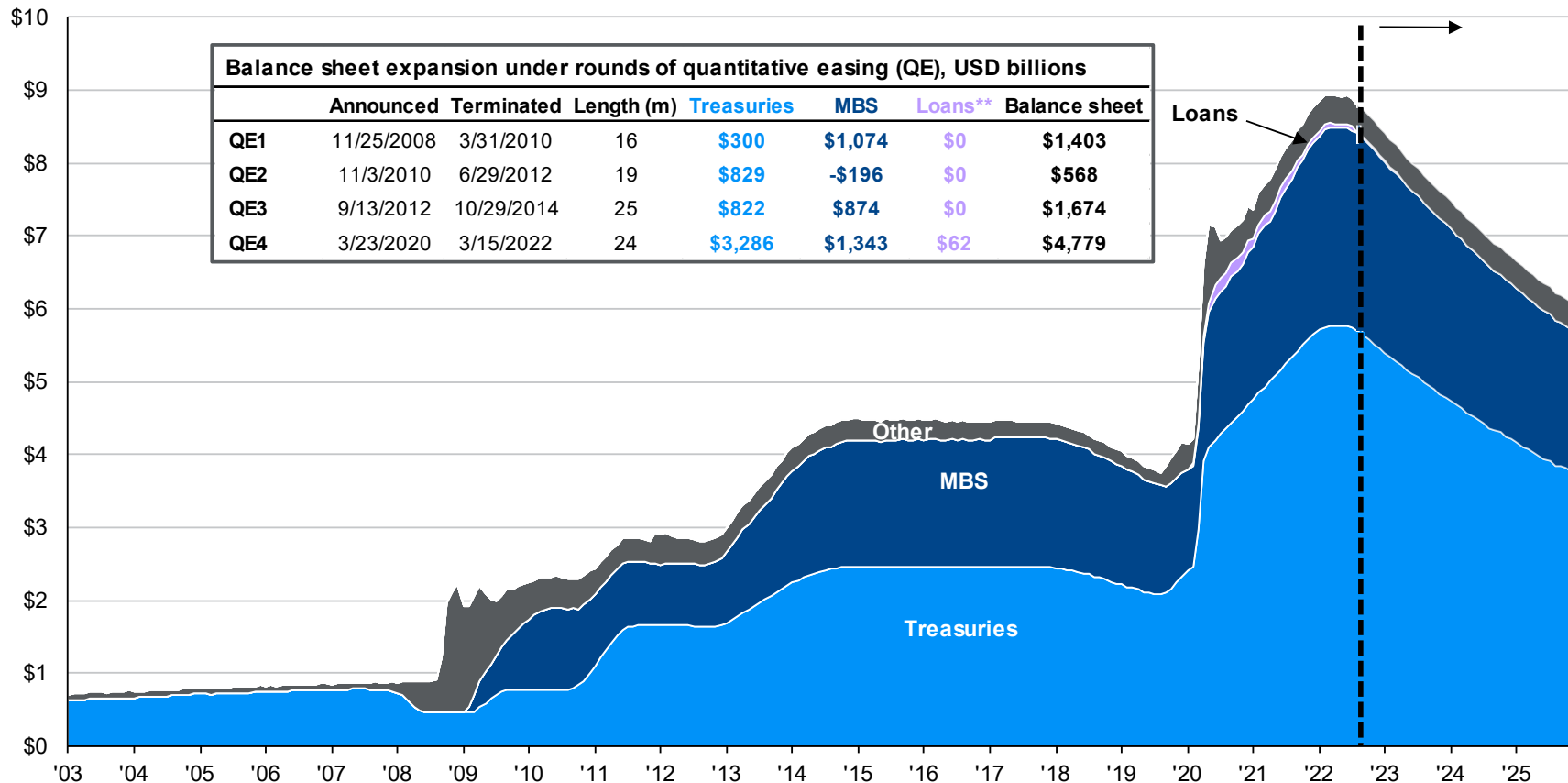
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# Quantitative Tightening

## The Federal Reserve balance sheet

USD trillions



Source: FactSet, Federal Reserve, J.P. Morgan Investment Bank, J.P. Morgan Asset Management.

At its peak, the balance sheet contained \$5.8tn in Treasuries and \$2.7tn in MBS. \*Per the most recent Federal Reserve policy meeting, the forecast assumes the Federal Reserve began balance sheet runoff in June 2022. From June to August, the committee allowed up to \$30bn in U.S. Treasury securities and \$17.5bn in agency mortgage-backed securities to mature per month, with that pace doubling to \$60bn and \$35bn, respectively, in September. Any maturing amount in excess of these caps are reinvested. The forecast does not include the active selling of securities from the committee. \*\*Loans include liquidity and credit extended through corporate credit facilities established in March 2020. Other includes primary, secondary and seasonal loans, repurchase agreements, foreign currency reserves and maiden lane securities. Forecasts are not a reliable indicator of future performance. Forecasts, projections and other forward-looking statements are based upon current beliefs and expectations. They are for illustrative purposes only and serve as an indication of what may occur. Given the inherent uncertainties and risks associated with forecasts, projections or other forward-looking statements, actual events, results or performance may differ materially from those reflected or contemplated.

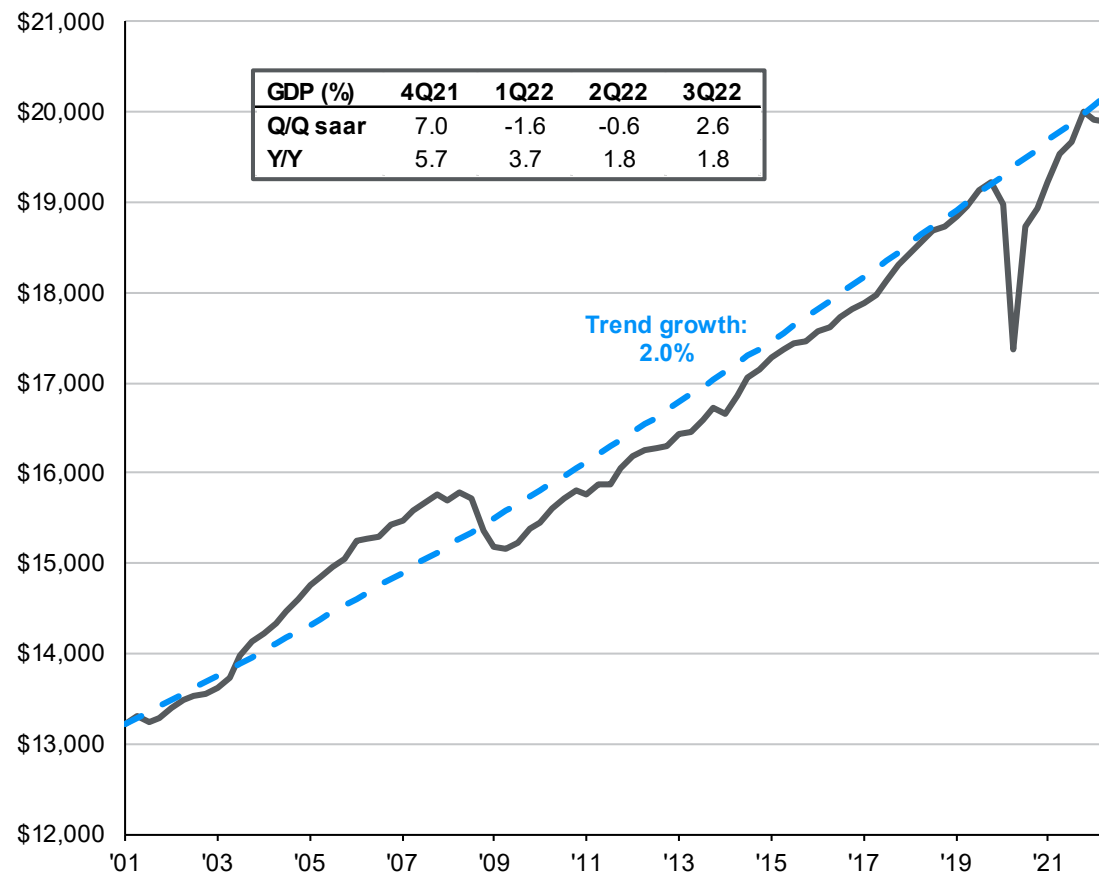
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# Economic Growth and the Composition of GDP

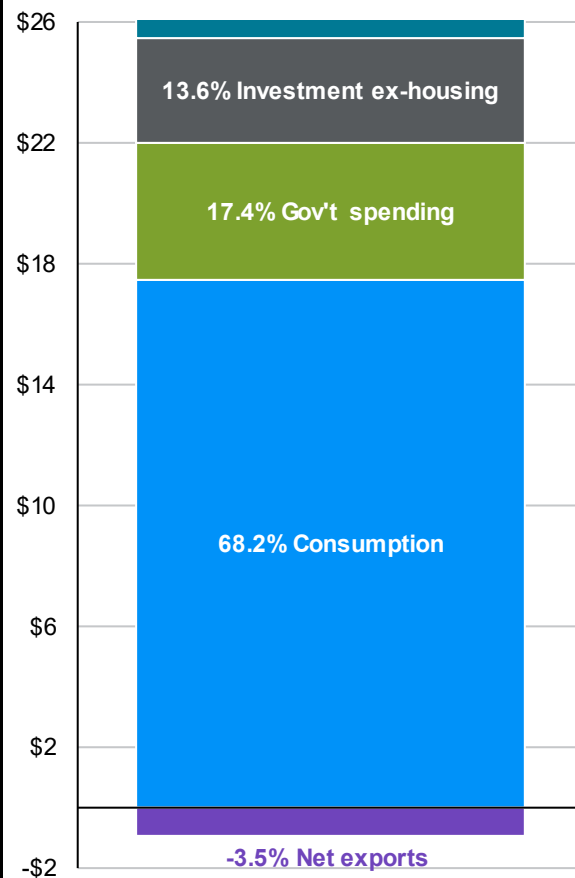
## Real GDP

Billions of chained (2012) dollars, seasonally adjusted at annual rates



## Components of GDP

3Q22 nominal GDP, USD trillions



Source: BEA, FactSet, J.P. Morgan Asset Management. Values may not sum to 100% due to rounding. Trend growth is measured as the average annual growth rate from business cycle peak 1Q01 to business cycle peak 4Q19.  
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# Question #4

