BEACON ECONOMICS

SANTA FE SPRINGS CHAMBER OF COMMERCE

Social Narratives, Economic Realities, and the Outlook for ’24

Focus on Los Angeles

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beaconecon.com

Narratives vs Reality

There was no risk of a "hard landing"

- Excess demand causes inflation, not recessions
- Higher rates offset by high liquidity, low private sector debt levels

Outlook for 24—more of the same

- Consumer demand still strong, Fiscal stimulus still a strong offset
- Fed likely to moderate stance, albeit not as much as the market thinks

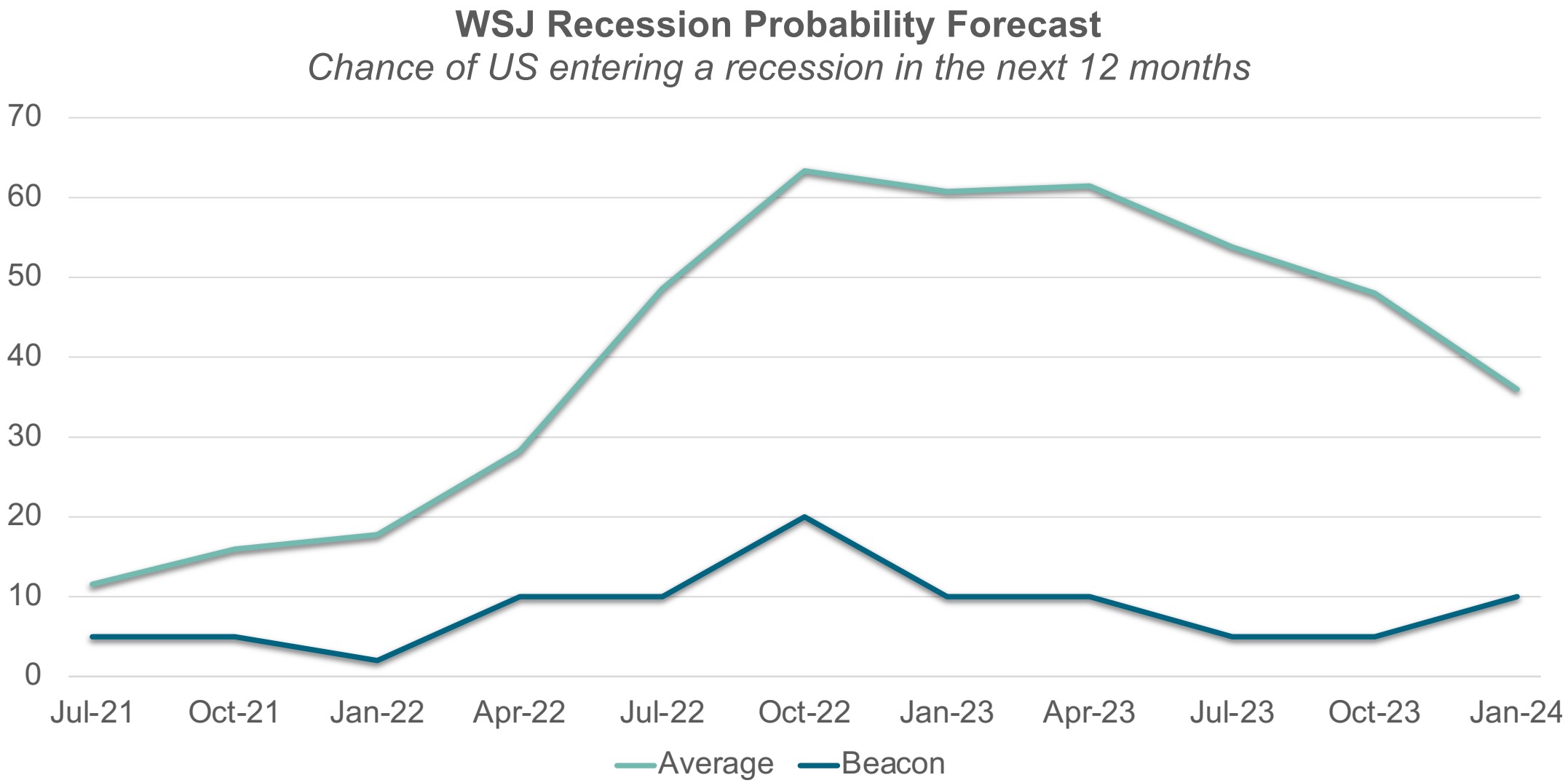
Economic reality checks

- Record federal deficits to keep long run rates high
- Asset prices remain frothily high
- Labor supply issues constrain overall US growth

