Where Do We Go From Here?: Expect Volatility in Q4, Strong Economy in H1 2026, Structural Housing Headwinds

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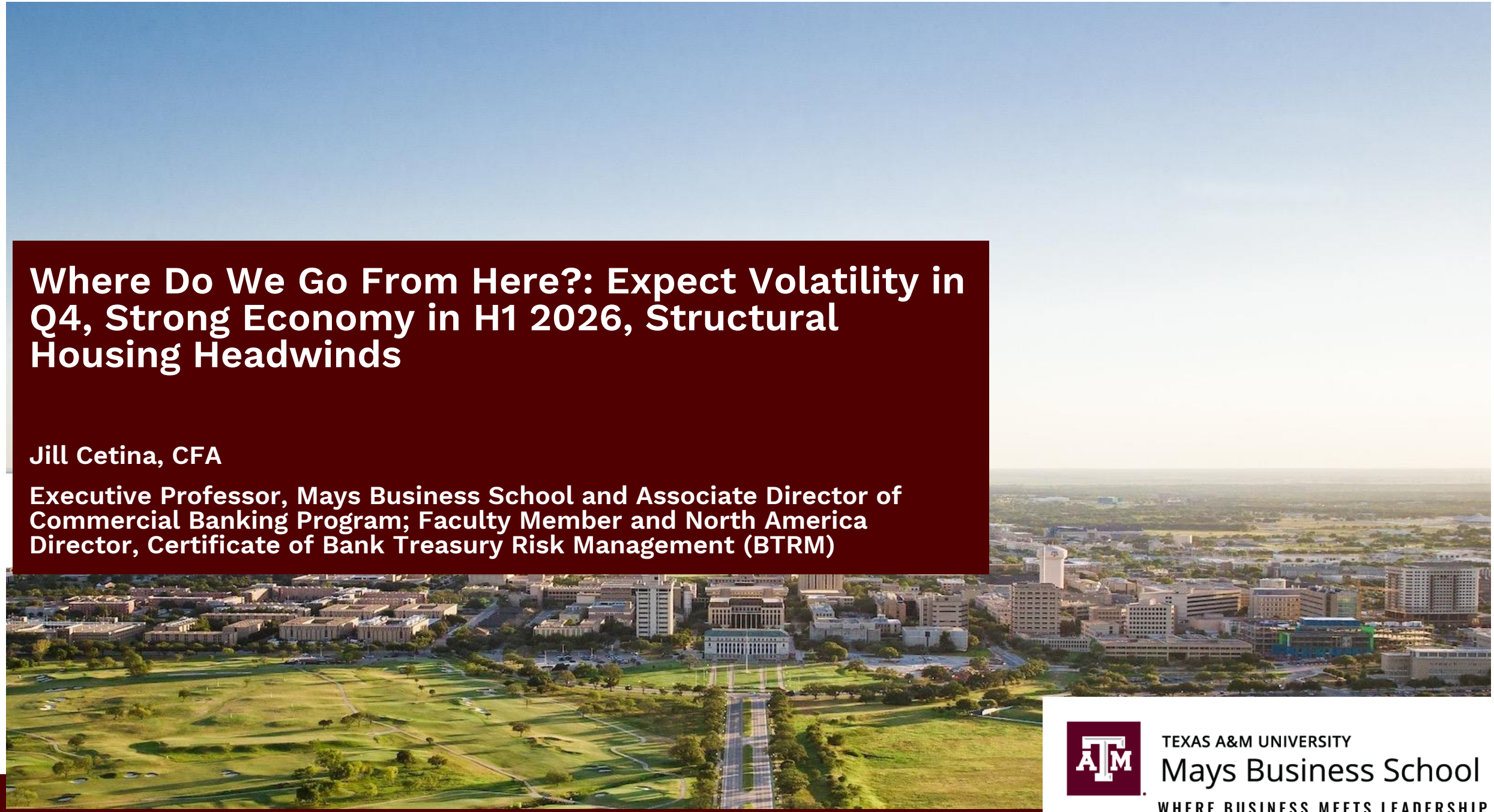

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Agenda

- Key messages
- Where do we go from here?
- What about housing?
- Discussion/questions

Key messages

- Multi-decade dynamics have left us with significant economic challenges. The Administration has not published an economic plan, but its broad aims appear to be to strengthen US national security through reindustrialization and addressing government debt to GDP through higher economic growth.

- Six key areas of US economic policy
  - Fiscal policy
  - Trade/tariffs/reindustrialization – revenue source – expect them to be permanent
  - Monetary policy/role of the Fed
  - Immigration
  - Energy
  - Deregulation
- In early 2025 the market focused on economic positives – deregulation and taxes – and ignored growth negatives like tariffs, DOGE layoffs, immigration and dislocations in supply chains. Anticipate volatile Q4 2025 due to resolution of government shutdown vs stronger US economy narrative and pressures associated with ongoing Fed QT. In H1 2026, tax cuts will be a significant economic tailwind.

- Market may have Fed rate path priced too dovish and ongoing QT creates liquidity risks – expect volatility to rise into year end. But look for H1 2026 to be strong due to OBBBA tax cuts providing stimulus. Monetary policy outlook will depend on new Fed leadership.

- Housing is important to accelerating US economic growth, but faces structural headwinds related to demographics. Broadly demographics need more attention from US economic policymakers.

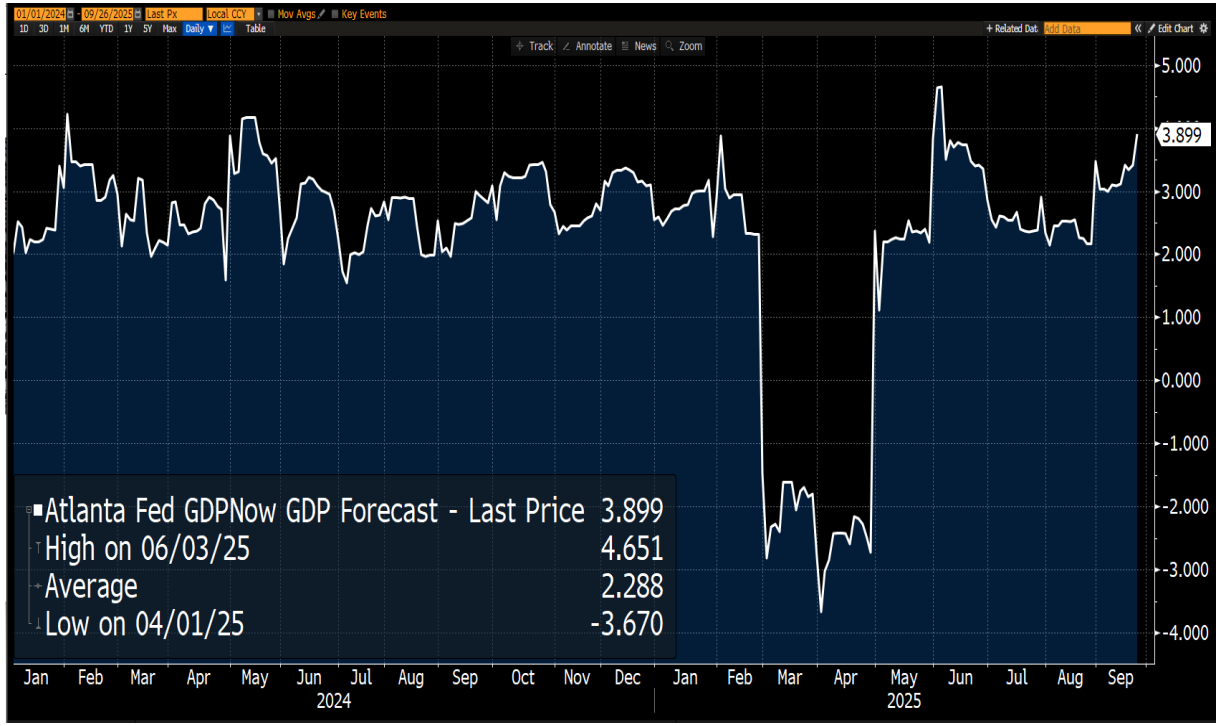
US Administration policy mix -- expected impact on US economic growth and inflation

- Growth positive
  - Deregulation
  - Tax cuts
  - Increased investment
- Growth negative
  - Tariffs – viewed as a revenue source
  - Immigration
  - Energy
  - Economic policy uncertainty
- Lower inflation
  - Tighter fiscal/DOGE (until OBBBA)
  - Deregulation
- Higher inflation
  - Immigration
  - Tariffs
  - Tax cuts
  - Dollar deprecation