The largest component of GDP is

- A. Investment ex-housing
- B. Government Spending
- C. Consumption
- D. Net Exports

# Labor Demand

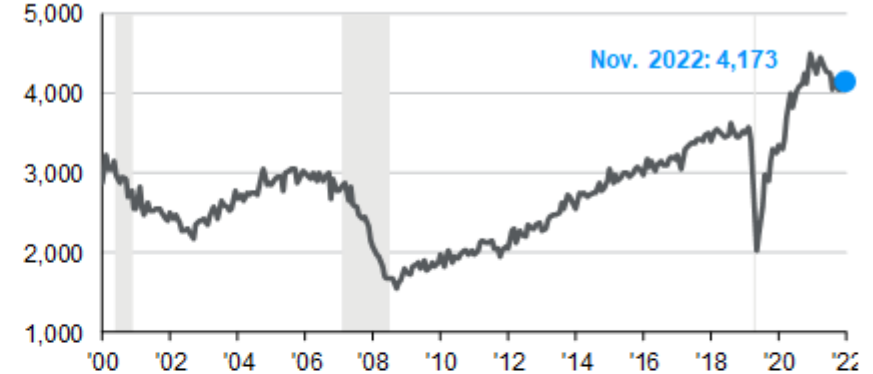
## Ratio of job openings to job seekers

Job openings\* lagged 1 month divided by unemployed persons, SA



## JOLTS quits

Total nonfarm quits, thousands, seasonally adjusted



## JOLTS layoffs

Total nonfarm layoffs, thousands, seasonally adjusted



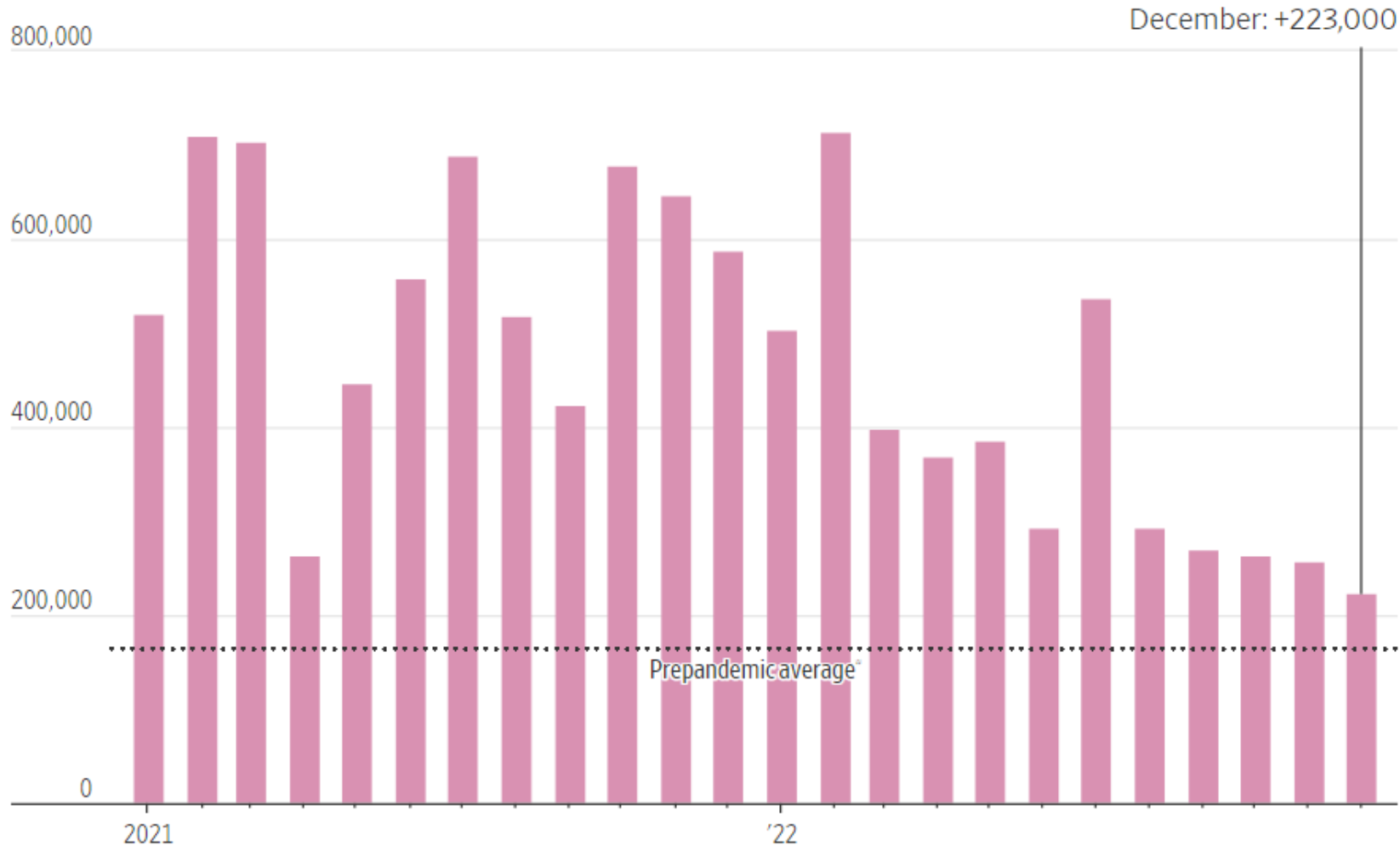
Source: U.S. Department of Labor, J.P. Morgan Asset Management. \*JOLTS job openings from February 1974 to November 2000 are J.P. Morgan Asset Management estimates.

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# Nonfarm Payrolls, monthly change



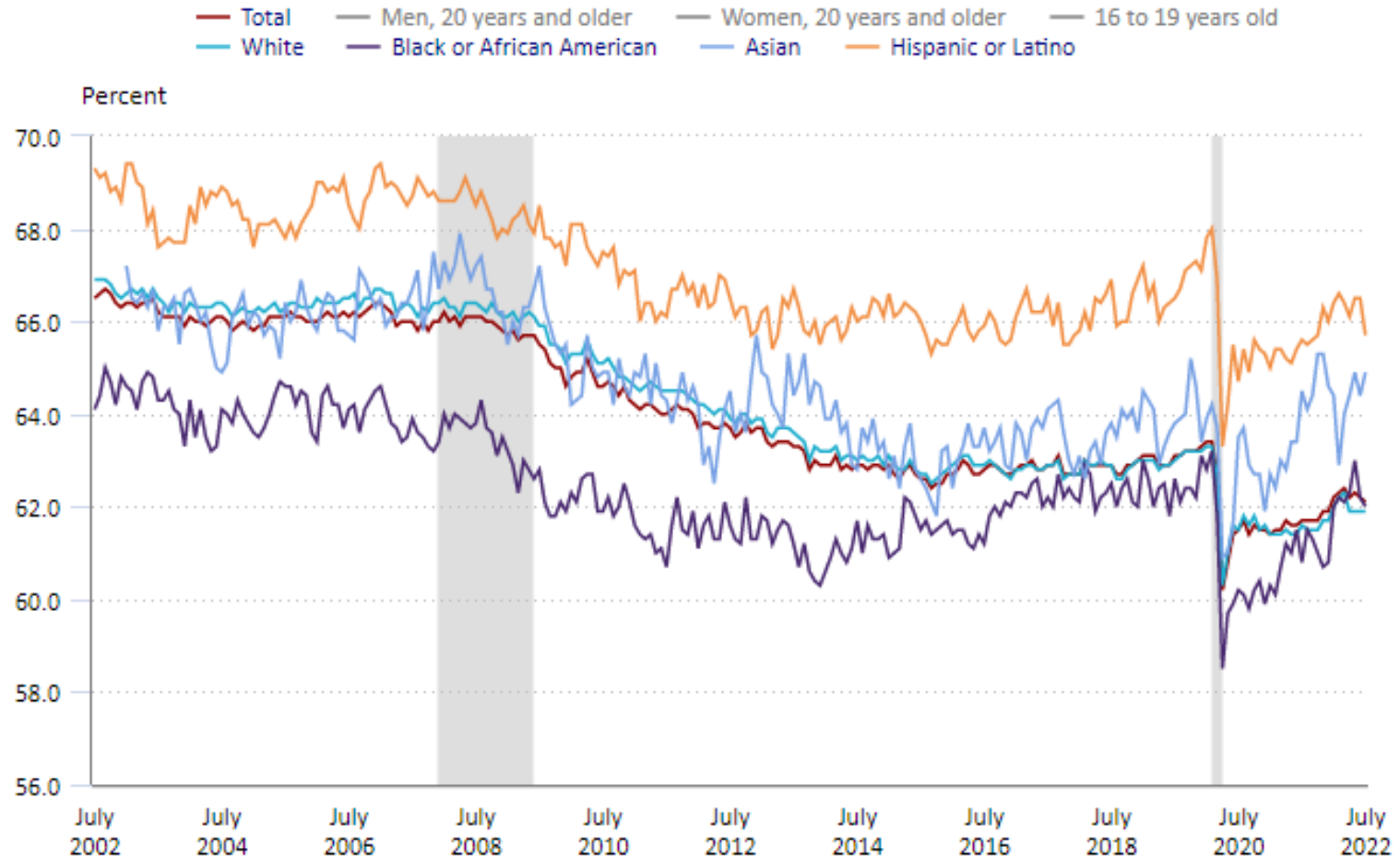
\*2019 average. Note: Seasonally adjusted.

Source: Labor Department

Wall Street Journal 1/6/23

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# Participation Rate by Race



Hover over chart to view data.