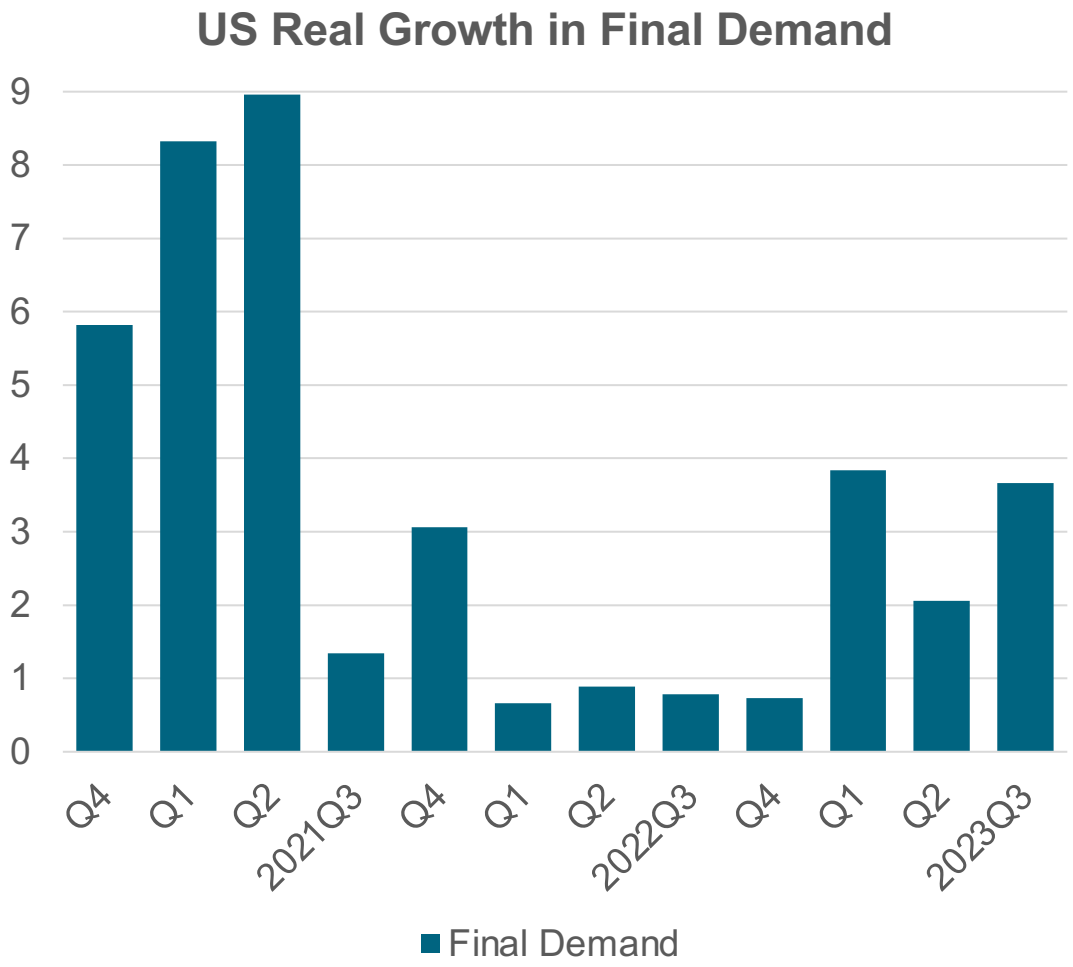
The problem is the narrative

- Record prosperity irrelevant to an angry public convinced of the opposite
- Political divide: inequality vs economic freedom
- Ugly election season will dominate headlines, economy is 2nd