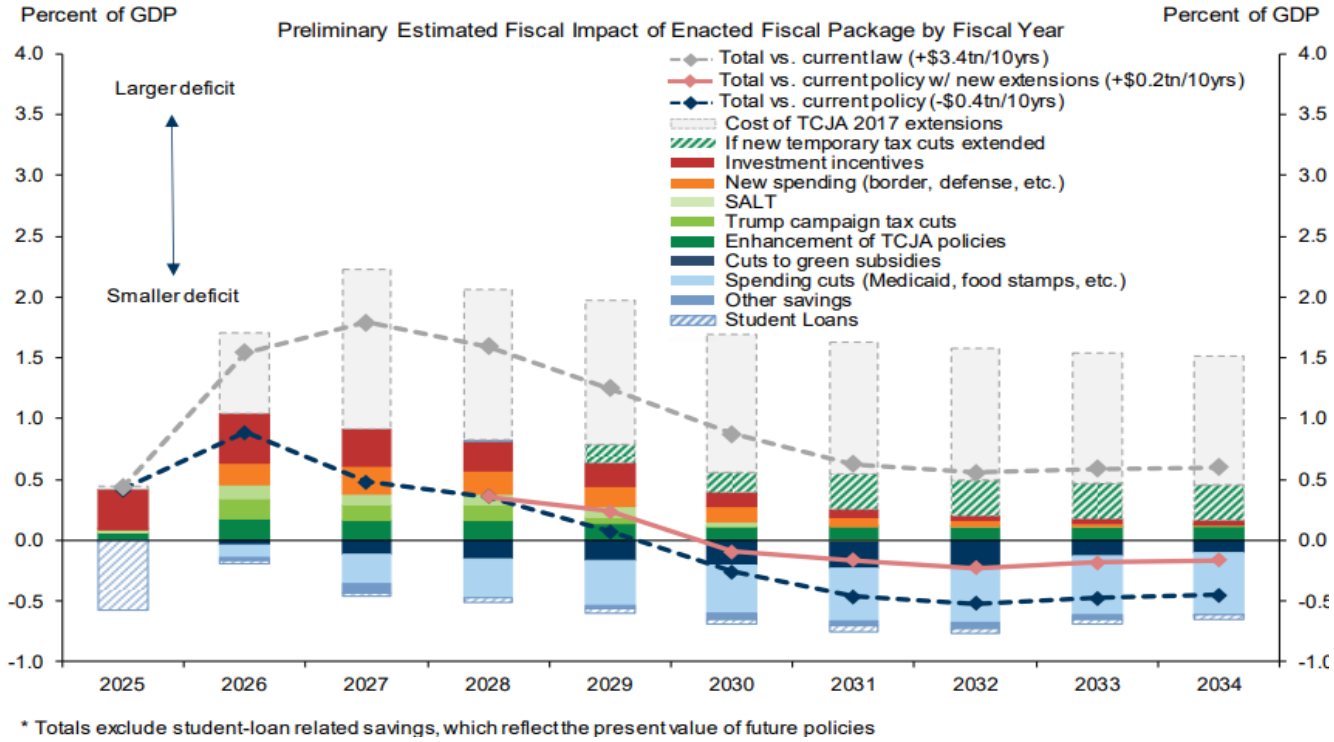
2025 US growth forecasts -- tariffs, DOGE, uncertainty & immigration impact H1 … fiscal, investment & DOGE layoffs to impact H2 25 & H1 26

SURVEY	2025	Q1	Q2	Q3	Q4
Sept 25	1.7%	**-0.6%**	**3.8%**	1.7%	1.4%
May 25	1.4%	**-0.3%**	1.4%	0.8%	1.2%
April 25	1.4%	**-0.3%**	0.8%	0.6%	1.1%
Mar 25	2.0%	1.2%	1.5%	1.7%	1.8%
Jan 25	2.2%	2.1%	2.0%	2.0%	2.0%
Oct 24	1.8%	1.7%	1.9%	2.0%	2.1%

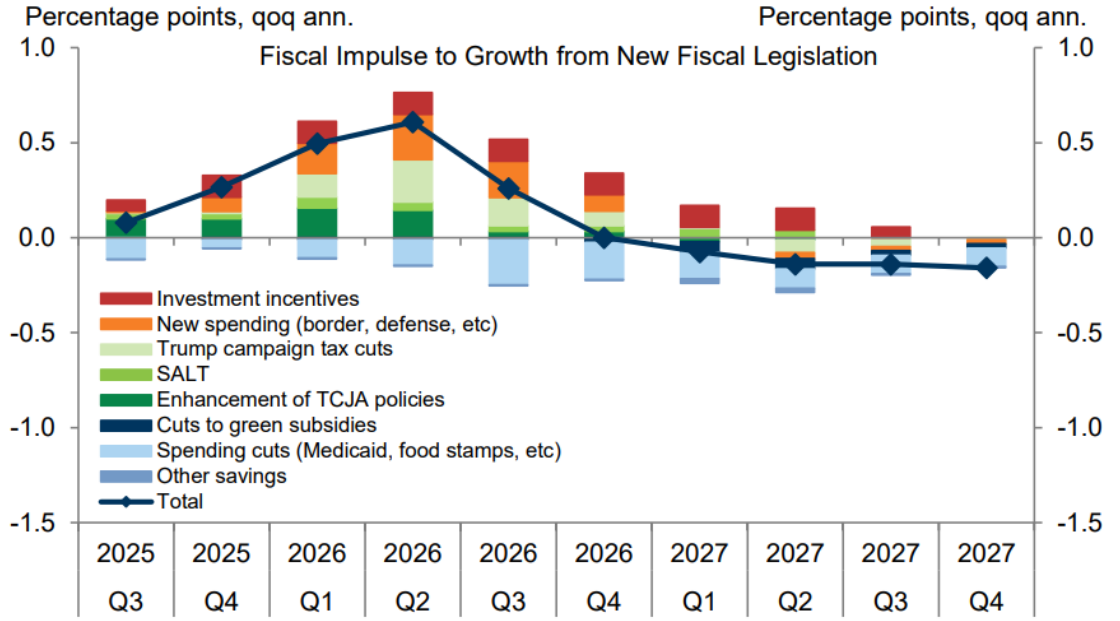
Consensus forecast from Bloomberg survey for US GDP growth; Sept 26, 2025
Bold values = actual data, inclusive of GDP revisions



OBBBA – Frontloaded Tax Cuts; Backloaded Spending Cuts = Fiscal Stimulus in 2026

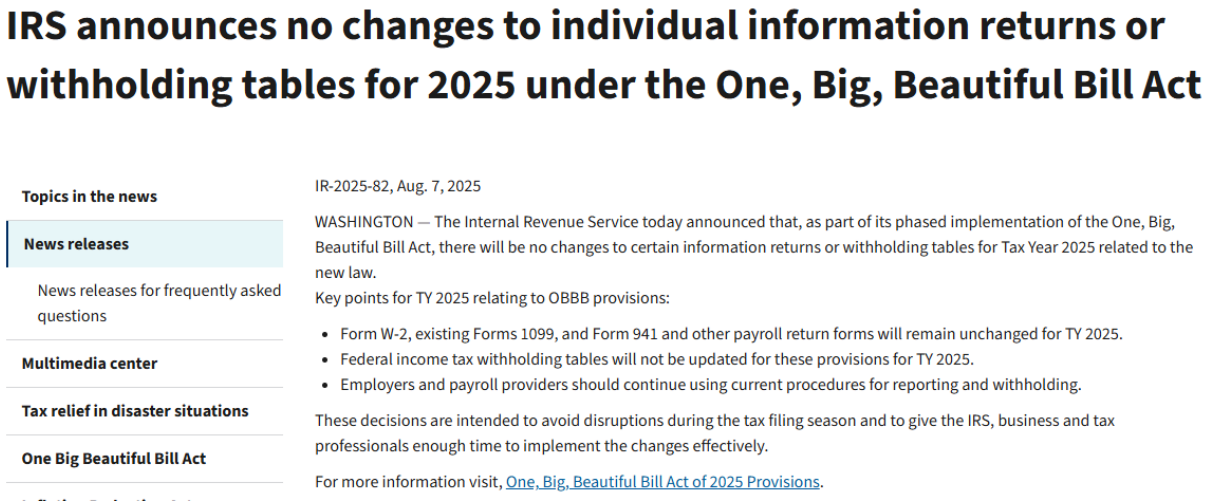


* Totals exclude student-loan related savings, which reflect the present value of future policies



Source: Goldman Sachs Global Investment Research.