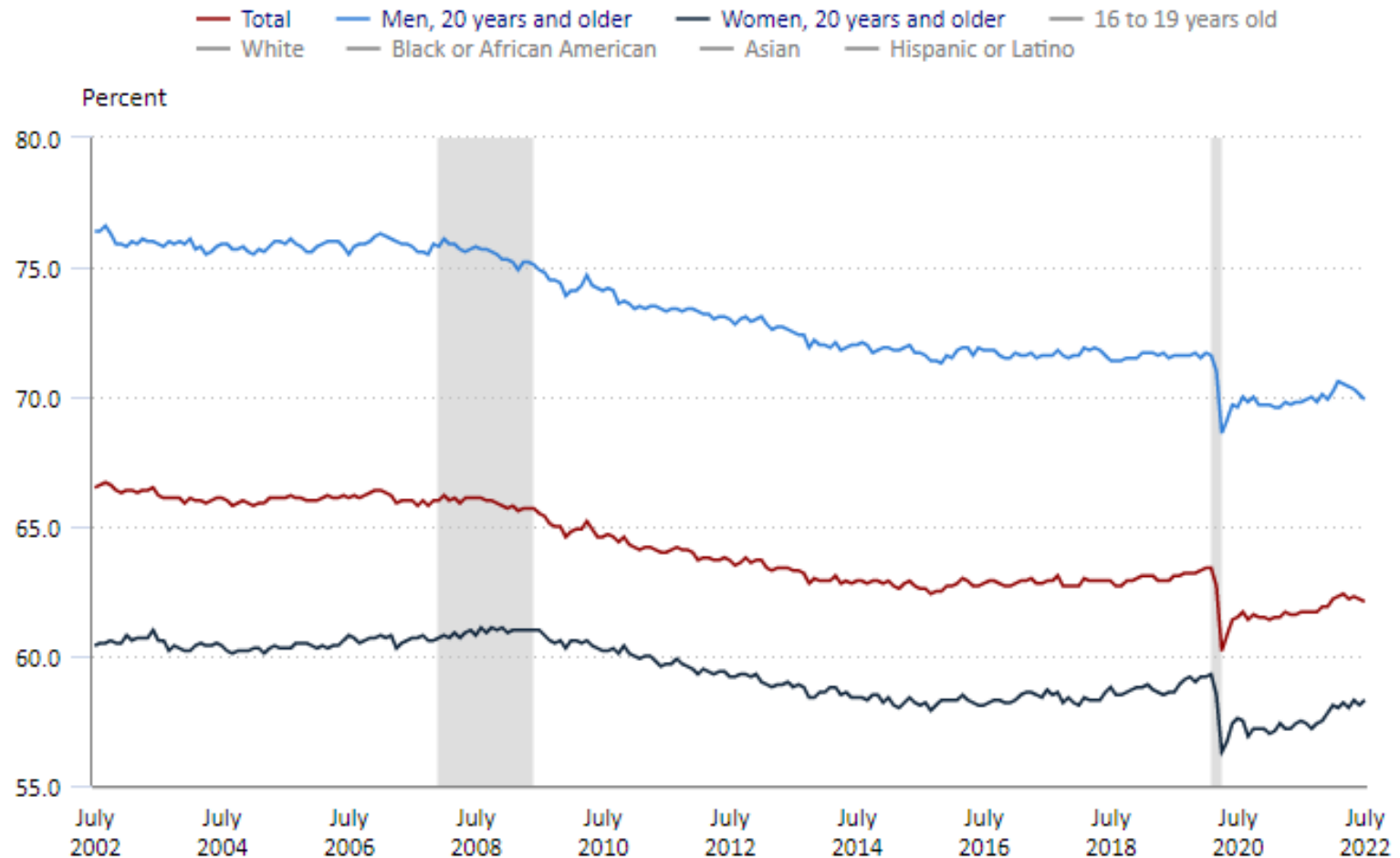
Note: Shaded area represents recession, as determined by the National Bureau of Economic Research.

Persons whose ethnicity is identified as Hispanic or Latino may be of any race.

Source: U.S. Bureau of Labor Statistics.

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# Participation Rate by Sex



Hover over chart to view data.

Note: Shaded area represents recession, as determined by the National Bureau of Economic Research.

Persons whose ethnicity is identified as Hispanic or Latino may be of any race.

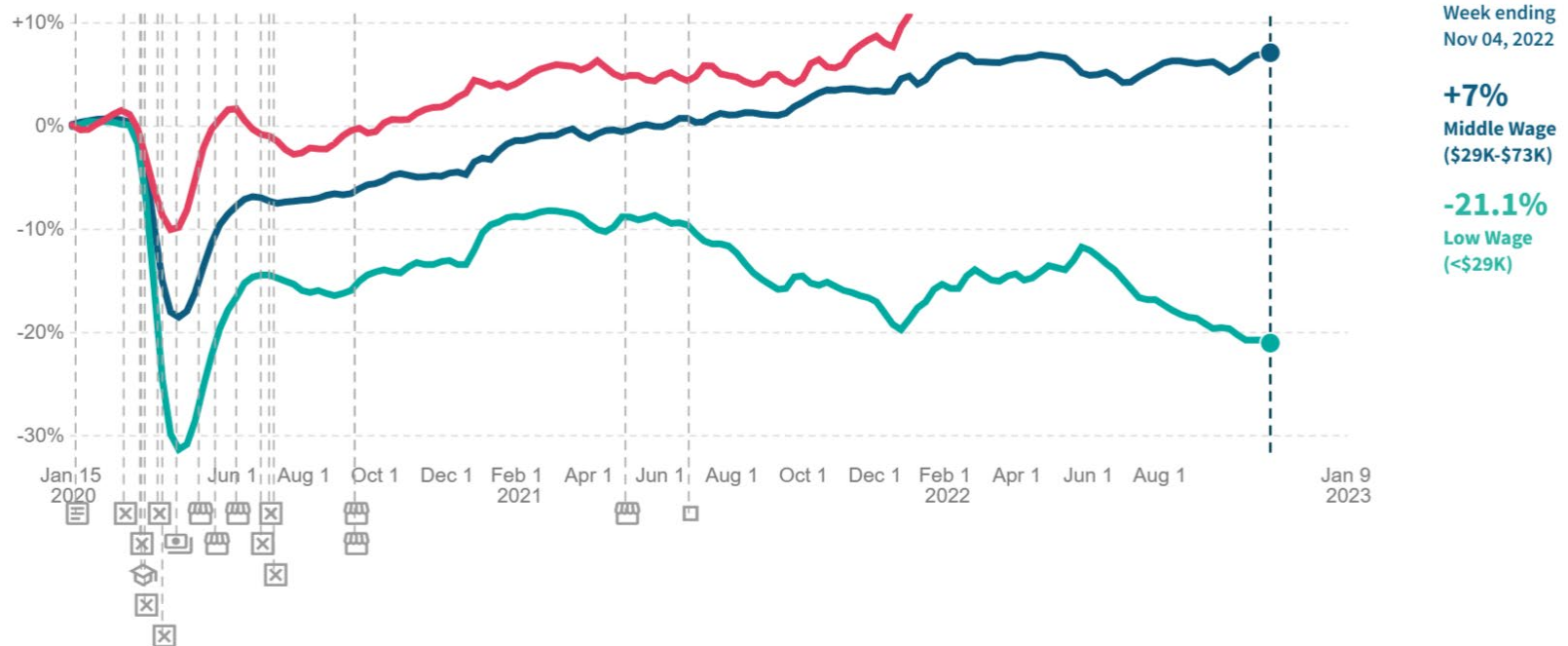
Source: U.S. Bureau of Labor Statistics.

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# Percentage Change in Employment (FL)

## Percent Change in Employment\*

In **Florida**, as of **November 04, 2022**, employment rates among workers in the middle wage quartiles **increased by 7%** compared to January 2020 (not seasonally adjusted).



data source: **Earnin, Intuit, Kronos, Paychex**

\*Change in employment rates (not seasonally adjusted), indexed to January 4-31, 2020. This series is based on payroll data from Paychex and Intuit, worker-level data on employment and earnings from Earnin, and timesheet data from Kronos. The dotted line is a prediction of employment rates based on Kronos and Paychex data.

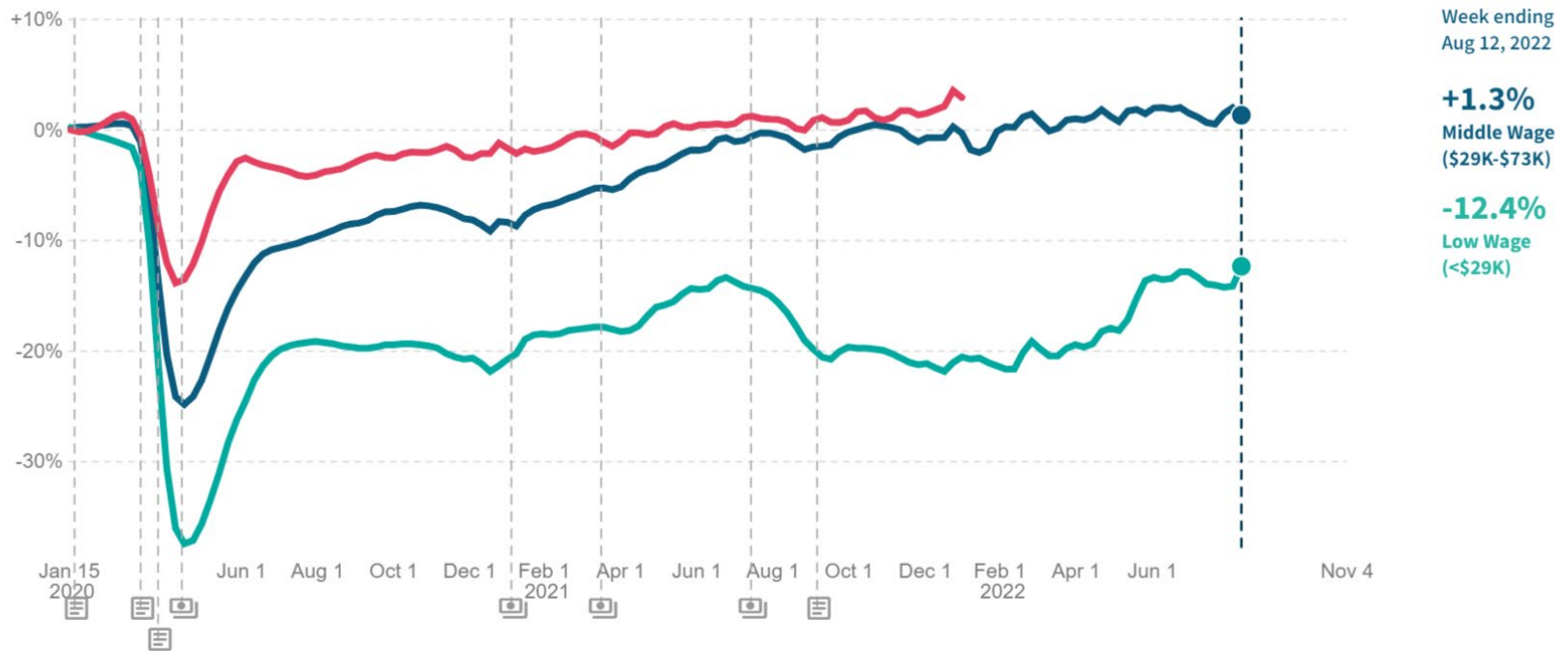
last updated: **January 06, 2023** next update expected: **January 13, 2023**

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# Percentage Change in Employment (US)

## Percent Change in Employment\*

In **the United States**, as of **August 12 2022**, employment rates among workers in the middle wage quartiles **increased** by **1.3%** compared to January 2020 (not seasonally adjusted).