Beacon's Outlook: No Recession



2023: A great year for growth

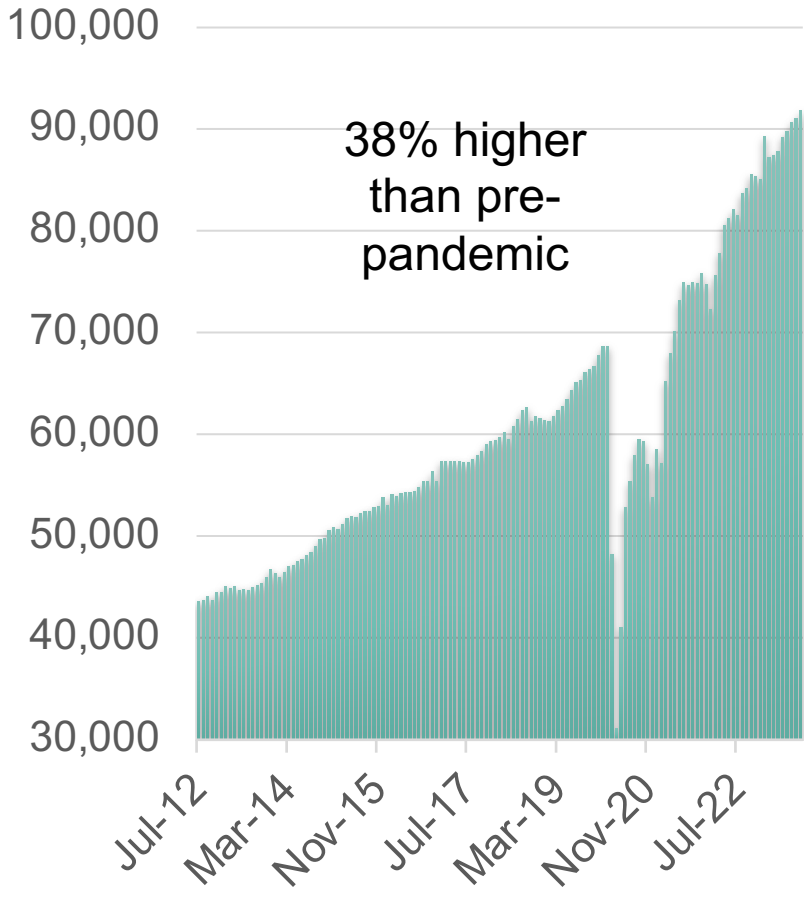


Annual Avg Contributions to Real Growth

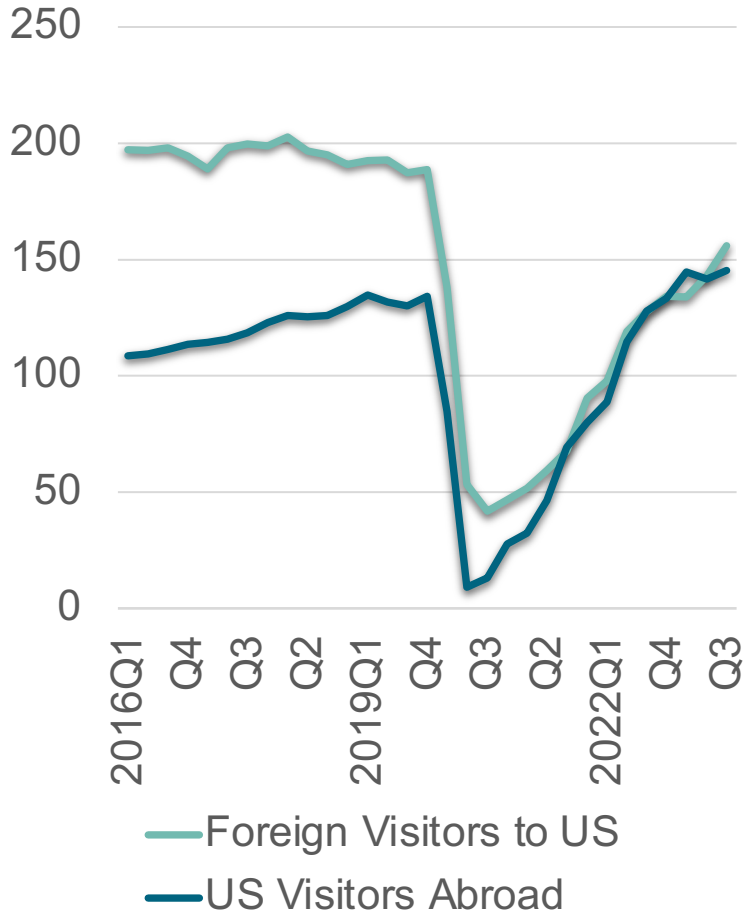
	2021	2022	2023
GDP	**5.43**	**0.68**	**3.07**
Final Demand	**5.42**	**0.77**	**3.19**
Personal consumption	**4.76**	**0.78**	**1.93**
Goods	1.48	-0.15	0.78
Services	3.28	0.93	1.15
Fixed investment	**0.69**	**-0.15**	**0.53**
Structures	-0.03	0.03	0.43
Equipment	0.10	0.26	-0.01
IPP	0.60	0.43	0.16
Residential	0.02	-0.87	-0.05
Net exports	-0.82	0.20	0.18
Exports	0.71	0.52	0.12
Imports	-1.53	-0.32	0.07
Government	**-0.02**	**0.13**	**0.73**
Federal	0.05	-0.02	0.26
State and local	-0.06	0.15	0.46

Americans: Partying!