But US fiscal stimulus in 2026 looks to be more concentrated than GS predicts -- why?



IRS announces no changes to individual information returns or withholding tables for 2025 under the One, Big, Beautiful Bill Act

Topics in the news

News releases

News releases for frequently asked questions

Multimedia center

Tax relief in disaster situations

One Big Beautiful Bill Act

IR-2025-82, Aug. 7, 2025

WASHINGTON — The Internal Revenue Service today announced that, as part of its phased implementation of the One, Big, Beautiful Bill Act, there will be no changes to certain information returns or withholding tables for Tax Year 2025 related to the new law.

Key points for TY 2025 relating to OBBB provisions:

- Form W-2, existing Forms 1099, and Form 941 and other payroll return forms will remain unchanged for TY 2025.
- Federal income tax withholding tables will not be updated for these provisions for TY 2025.
- Employers and payroll providers should continue using current procedures for reporting and withholding.

These decisions are intended to avoid disruptions during the tax filing season and to give the IRS, business and tax professionals enough time to implement the changes effectively.

For more information visit, One, Big, Beautiful Bill Act of 2025 Provisions.

- IRS announced on Aug 7th
- OBBBA retroactive to Jan 2025 – so a full year of OBBBA tax cuts will be delivered as refunds in H1 2026.
- If refunds spent in H1 2026, it could boost real GDP by ~0.5%.
- If consumers realize they will get a refund, it could boost 2025 holiday spending.
- Fiscal stimulus/tax rebates could provide $ to allow companies to pass on tariff costs to consumers, permitting inflation to rise.

Economists' near-term US inflation expectations still a touch lower than the bond market

- Bloomberg consensus forecasts puts Q4 US CPI at 3.1%, near fixed income markets (+3%).

- Inflation derivatives market – one-year and two-year inflation swaps at 3.2% and 2.9%, respectively.

- 60/40 equity/bond portfolio does not work well when inflation > 3%. For this reason, 10-year yield could come under pressure.

United States | Browse | Consumer Prices (YoY%) | Yearly | Quarterly

Q2 25 Actual 2.5 | Q2 25 Forecast 2.5

	Q3 25	Q4 25	Q1 26	Q2 26	Q3 26	Q4 26	Q1 27	Q2 27
Median	2.9	3.1	2.9	3.1	2.9	2.6	2.6	
Mean	2.9	3.1	2.9	3.1	2.9	2.7	2.6	
Bloomberg Weighted Average	2.9	3.1	2.9	3.1	2.9	2.7	2.6	
High	4.0	4.5	4.5	4.5	4.5	4.5	4.5	
Low	2.7	2.1	1.6	1.9	1.8	1.7	2.0	
Responses	56	56	54	54	54	53	30	
Sept. Survey	2.9	3.1	2.9	3.1	2.9	2.6	2.6	
Aug. Survey	2.9	3.0	2.9	3.0	2.7	2.6	2.5	

United States | Browse | Core PCE Price Index (YoY%) | Yearly | Quarterly

Q2 25 Actual 2.7 | Q2 25 Forecast 2.7

	Q3 25	Q4 25	Q1 26	Q2 26	Q3 26	Q4 26	Q1 27	Q2 27
Median	3.0	3.2	3.1	3.1	2.8	2.5	2.4	
Mean	3.0	3.2	3.1	3.0	2.8	2.6	2.4	
Bloomberg Weighted Average	3.0	3.2	3.1	3.0	2.8	2.6	2.4	
High	3.7	4.3	4.2	4.0	4.1	4.1	4.2	
Low	2.5	2.4	2.1	1.8	1.5	1.4	2.0	
Responses	55	55	53	53	53	51	29	
Sept. Survey	3.0	3.2	3.1	3.1	2.8	2.5	2.4	
Aug. Survey	3.0	3.2	3.1	3.0	2.8	2.5	2.3	

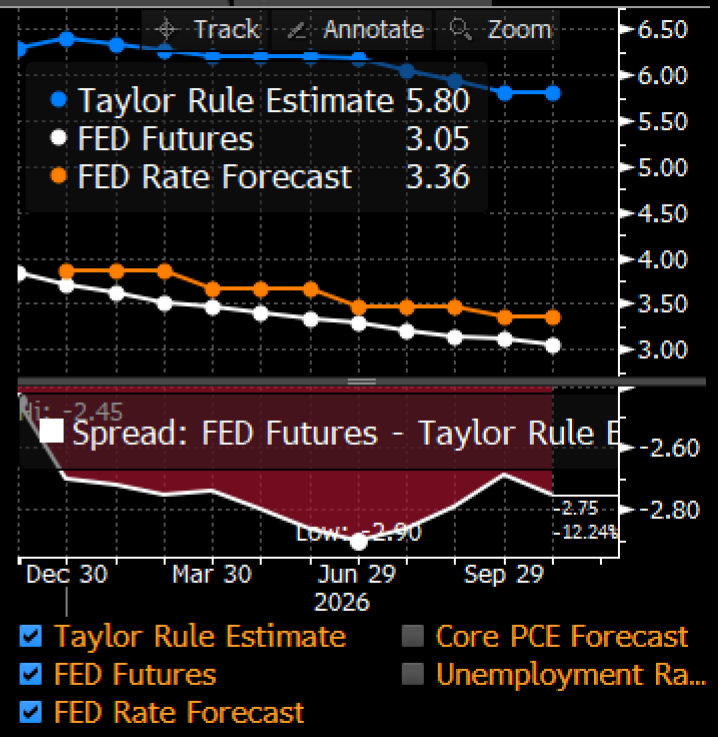
Sept Fed rate cut poorly justified; combo of monetary + fiscal stimulus could mean H4L inflation

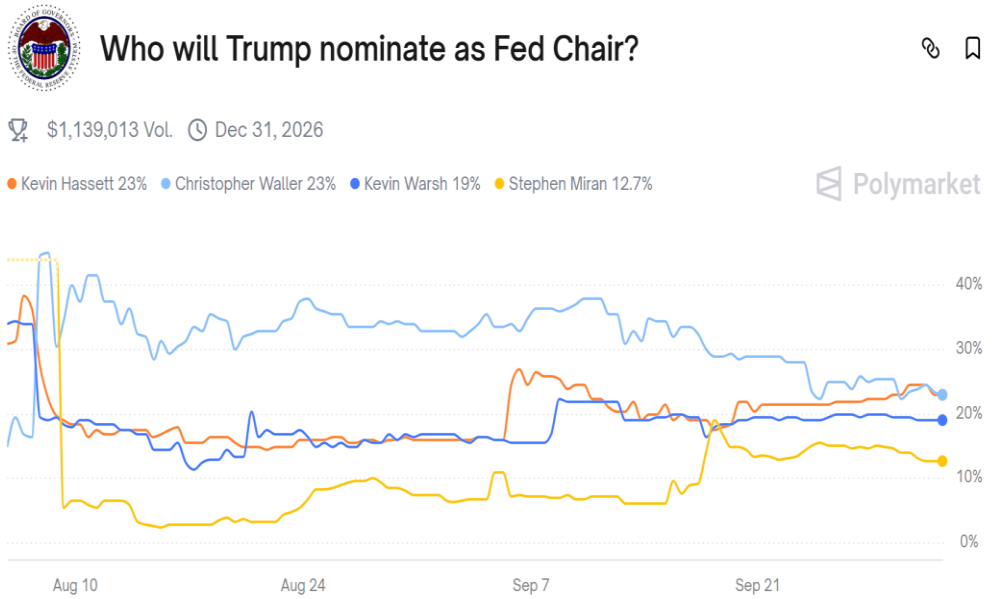
United States | Model: Baseline Taylor Rule Model

1) Taylor Rule Model | 2) Forward Looking Est | 3) Model Performance | 4) Outlook Matrix