\*Change in employment rates (not seasonally adjusted), indexed to January 4-31, 2020. This series is based on payroll data from Paychex and Intuit, worker-level data on employment and earnings from Earnin, and timesheet data from Kronos. The dotted line is a prediction of employment rates based on Kronos and Paychex data.

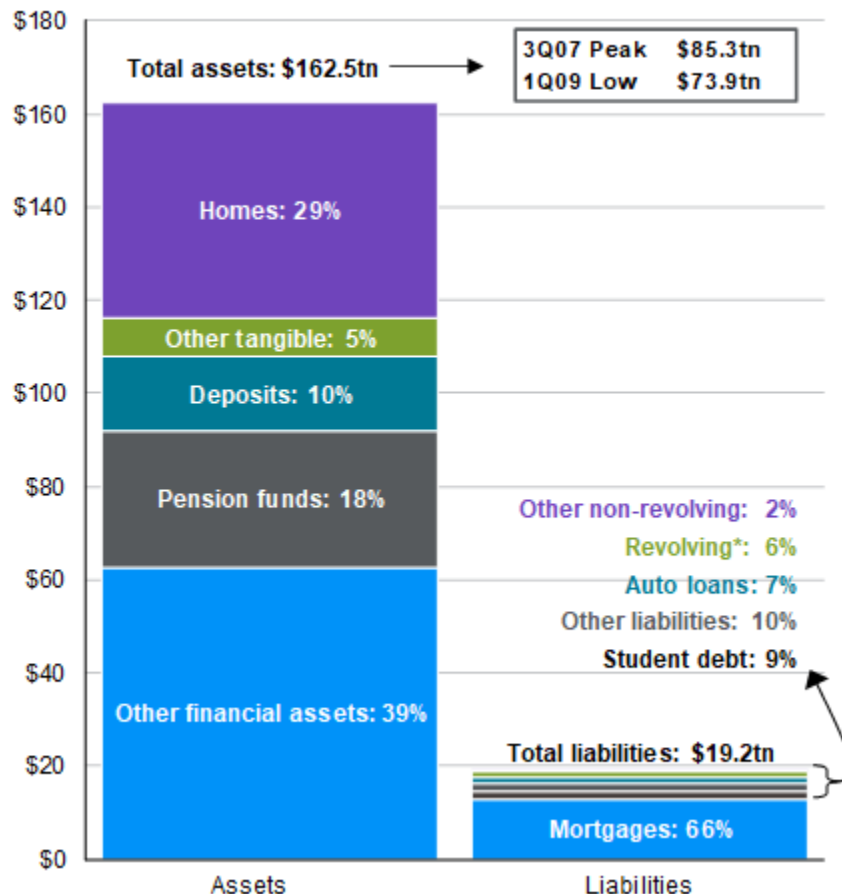
last updated: **October 17, 2022** next update expected: **November 11, 2022**

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# Consumer Finances

## Consumer balance sheet

3Q22, trillions of dollars outstanding, not seasonally adjusted



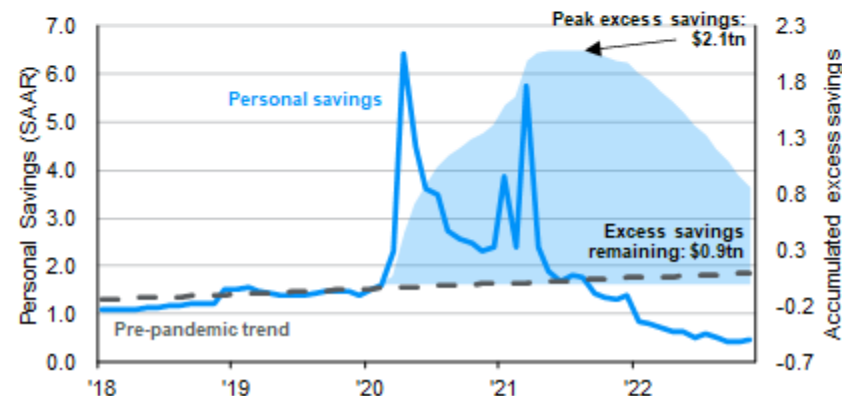
## Household debt service ratio

Debt payments as % of disposable personal income, SA



## Household excess savings

Trillions of USD



Source: FactSet, FRB, J.P. Morgan Asset Management; (Top and bottom right) BEA.

Data include households and nonprofit organizations. SA – seasonally adjusted. \*Revolving includes credit cards. Values may not sum to 100% due to rounding.

\*\*4Q22 figures for debt service ratio are J.P. Morgan Asset Management estimates. From March 2020 to August 2021, consumers amassed a peak \$2.1 trillion in excess savings relative to the pre-pandemic trend. Since August 2021, consumers have drawn down on those excess savings, with the remaining reflected in the chart annotation.

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# Question #5

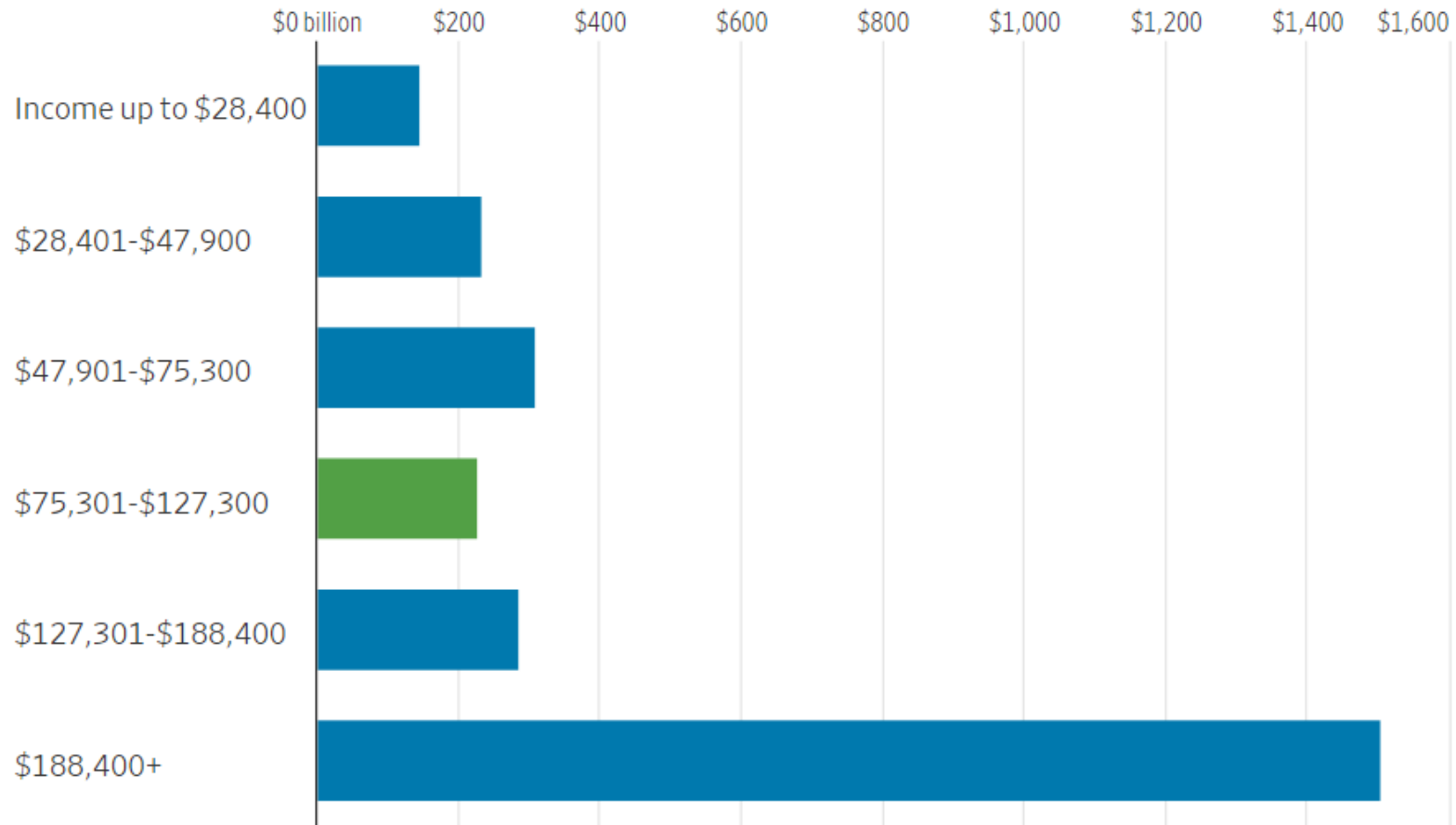
The household debt ratio the 4<sup>th</sup> quarter 2022 is \_\_\_\_\_ as/than the 4<sup>th</sup> quarter 2007

- A. Higher
- B. Lower
- C. Same



# U.S. Households' Excess Savings

Amount of money saved above average levels for each income group from Q1 2020 to Q1 2022



Note: Green bar shows upper-middle-class households.