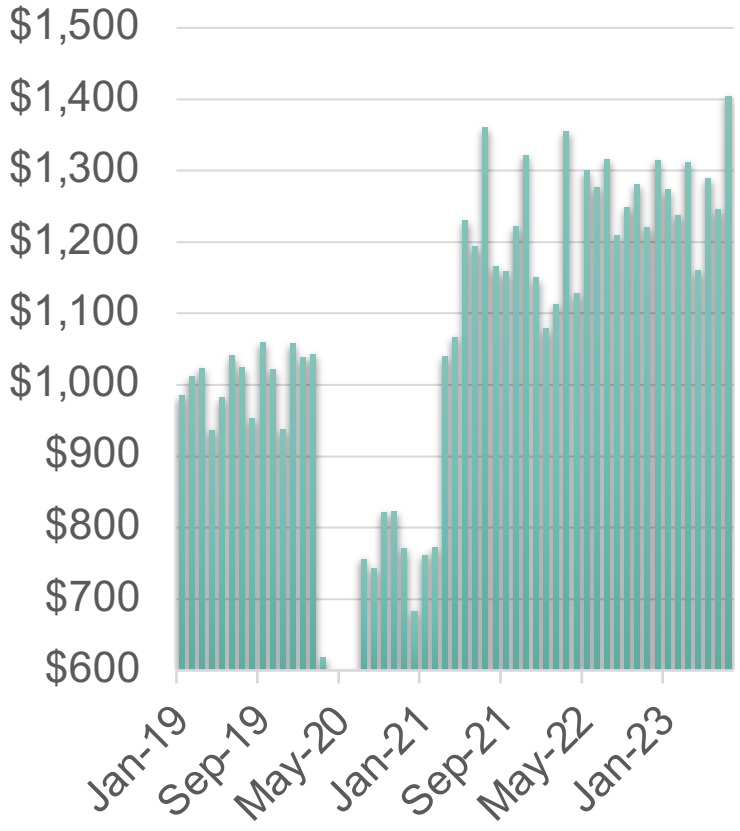
Retail: Restaurant and Bars



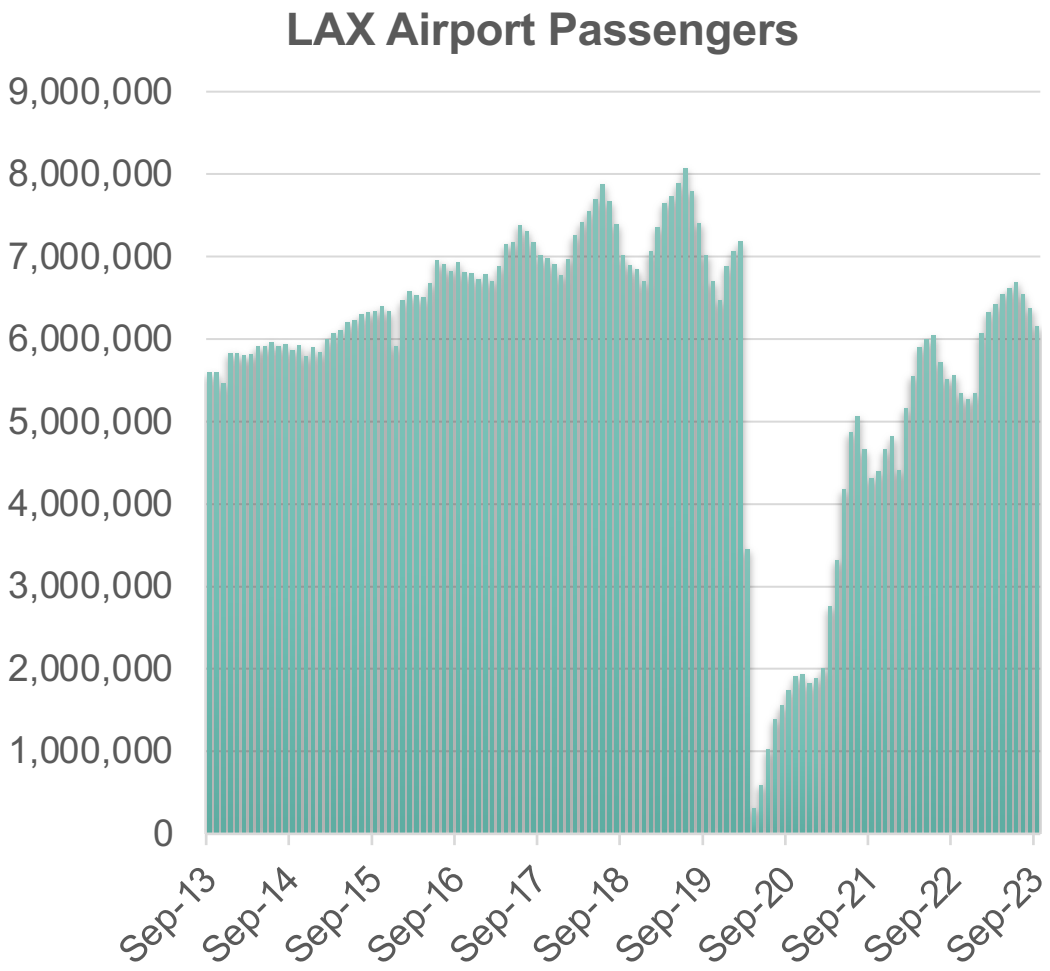
Real Spending on Travel

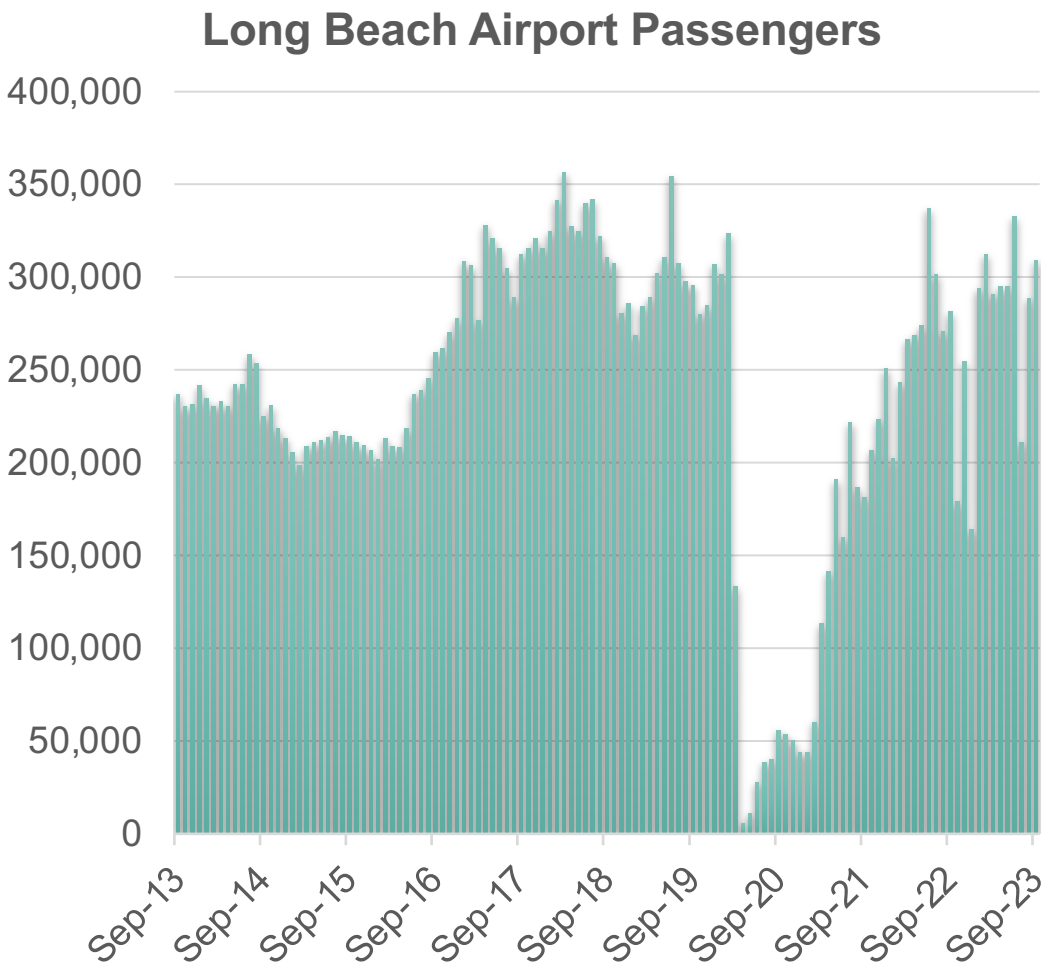


Nevada Gaming Revenues