Contributor: ECFC Contributor Composite

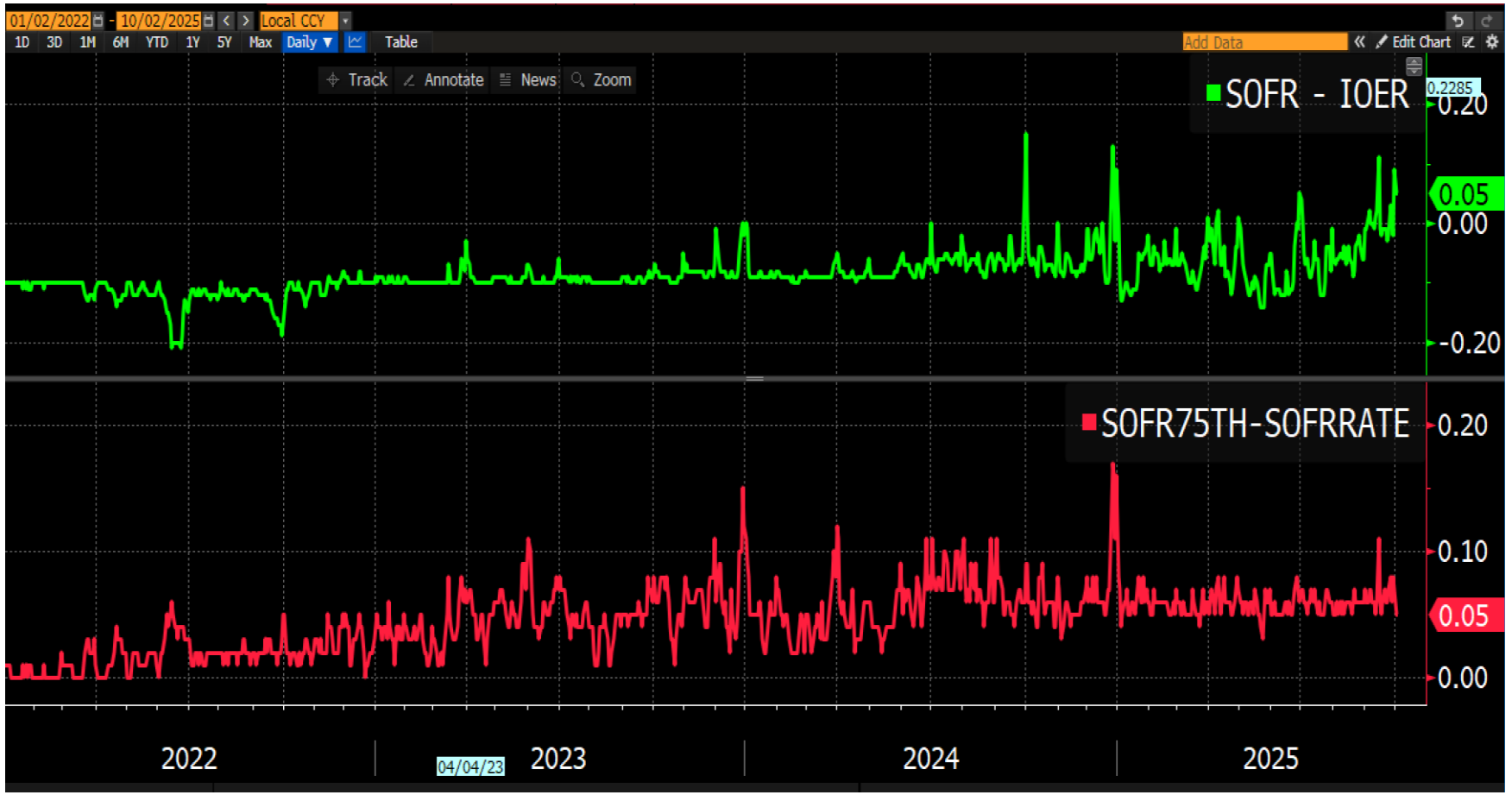
Month	Inflation Core PCE Forecast	Unemp. Forecast	Taylor Rule Estimate	FED Funds Futures
Oct 25	3.00	4.33	6.17	4.08
Nov 25	3.10	4.37	6.29	3.84
Dec 25	3.20	4.40	6.40	3.70
Jan 26	3.17	4.41	6.34	3.62
Feb 26	3.13	4.43	6.27	3.52
Mar 26	3.10	4.44	6.21	3.47
Apr 26	3.10	4.45	6.20	3.40
May 26	3.10	4.45	6.20	3.34
Jun 26	3.10	4.46	6.19	3.29
Jul 26	3.00	4.44	6.06	3.20
Aug 26	2.90	4.42	5.93	3.14
Sep 26	2.80	4.40	5.80	3.11
Oct 26	--	--	--	3.05