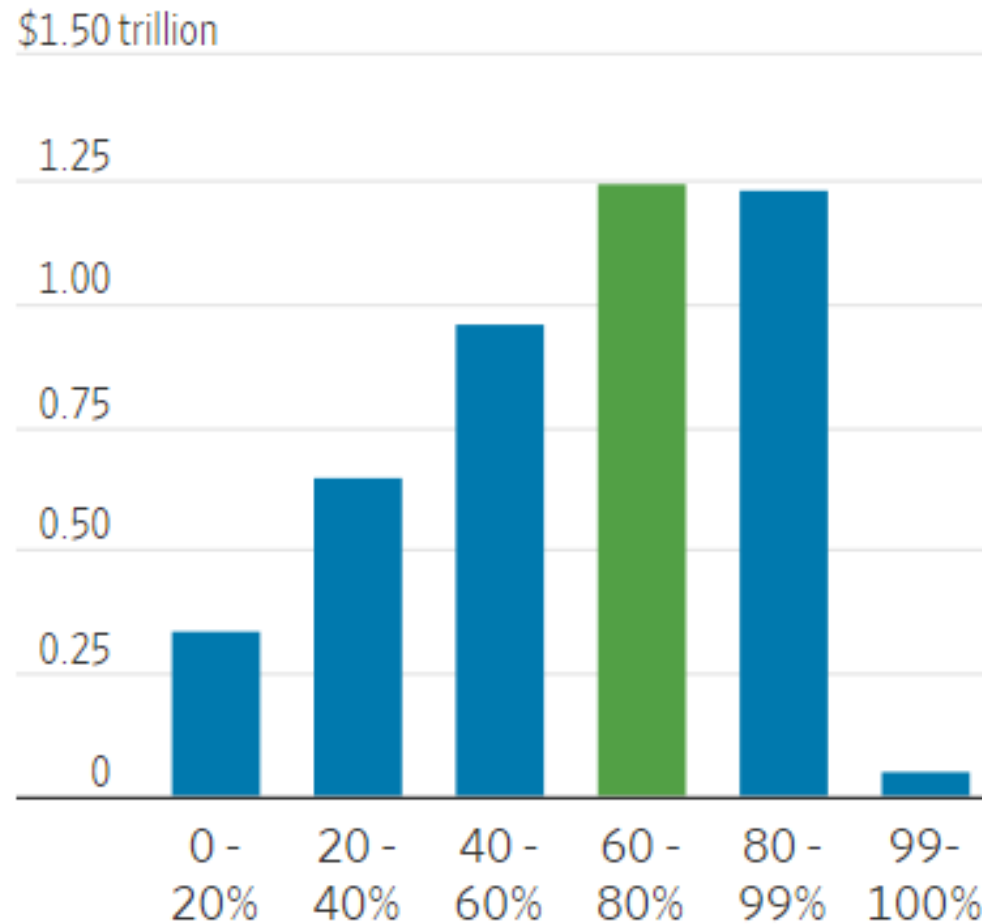
Source: Moody's Analytics

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# Consumer Debt by Income Percentile, Q1 2022



Note: Green bar shows upper-middle-class households.

Source: Federal Reserve

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# Total Outstanding Credit Card Balances

In billions; seasonally adjusted



Source: New York Fed Consumer Credit Panel/Equifax

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# Household Debt as of June 30, 2022

CATEGORY	QUARTERLY CHANGE * (BILLIONS \$)	ANNUAL CHANGE** (BILLIONS \$)	TOTAL AS OF Q2 2022 (TRILLIONS \$)
MORTGAGE DEBT	(+) \$207	(+) \$945	\$11.39
HOME EQUITY LINE OF CREDIT	(-) \$1	(-) \$3	\$0.32
STUDENT DEBT	(-) \$1	(+) \$19	\$1.59
AUTO DEBT	(+) \$33	(+) \$87	\$1.50
CREDIT CARD DEBT	(+) \$46	(+) \$100	\$0.89
OTHER	(+) \$25	(+) \$49	\$0.47
TOTAL DEBT	(+) \$312	(+) \$1197	\$16.15

Source: New York Federal Reserve Bank, 8/2/2022

\*Change from Q1 2022 to Q2 2022

\*\* Change from Q2 2021 to Q2 2022

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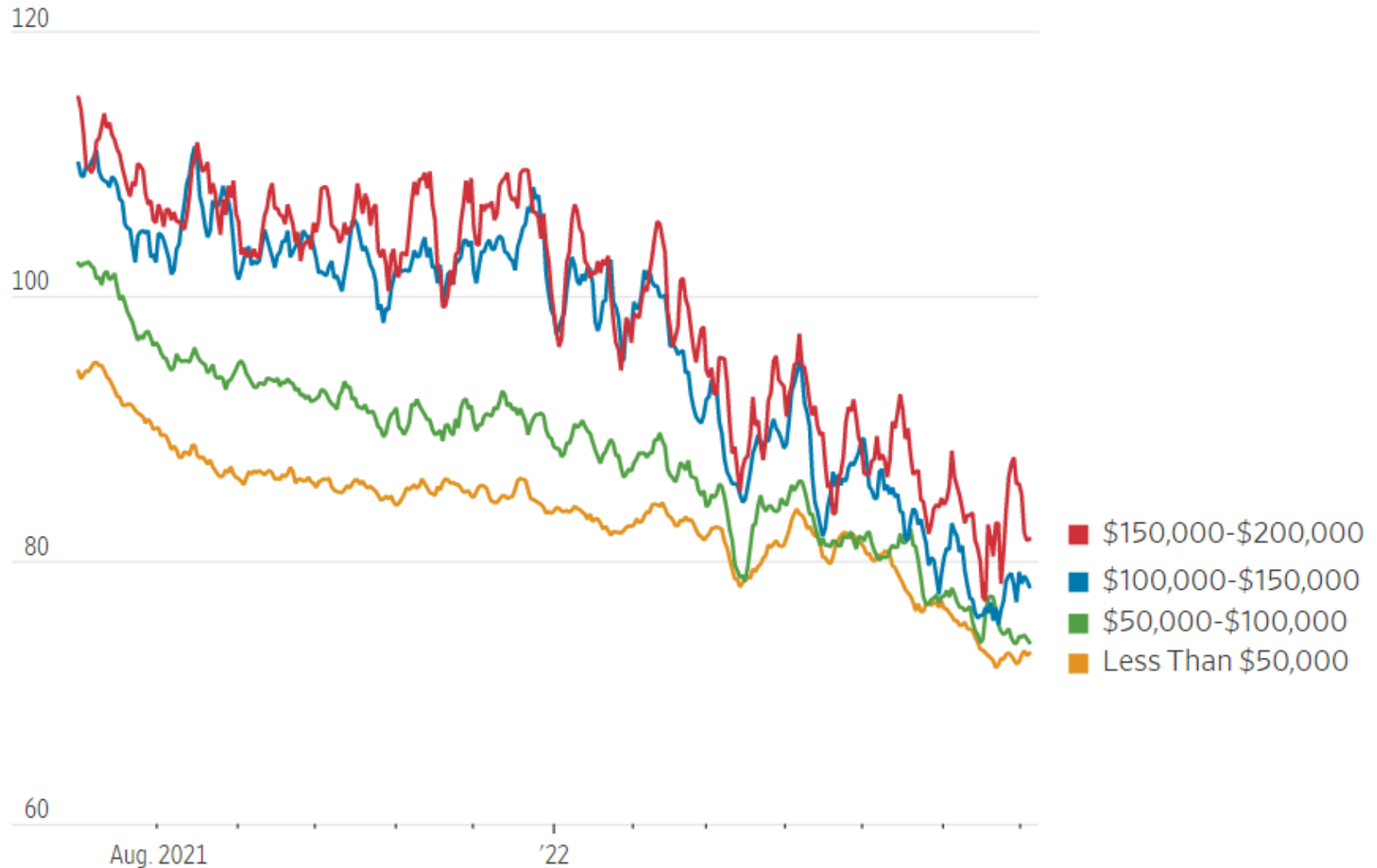
# Delinquent Loans (90 days or more)

CATEGORY <sup>1</sup>	Q2 2021	Q2 2022
MORTGAGE DEBT	0.34%	0.44%
HOME EQUITY LINE OF CREDIT	0.26%	0.32%
STUDENT LOAN DEBT	1.05%	0.98%
AUTO LOAN DEBT	1.61%	1.81%
CREDIT CARD DEBT	3.04%	3.35%
OTHER	2.88%	3.21%
ALL	0.72%	0.84%

Source: New York Federal Reserve Bank, 8/2/2022

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# Consumer Sentiment by Income

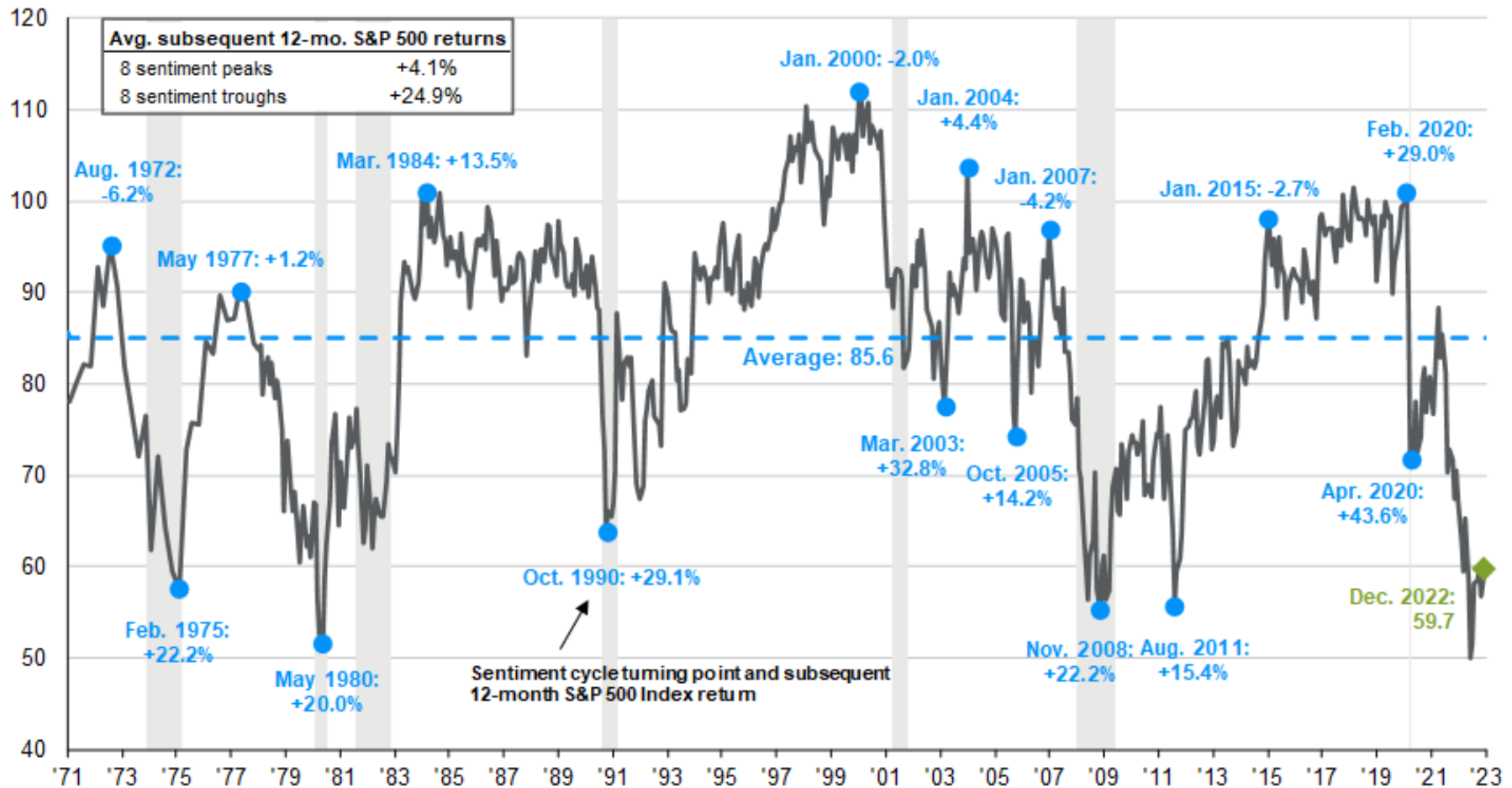


Source: Morning Consult

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# Consumer Confidence and the Stock Market