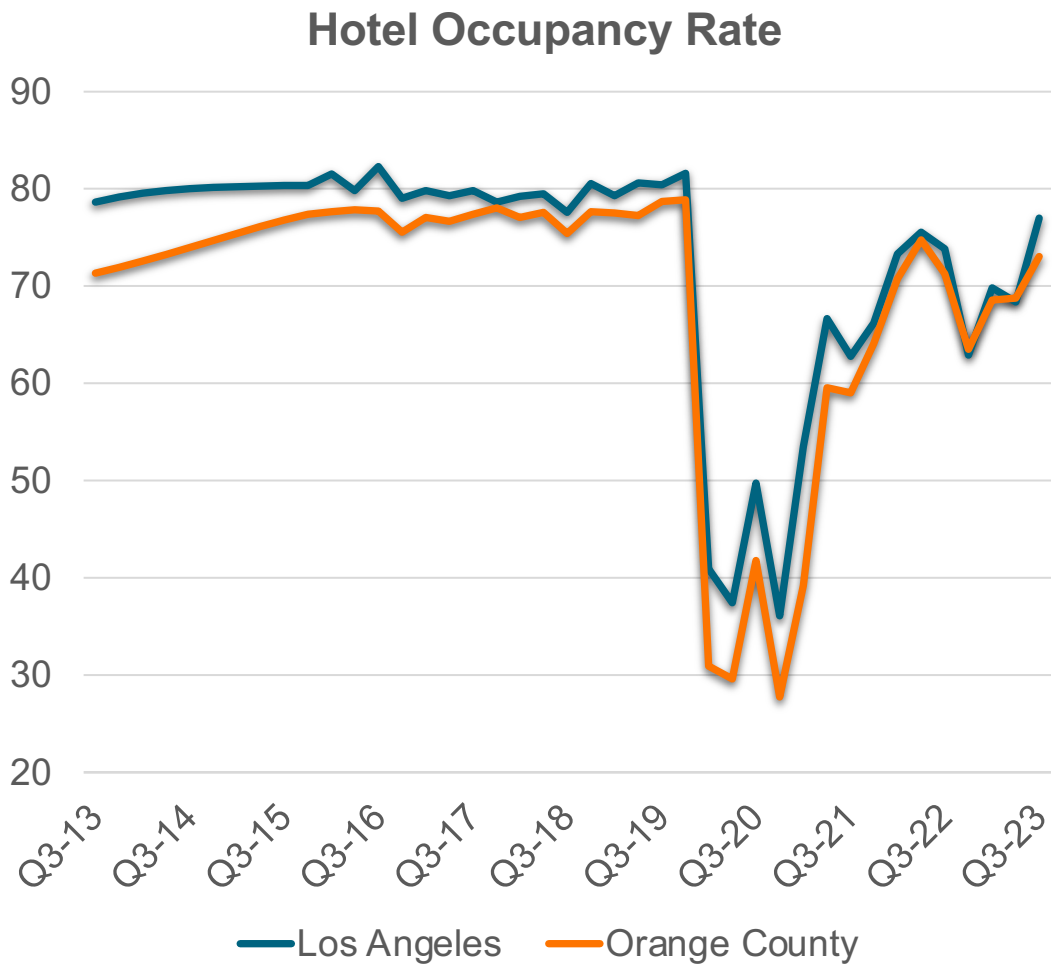


Airports


LAX Airport Passengers
9,000,000
8,000,000
7,000,000
6,000,000
5,000,000
4,000,000
3,000,000
2,000,000
1,000,000
0
Sep-13
Sep-14
Sep-15
Sep-16
Sep-17
Sep-18
Sep-19
Sep-20
Sep-21
Sep-22