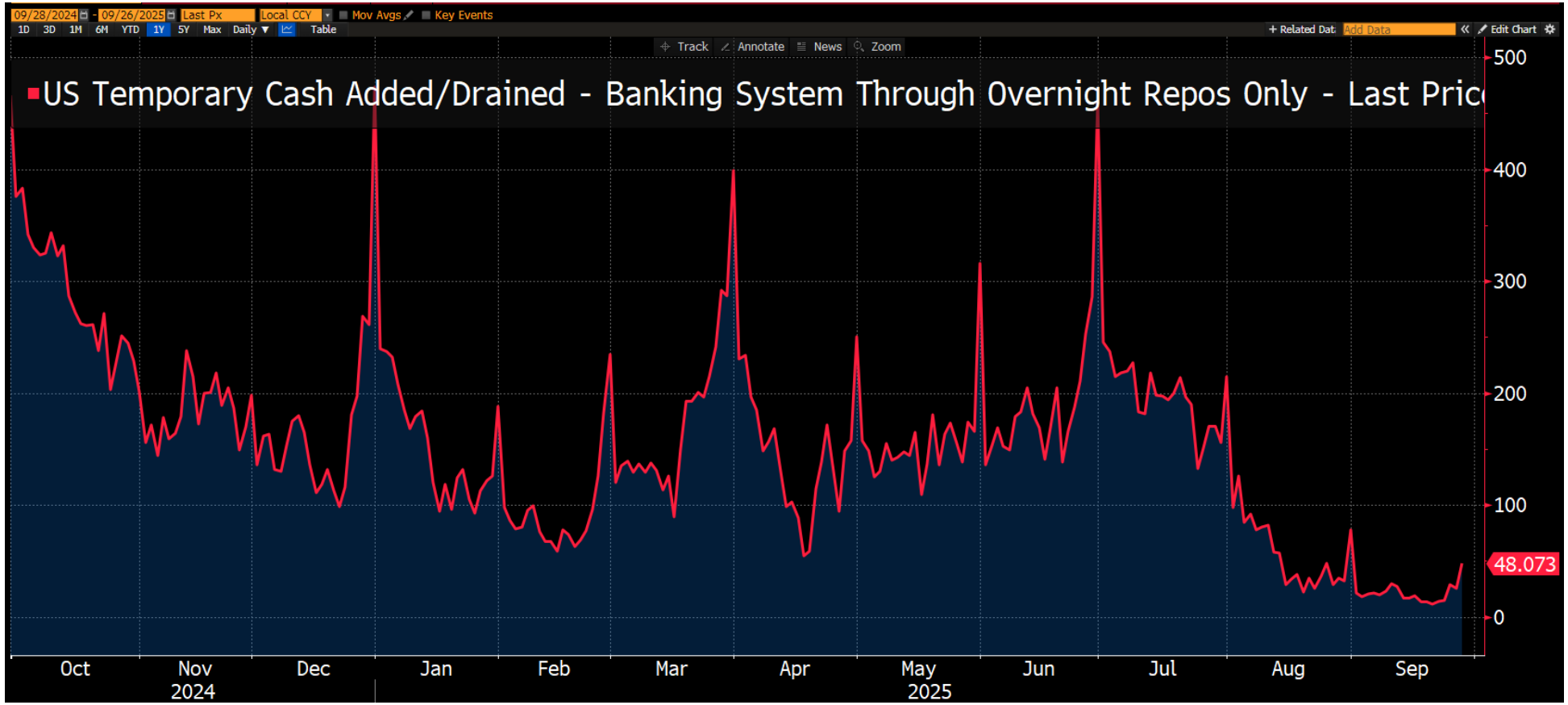


Quantitative tightening -- we are approaching a pain point for US bank liquidity

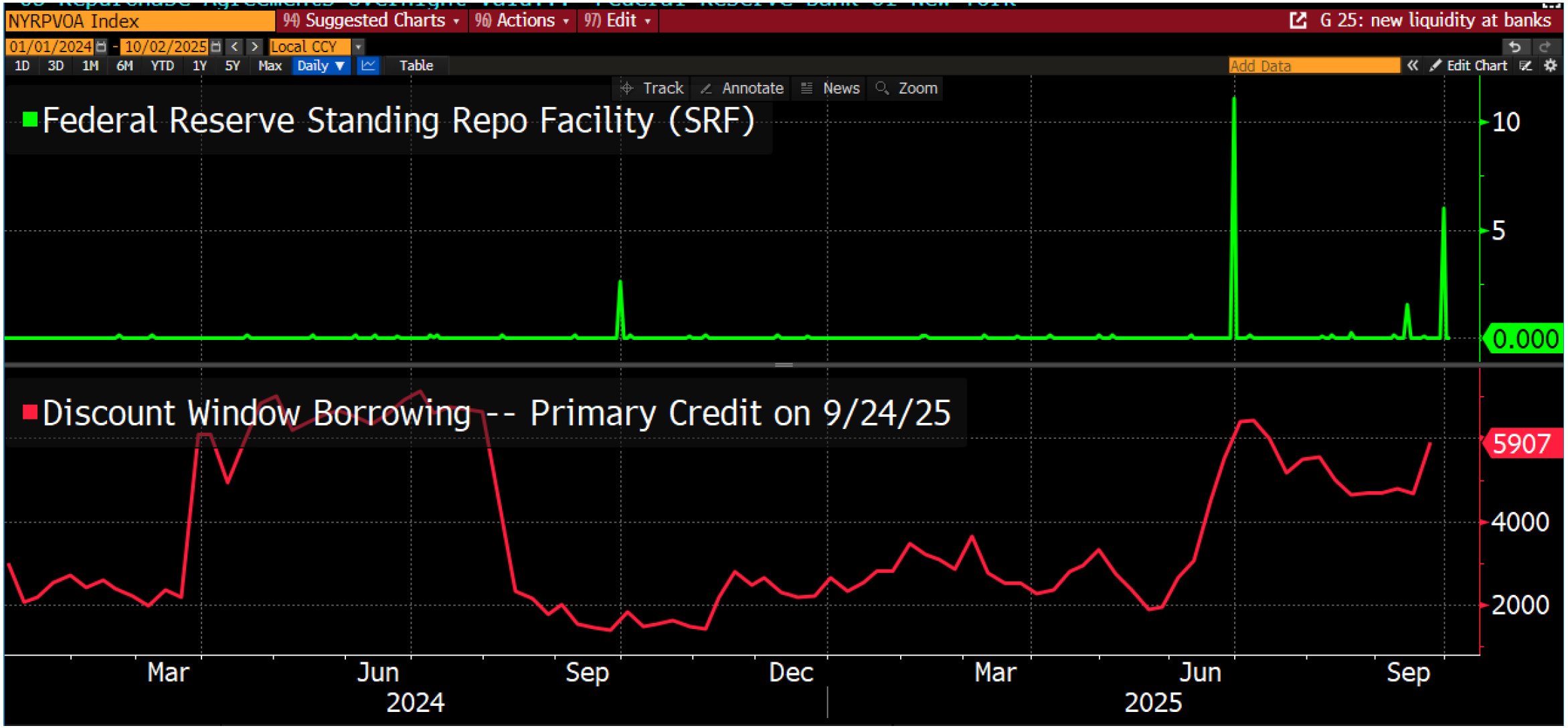
- Fed continuing to shrink its balance sheet. SOFR rose from 4.42% to 4.51% on 9/15, highest rate this year.
- On 9/15, SOFR rose 11 bps above IOER and 75th percentile SOFR trade was 11 bps above median.
- Shifts in the composition of Fed liabilities impact markets and US bank liquidity.
- US banking system liquidity ceasing to be ample in Q4 2025.
- Fed thinks minimal ample reserves $2.7 trillion. SVB failed at $3 trillion reserves – where we are as of last Friday. I believe that my Fed colleagues are too low on level of ample bank reserves (again).



Rate outlook impacts money fund balances in Fed's ON RRP, lower rates help bank liquidity while higher rate expectations reduce bank liquidity



Banks borrowing starting to borrow more from Fed

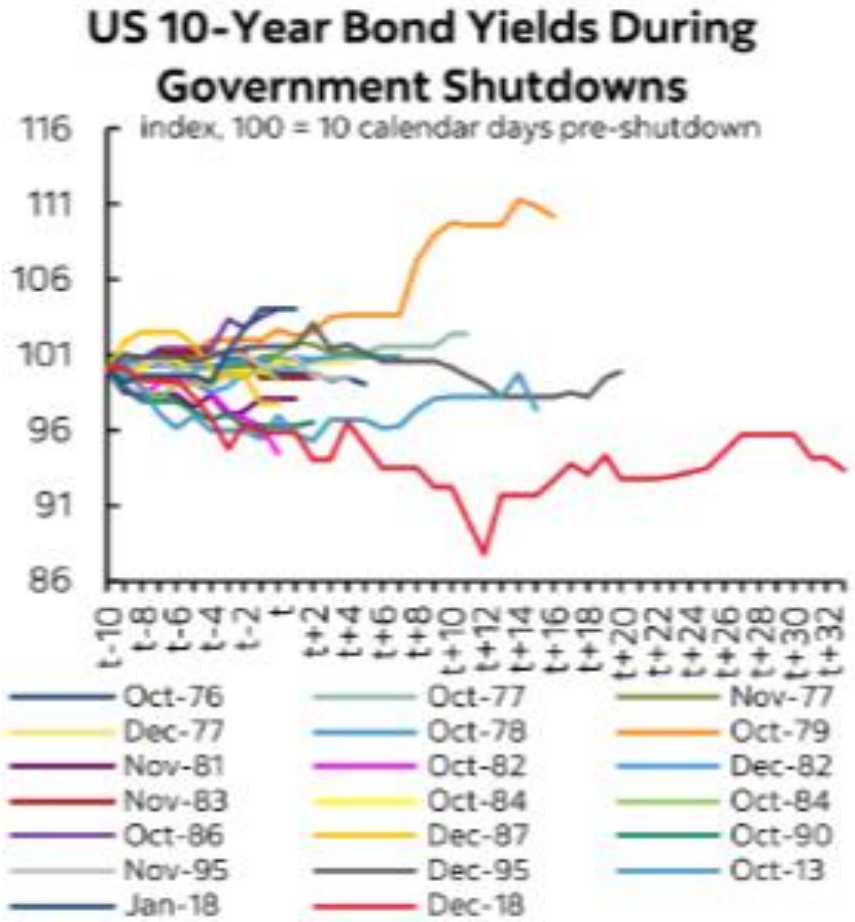


Alternative scenarios …

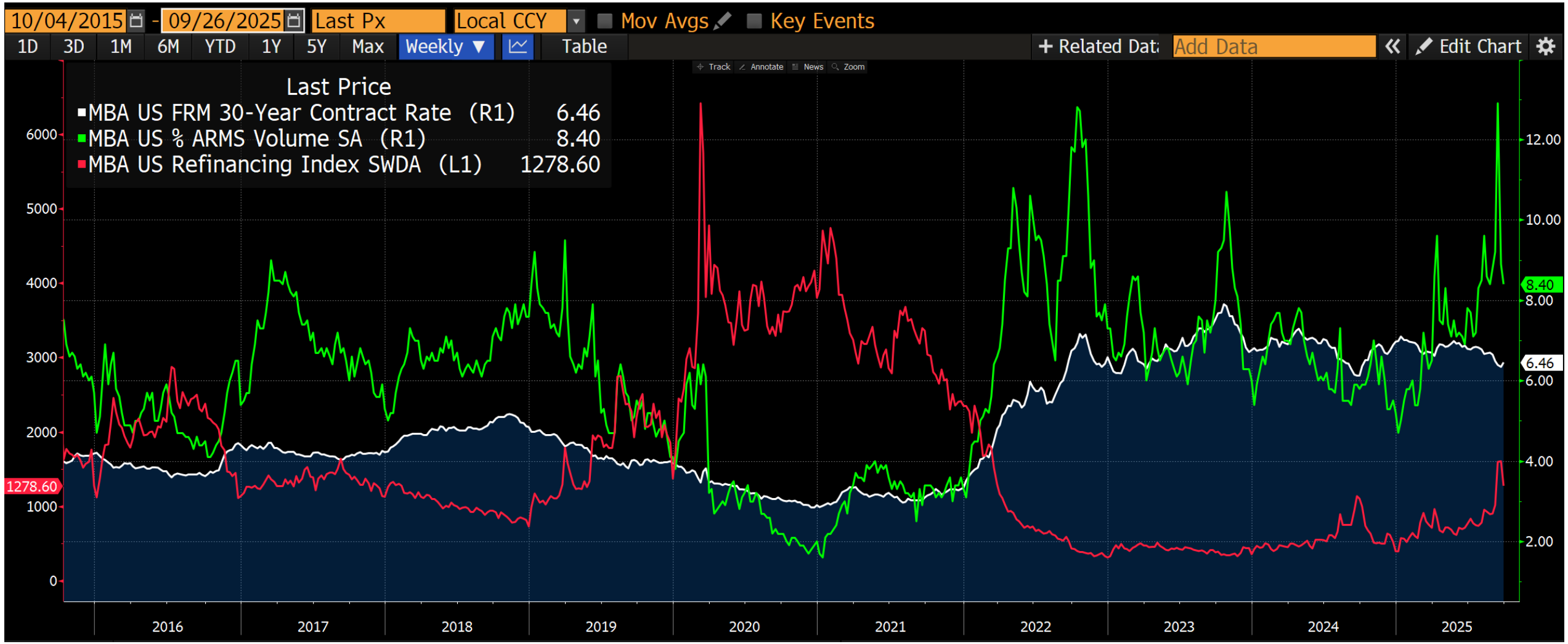
- Economy gets better
  - Government shutdown resolves quickly.
  - Household and business sentiment improves; algos trade WH tweets; US financial conditions continue to ease.
  - Less economic policy uncertainty and fiscal and monetary stimulus provides tailwind to US economy into 2026