## Consumer Sentiment Index and subsequent 12-month S&P 500 returns



Source: FactSet, Standard & Poor's, University of Michigan, J.P. Morgan Asset Management.

Peak is defined as the highest index value before a series of lower lows, while a trough is defined as the lowest index value before a series of higher highs.

Subsequent 12-month S&P 500 returns are price returns only, which excludes dividends. Past performance is not a reliable indicator of current and future results.

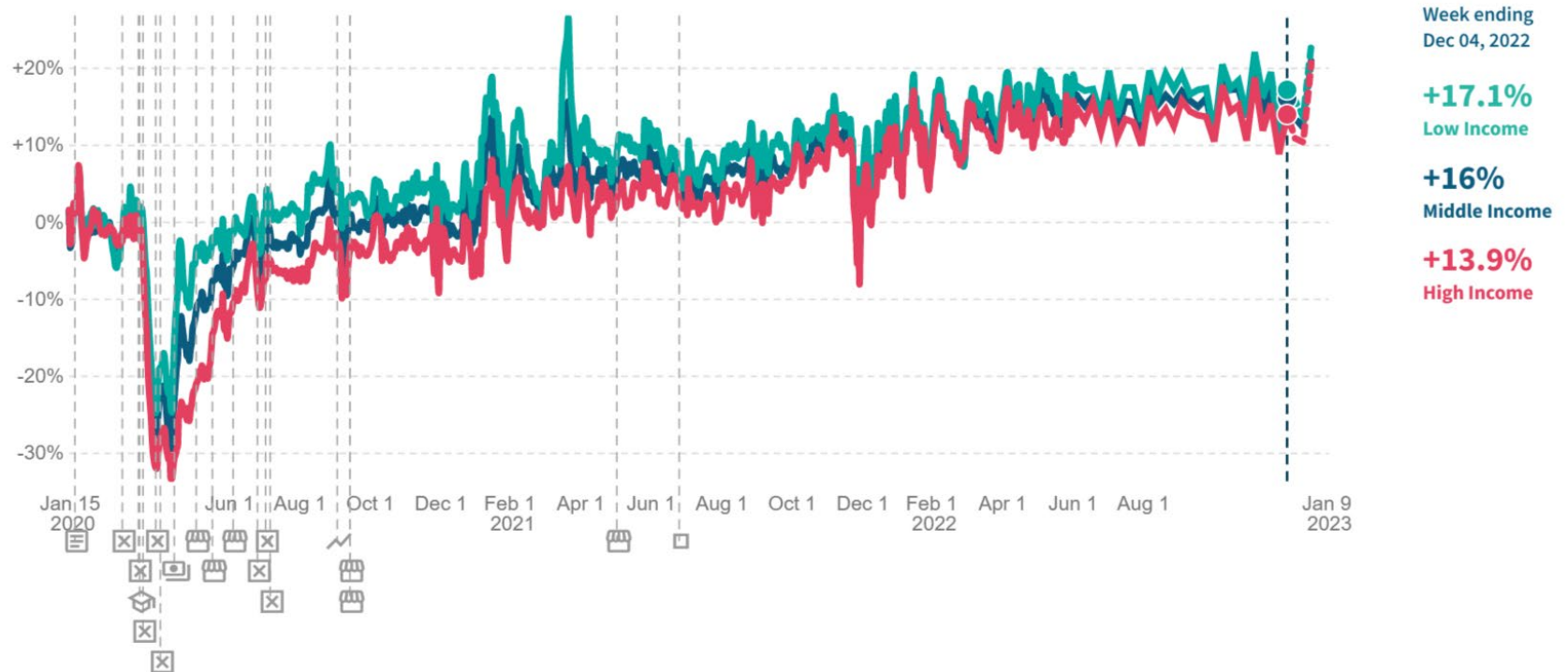
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# Percentage Change in Consumer Spending (FL)

## Percent Change in All Consumer Spending\*

In **Florida**, as of **December 04 2022**, total spending by middle-income consumers **increased** by **16%** compared to January 2020.



data source: Affinity

\*Change in average consumer credit and debit card spending, indexed to January 4-31, 2020 and seasonally adjusted. The dashed segment of the line is provisional data, which may be subject to non-negligible revisions as newer data is posted. This series is based on data from Affinity Solutions.

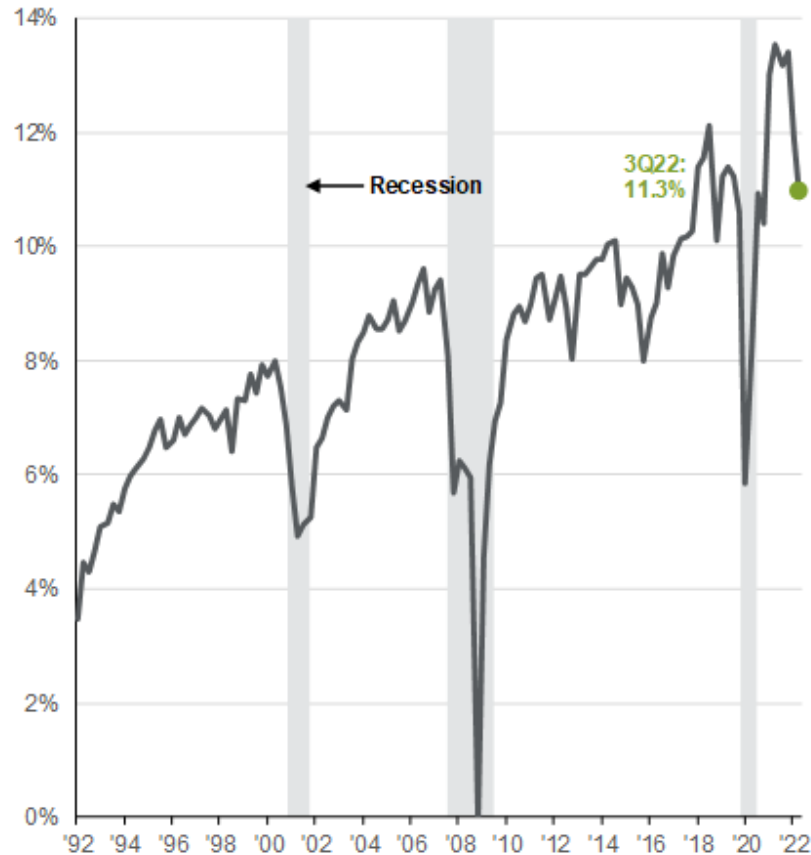
last updated: January 04, 2023 next update expected: January 11, 2023

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# Profit Margins

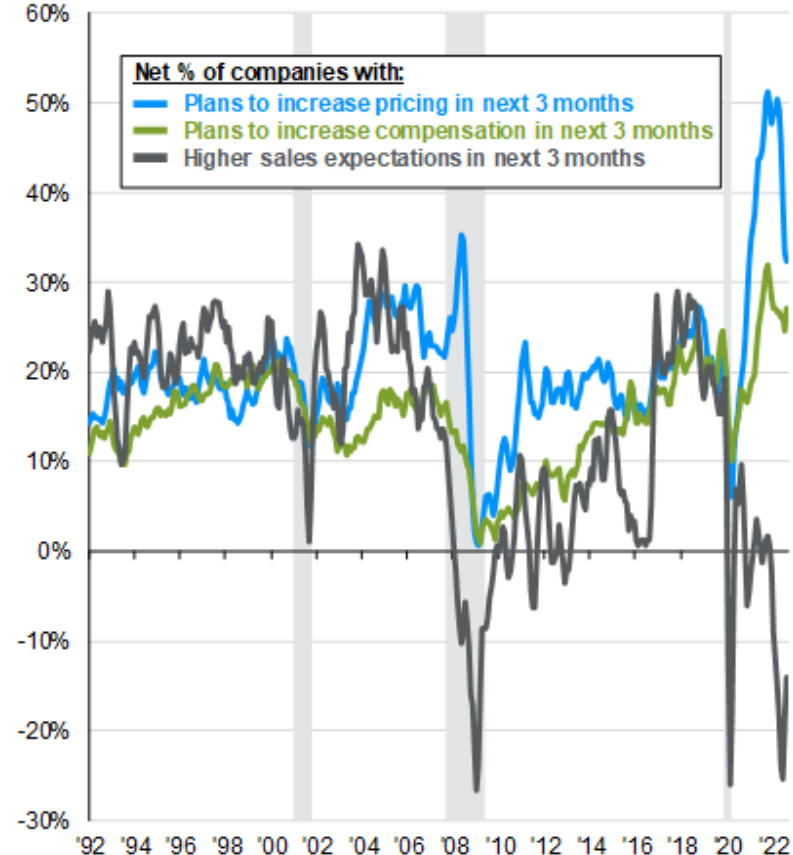
## S&P 500 profit margins

Quarterly operating earnings/sales



## Pricing, wages, and sales expectations for businesses

NFIB Small Business Economic Survey, three-month moving average



Source: Compustat, FactSet, NFIB, Standard & Poor's, J.P. Morgan Asset Management. Past performance is not indicative of future returns. (Right) All three data series are net and represent the % of respondents answering higher less the % of respondents answering lower. Data reflects answers to the following three questions: "What are your pricing plans in the next 3 months?", "What are your compensation plans in the next 3 months?", "What are your sales expectations in the next 3 months?"