Sep-23

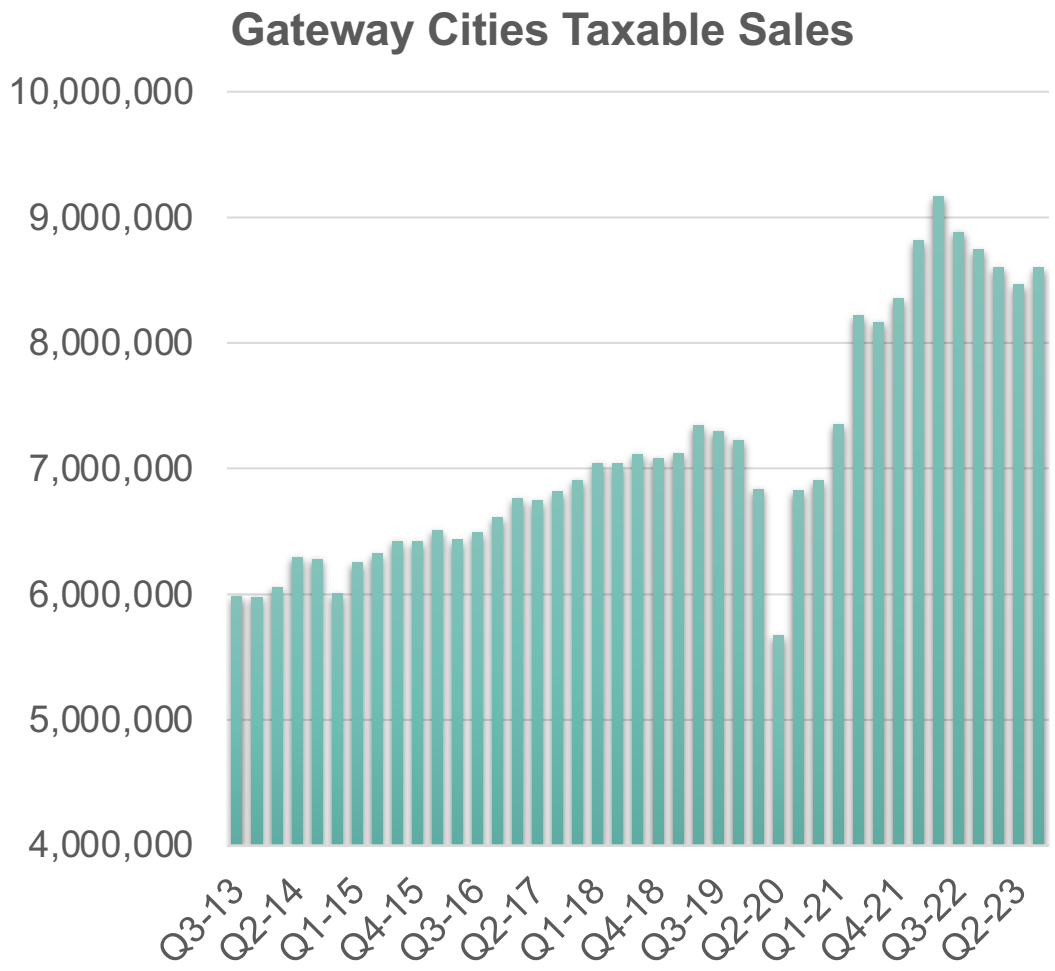

Long Beach Airport Passengers
400,000
350,000
300,000
250,000
200,000
150,000
100,000
50,000
0
Sep-13
Sep-14
Sep-15
Sep-16
Sep-17
Sep-18
Sep-19
Sep-20
Sep-21
Sep-22
Sep-23