- Economy gets worse
  - DOGE job losses to worsen labor market as severance packages end (effect could appear in Nov NFP)
  - There have been 20 government shutdowns since the 1970s. Most are short-lived, but a few have negatively impacted the US economy.
  - Further large shocks to confidence in US economic policy.
  - Administration replaces Fed leadership with perceived weak candidate.
  - QT causes US funding market disruption or bank stress.
  - Tariff war is prelude to real geopolitical conflict.

Uncertainty on 10-year Treasury yield significant now

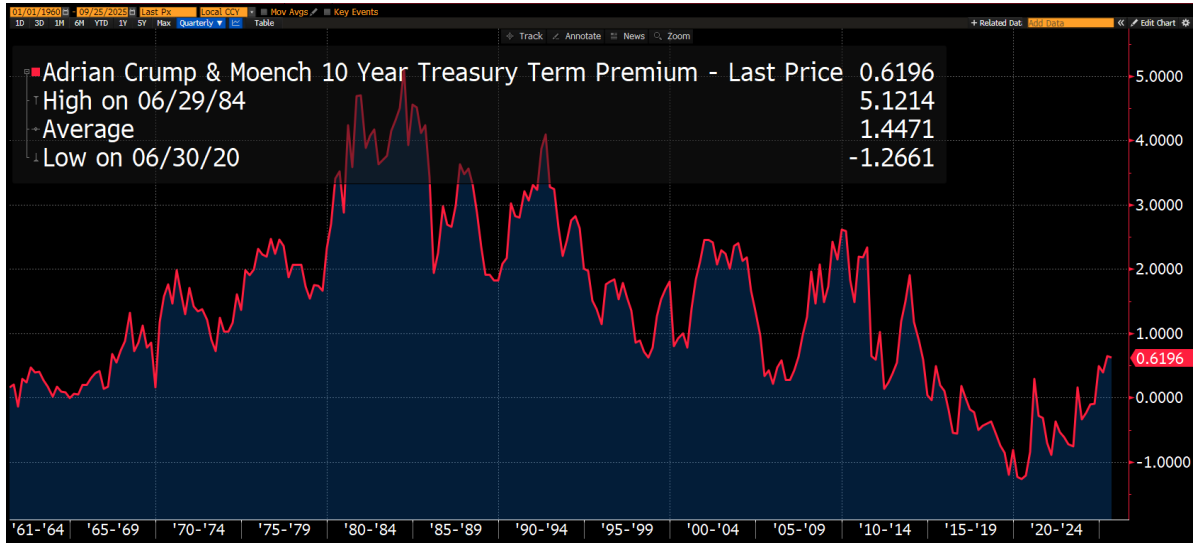


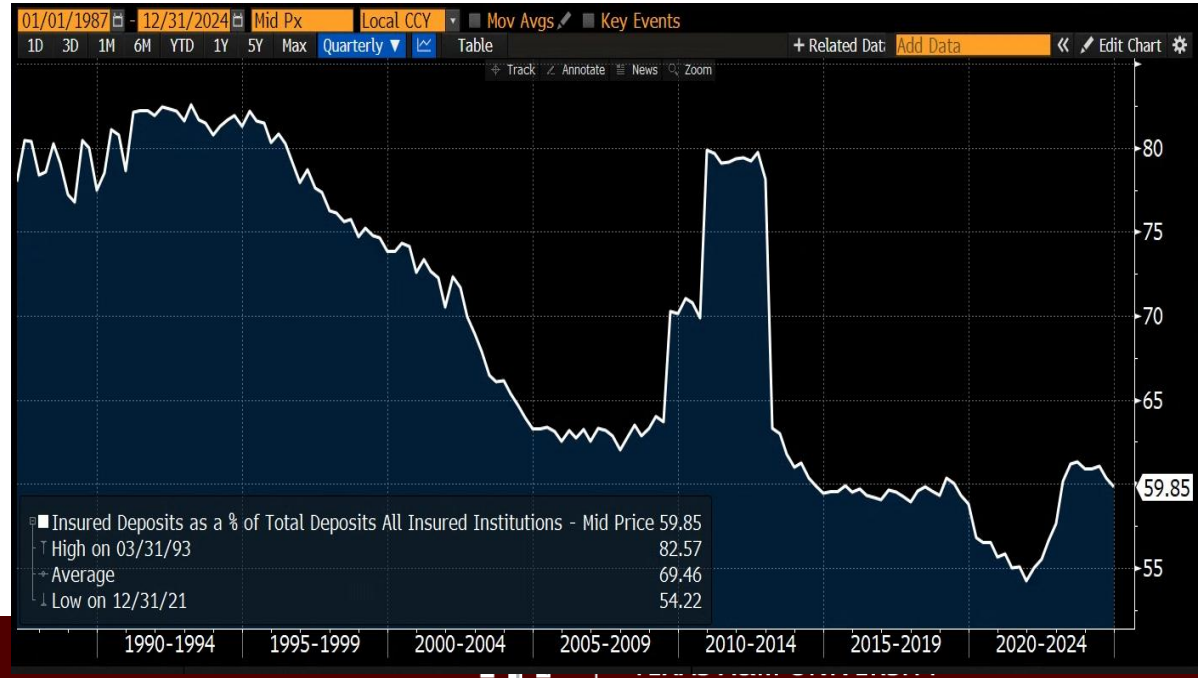
US housing finance channel congested



What does this mean for banks?

- 10-year US Treasury term premium (chart) has pivoted from long-run trend – beginning a structural rise.
- In the prior ultra-low rate environment, many US banks chased NII through higher duration and more rate volatility (agency MBS) and took EVE risk.
- **Lagged impacts of interest rate risk still a likely headwind for some banks.** Use of HTM really should be limited.
- Resist the temptation to go beyond a duration of 2-3.
- **Stablecoins** create new risks related to $6 trillion in uninsured non-interest bearing deposit funding.
- <u>Consider obtaining some term funding (2-3 years) and increase your cash buffer.</u>