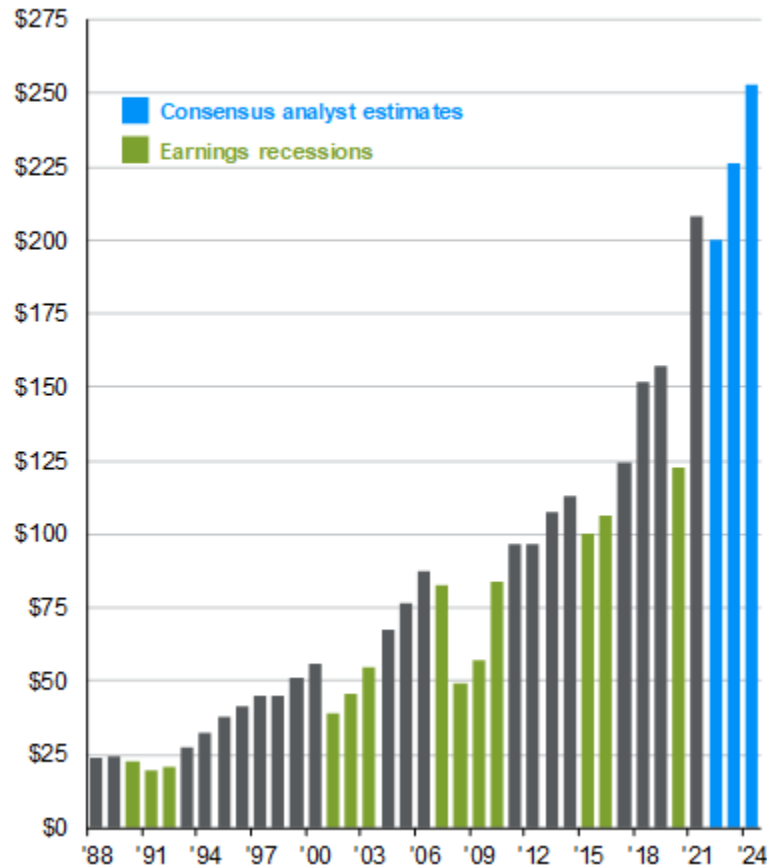
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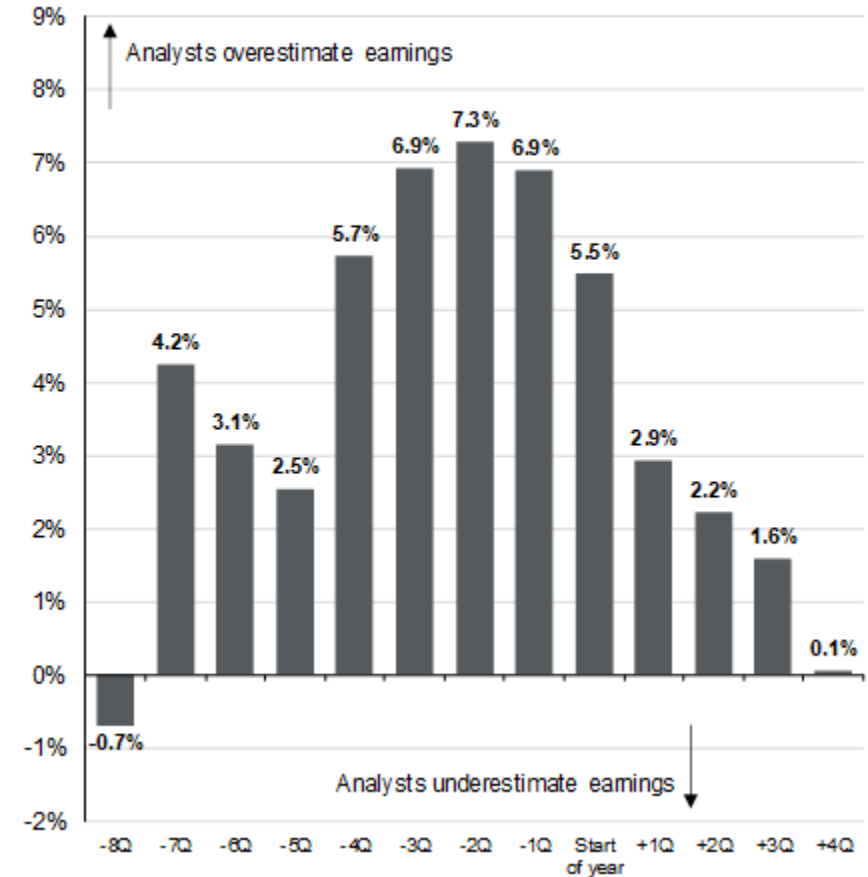


# Corporate Earnings

**S&P 500 earnings per share**  
Index annual operating earnings



**Average analyst over/underestimate of annual earnings**  
S&P 500, pro-forma EPS, 1996 - 2021



Source: Compustat, FactSet, NFIB, Standard & Poor's, J.P. Morgan Asset Management. Past performance is not indicative of future returns. (Right) All three data series are net and represent the % of respondents answering higher less the % of respondents answering lower. Data reflects answers to the following three questions: "What are your pricing plans in the next 3 months?", "What are your compensation plans in the next 3 months?", "What are your sales expectations in the next 3 months?"

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# Question #6

The S&P 500 consensus for 2024 is  
\_\_\_\_\_ as/than 2021

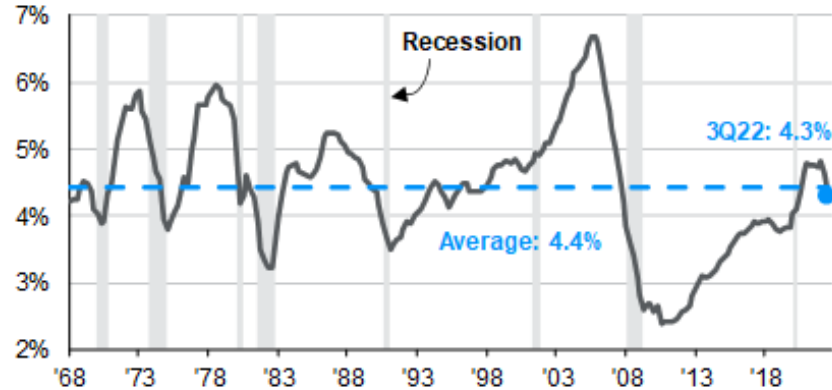
- A. Higher
- B. Lower
- C. Same

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# Business Environment

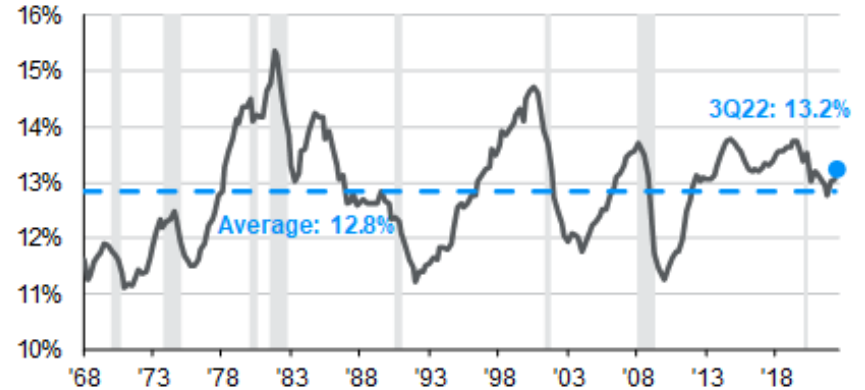
## Residential investment as a % of GDP

Quarterly, seasonally adjusted



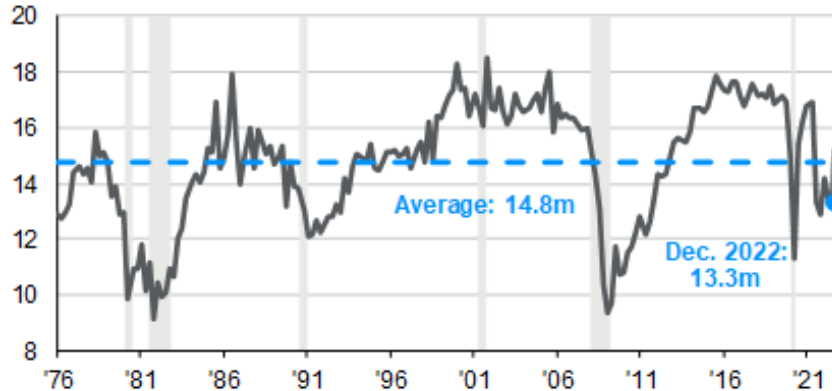
## Business fixed investment as a % of GDP