Hotels



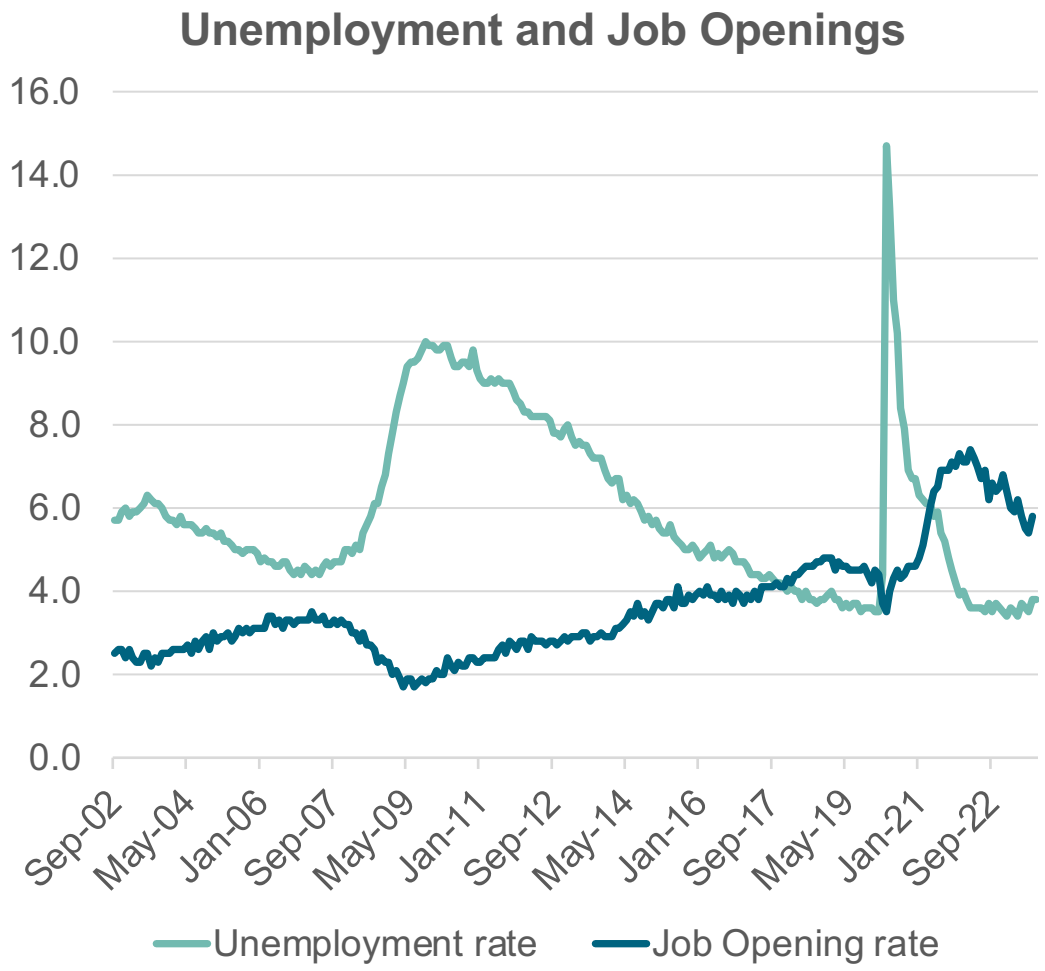
Location	Q3-23 ($)	1-Year Chg. (%)	Chg. Since Q4-19 (%)
Average Daily Rate			
Inland Empire	127.99	1.3	19.2
Los Angeles	186.53	-1.2	16.4
Orange County	181.31	-2.2	31.4
San Diego	190.43	-6.9	30.1
RevPAR			
Inland Empire	87.87	-3.4	11.1
Los Angeles	143.67	3.1	9.8
Orange County	132.46	0.3	21.7
San Diego	145.11	-7.4	30.3