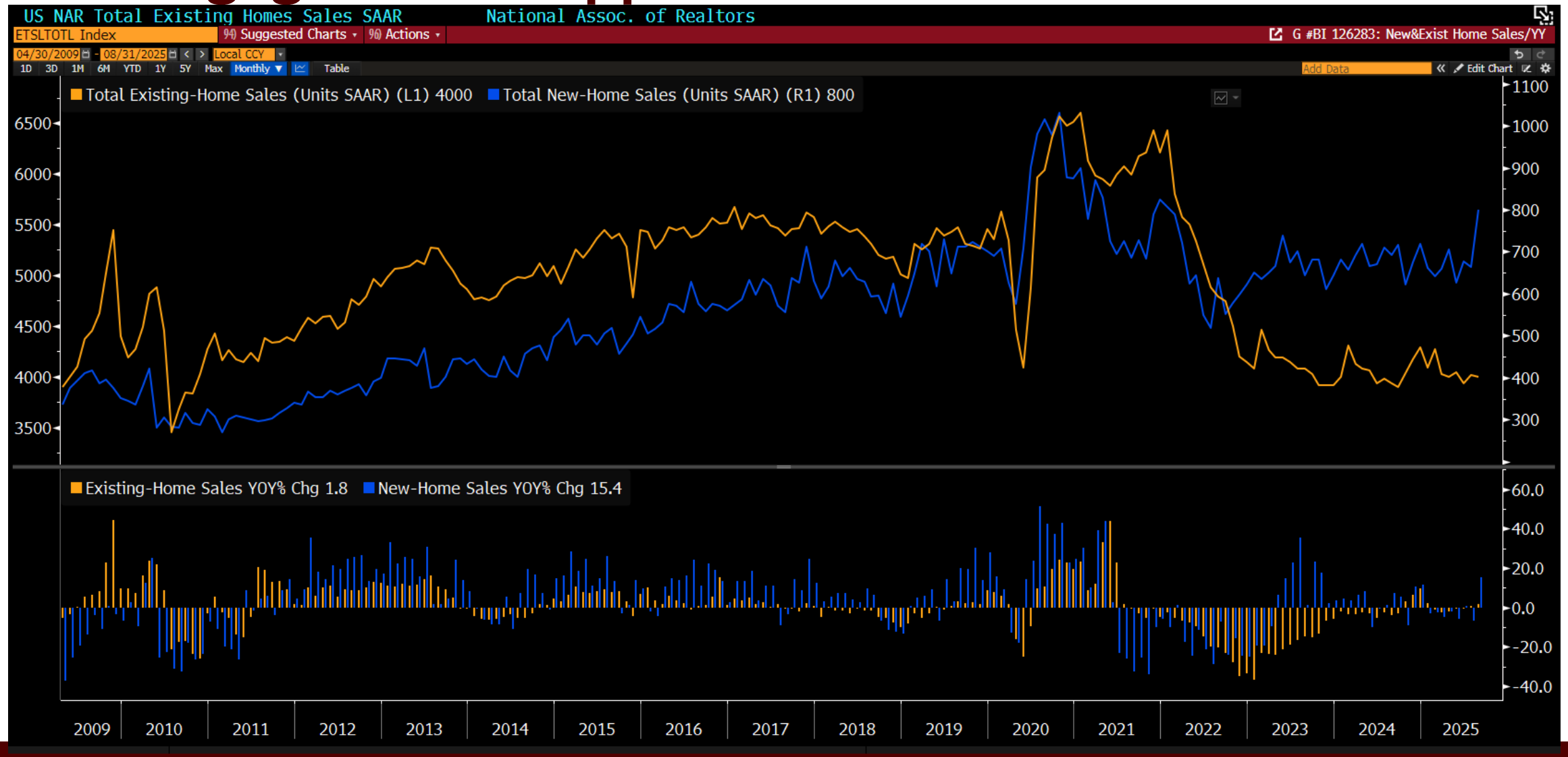




Aging demographics and baby bust hits five life cycle US housing drivers – diamonds, diapers, divorce, downsizing and death

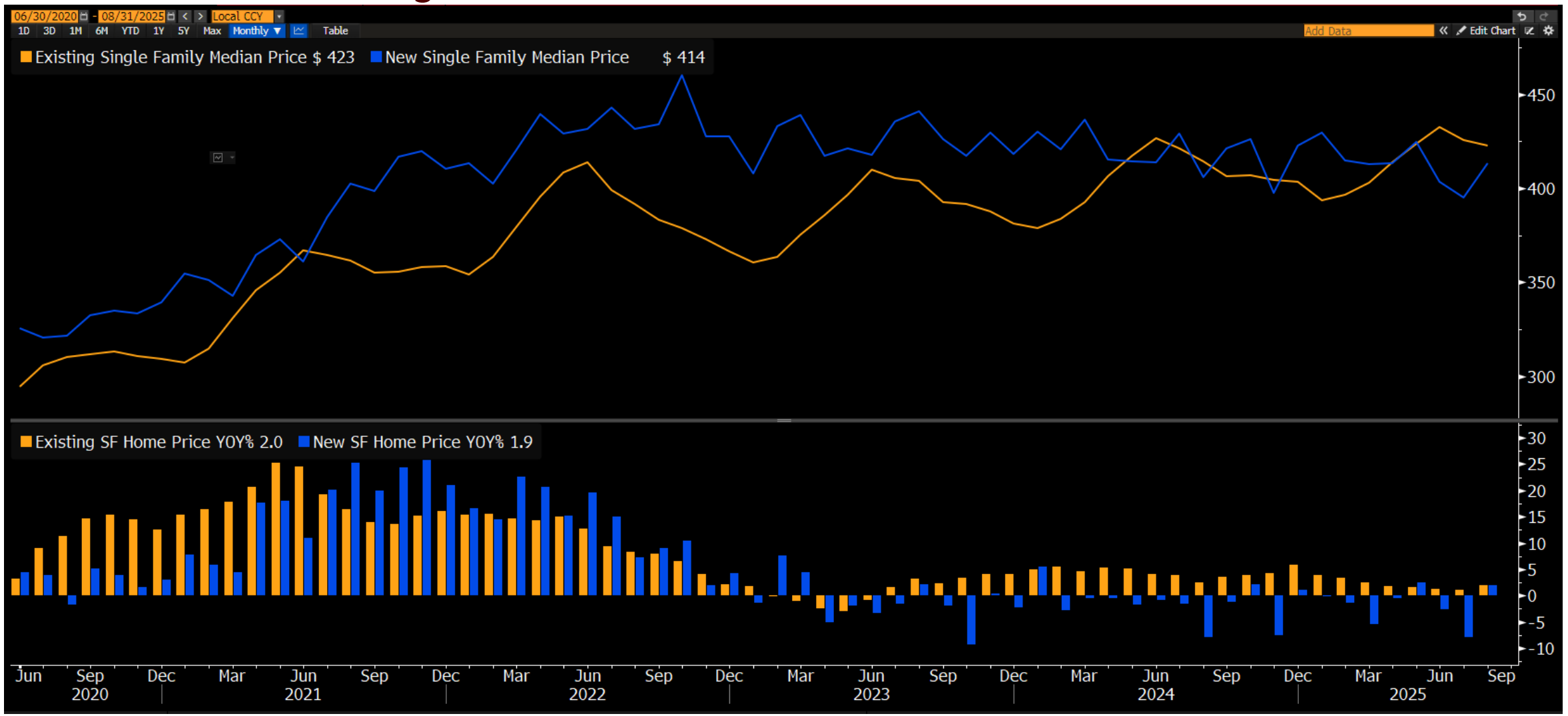
- Marriage rate is slightly up, but below 2008 levels.
- US birth rate hit new all time low in 2024 – 1.6 – now below replacement.
- Median first time US homebuyer now 40.
- Divorce rate down relative to pre-pandemic level.
- 54% US homes owned by seniors vs 44% in 2008
- Per Redfin, 78 percent of seniors do not want to downsize.
- High asset prices and ability to tap into home equity will keep a lid on housing inventory.
- HEL and IO HEL products keeping seniors in place despite rising ownership and insurance costs
  - In 2009 $71 B vs $18T in US home value
  - In 2025 $411 B vs $47T in US home value

Home resales could be slowest in 25 years; lower mortgage rates support new builds