Quarterly, seasonally adjusted



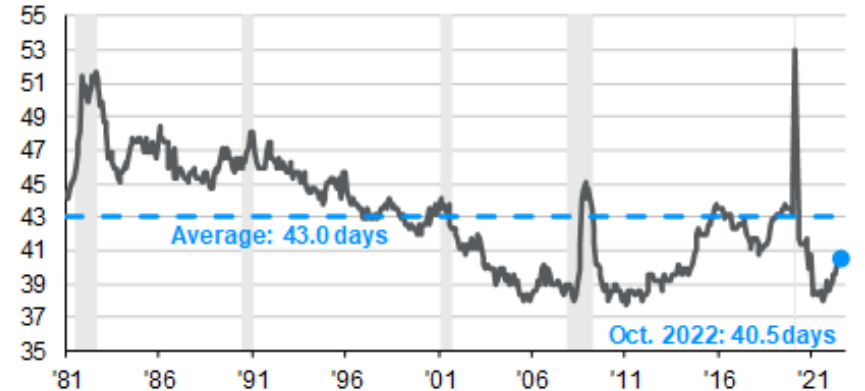
## Light vehicle sales

Mil vehicles, seasonally adjusted ann. rate



## Total business inventory/sales ratio

Days of sales, monthly, seasonally adjusted



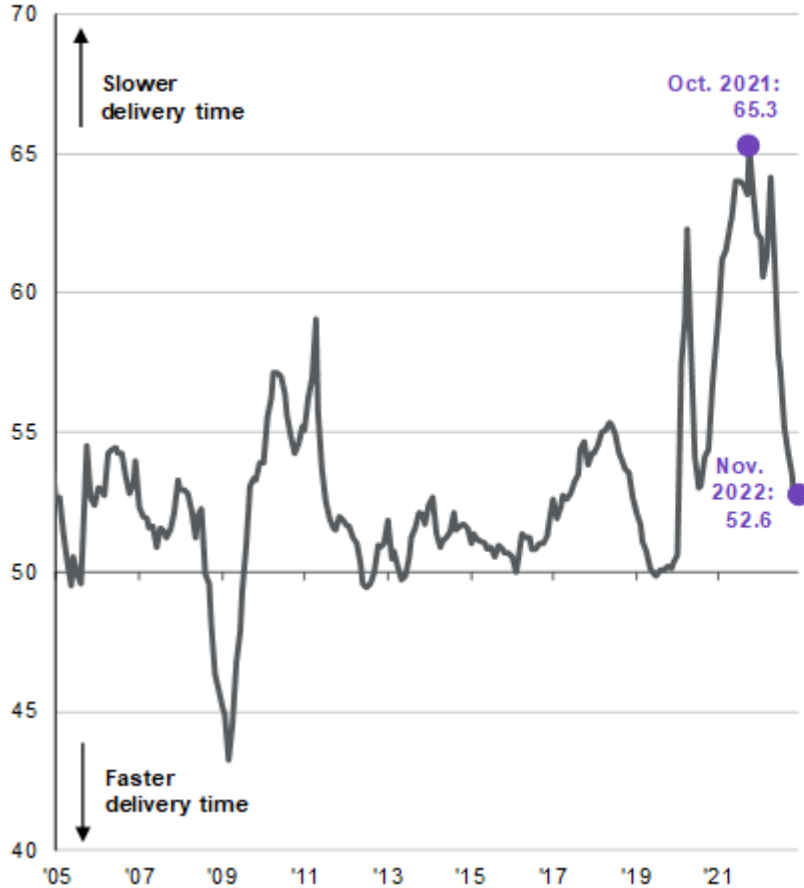
Source: BEA, Census Bureau, FactSet, J.P. Morgan Asset Management. Data for light vehicle sales is quarterly apart from the latest monthly data point.  
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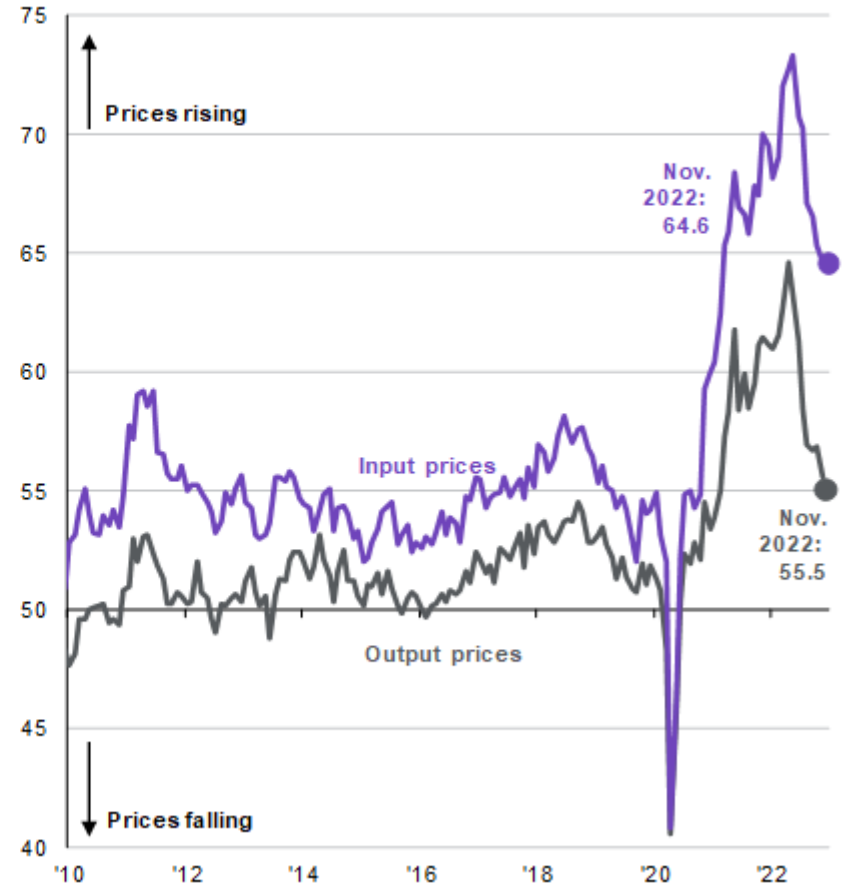
# Global Supply Chains

## Global PMI suppliers' delivery times index\*

Figure shown is 100 - Global PMI suppliers' delivery times index



## Global PMI input and output prices\*\*



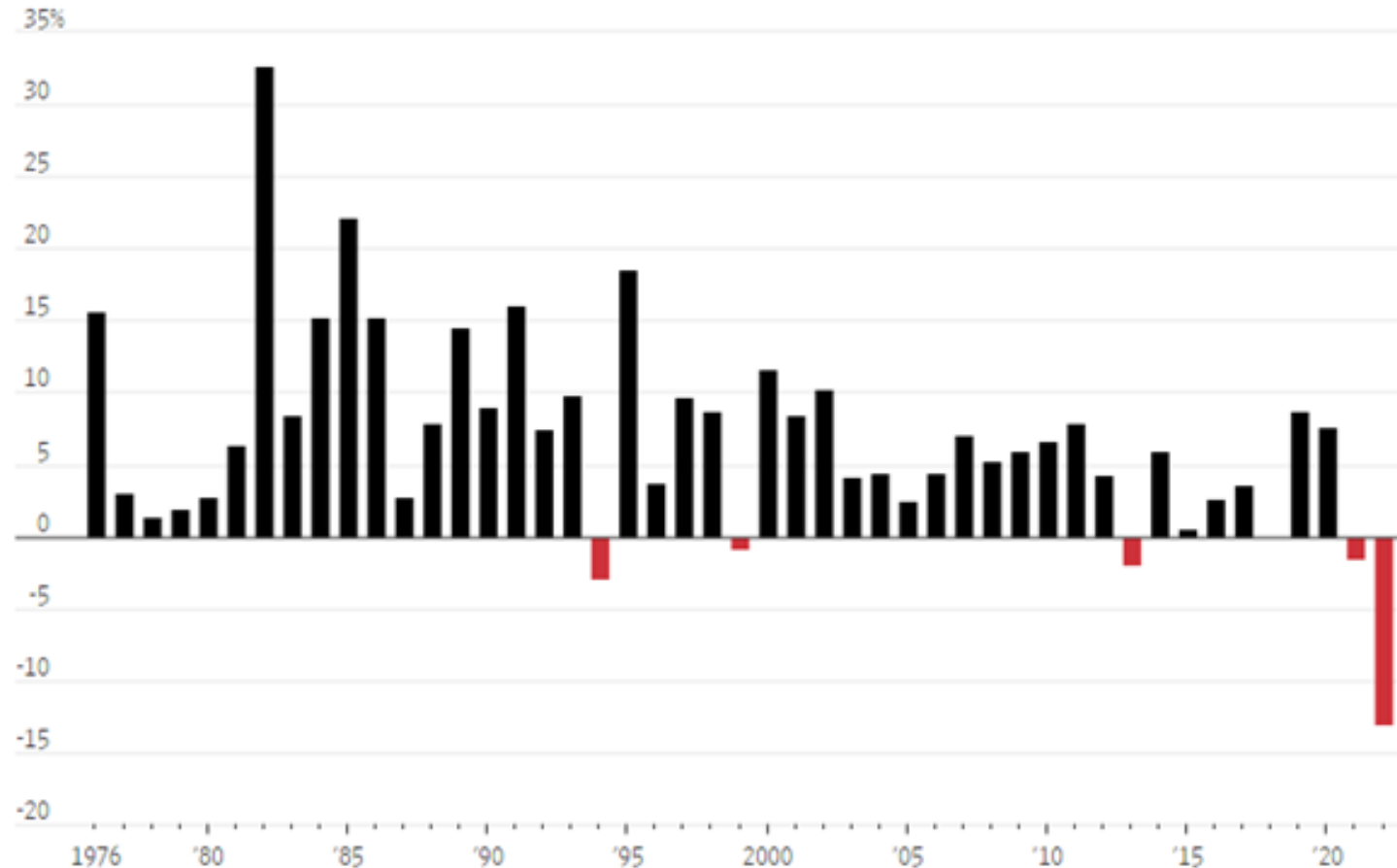
Source: Standard & Poor's, J.P. Morgan Asset Management.

\*Participants in Standard & Poor's PMI business surveys, conducted in 44 countries, are asked: "Are your suppliers' delivery times slower, faster or unchanged on average than one month ago?". Index includes the manufacturing and construction sectors. PMI score reflected above is 100 - PMI report by Standard & Poor's. A reading of 50 = no change, <50 = faster delivery time, >50 = slower delivery time. \*\*Participants are asked: "Are input/output prices the same, higher or lower?". Values shown reflect the composite index, which includes both manufacturing and services. A reading of 50 = no change, >50 = price increase, <50 = price decrease. Guide to the Markets - U.S. Data are as of January 5, 2022.

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# Fixed Income Returns

Bloomberg U.S. Aggregate bond index total return



Source: FactSet

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# Session Summary

## Inflation

- Sticky – Housing
- Volatile – Food & Energy

## Interest Rates

- Fed Funds terminal rate expected to be 5.00-5.50%
- Yield Curve inverted from 1 year to 10 years
  - Not all yield curve inversions have led to a recession
  - All recessions have been preceded by an inverted yield curve

## Budget Impact

- Revenue
  - Housing sector has slowed but prices have not collapsed
  - Sales tax revenue have held up
- Expenses
  - Rising labor costs
  - Goods and services costs are higher
- Consider increasing operating and capital budgets

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# Questions



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