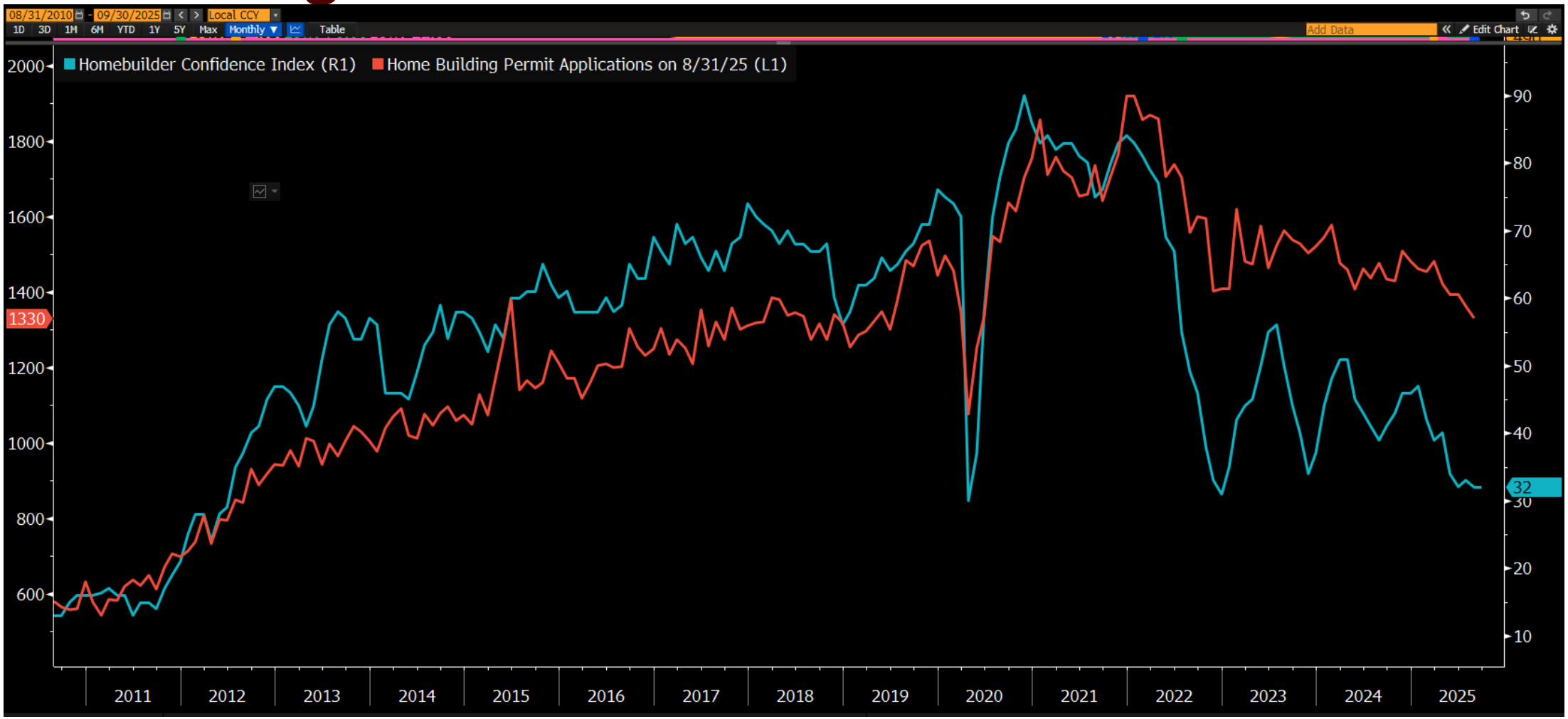


New homes share of US home sales elevated

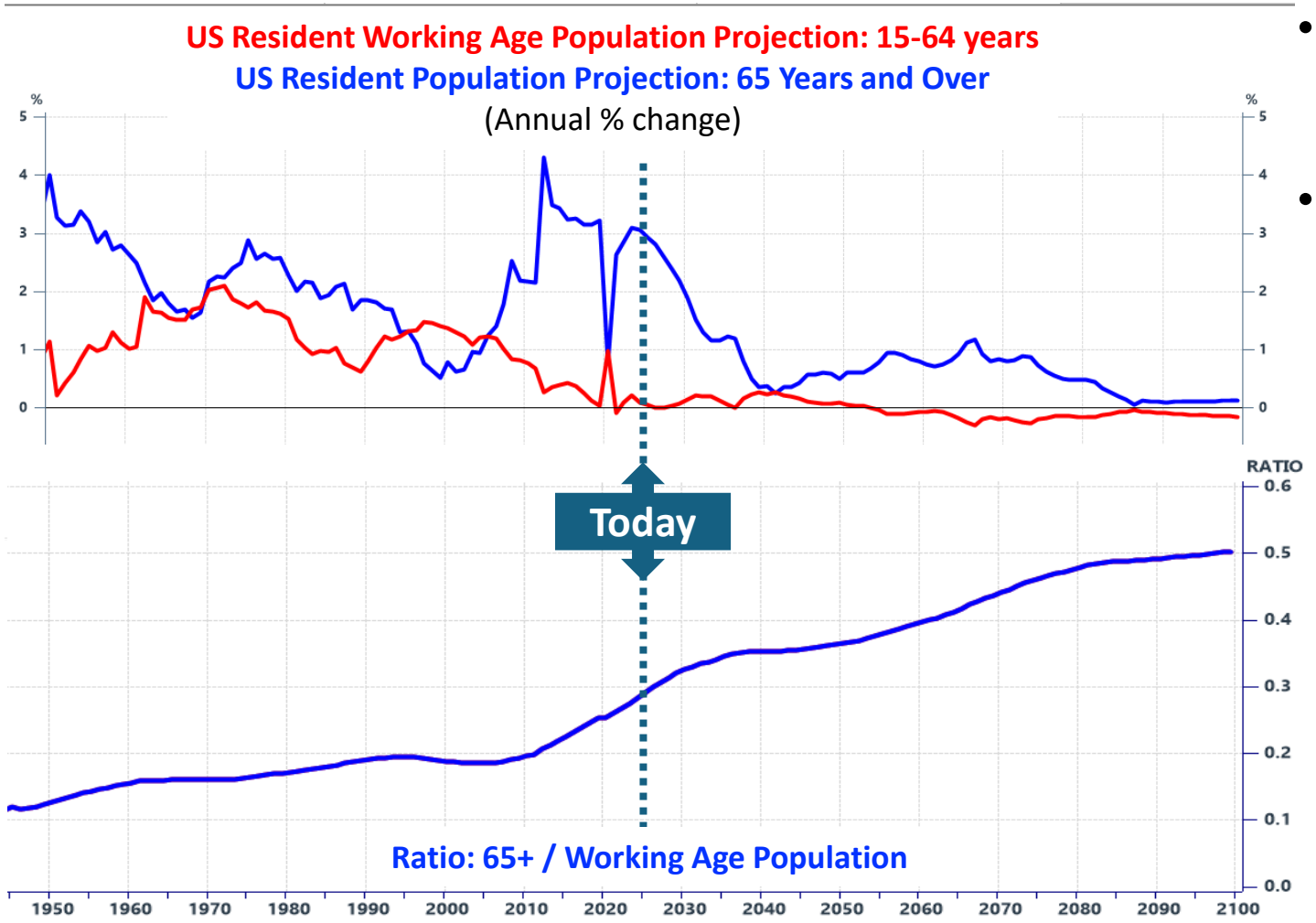
Builder discounts for new homes currently helping on affordability



But US homebuilder confidence low and permits declining



What is happening to housing in Japan? It is critical to stabilize US demographics



- Growth in empty homes in Japan, but housing still less affordable.
- Japan's experience so far shows widening of urban-rural divide:
  - Residential real estate prices in cities generally up, but prices in rural areas falling.
  - In rural areas, abandoned homes rising. By 2033, estimated ~30% of all homes in Japan could be vacant!
  - Properties in Japan's urban areas higher due to proximity to jobs plus rising land and material costs.
  - Urban home turnover is slow and high costs of new construction create need for redevelopment of existing homes.

Questions/discussion

Check out Certificate of Bank Treasury Risk Management program – you are welcome to a 30% discount (mention TDSML talk)

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Cetina's Bank Treasury Talk

We are delighted to introduce our new BTRM column by Jill Cetina, a highly respected expert in bank treasury risk management. With extensive experience in financial regulation and risk oversight, Jill brings deep insights into the evolving challenges faced by treasury professionals. Her column will explore key topics such as liquidity risk, balance sheet management, and regulatory developments, providing valuable analysis and practical perspectives. As the banking landscape continues to shift, Jill's expertise will help readers navigate complexities and stay ahead of industry trends. Stay tuned for her thought-provoking commentary and expert guidance in each edition.

Cetina #12: September 2025 – Markets prefer the blue pill, but watch out for an inflation revival and associated rate repricing; stablecoins a risk to bank deposits

Cetina #11: August 2025 – August 2025 – April evoked Ferris Bueller; will Q4 evoke Groundhog Day?

Cetina #10: July 2025 –Yes, it is hard to not watch the Apprentice summer episode involving the Fed Chair. But tighter liquidity, stagflation and impacts of fiscal dominance on long-dated yields are the three key forces banks need to monitor.