Gateway Cities Taxable Sales

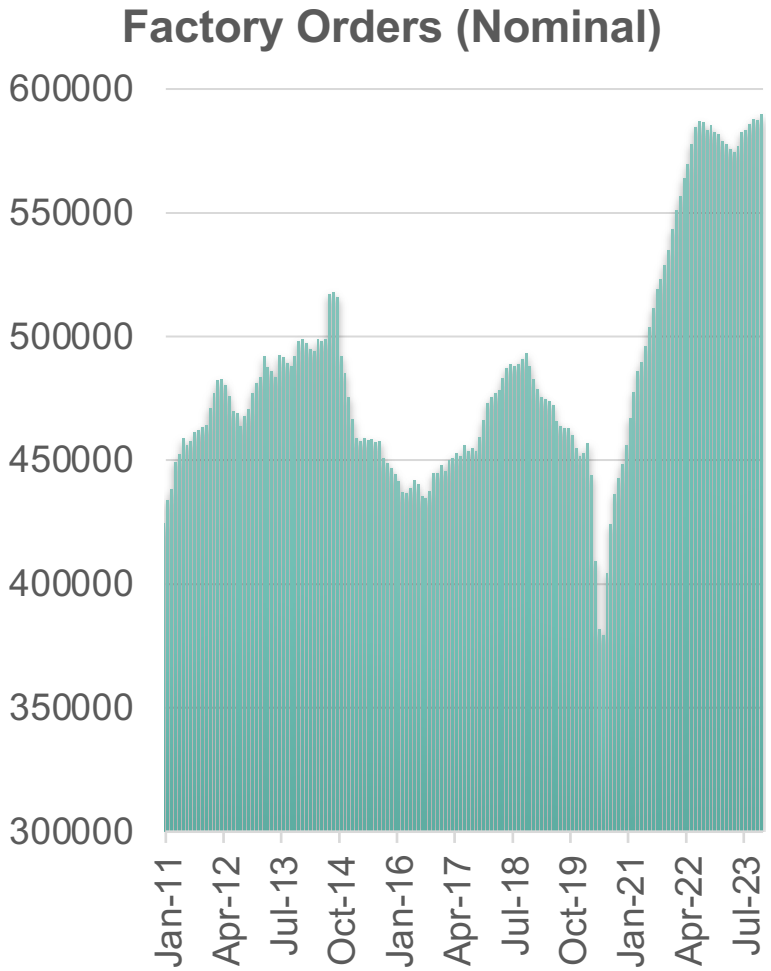


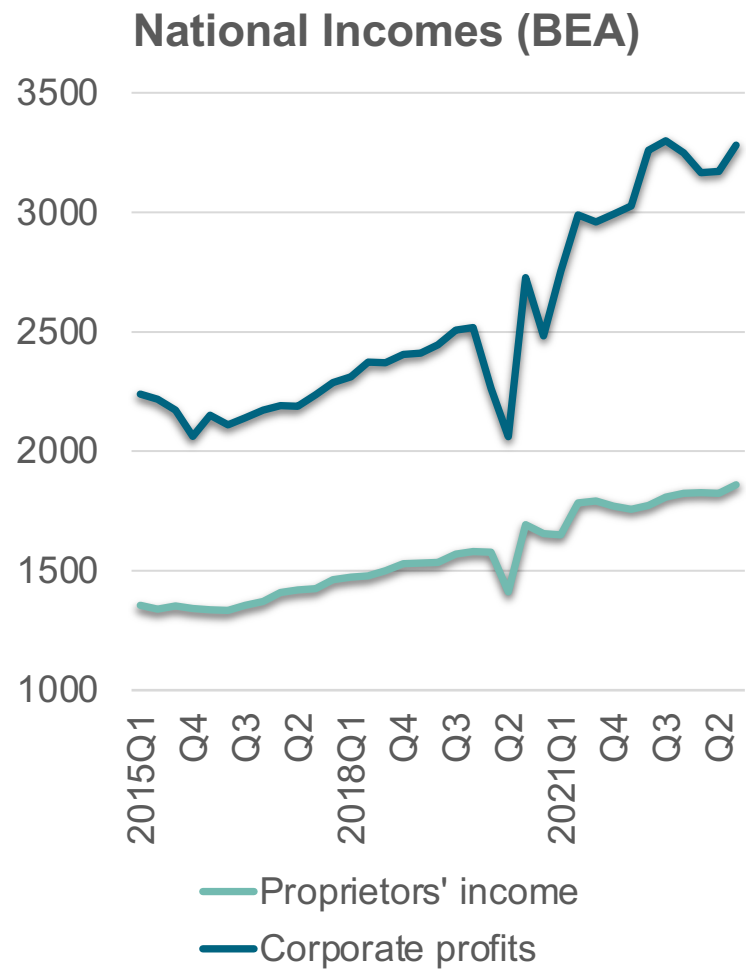
Top Gateway Cities	Q3-23 ($ 000s)	1-Year Chg. (%)	Chg. Since Q4-19 (%)
Long Beach	1,717,723	-1.7	15.3
Cerritos	919,514	-5.0	21.3
Santa Fe Springs	841,332	-1.5	36.9
Downey	540,204	-1.4	9.8
Signal Hill	489,149	5.7	15.2
Commerce	486,985	-13.8	2.3
Lakewood	340,224	-2.8	10.4
Whittier	329,954	-11.6	47.5
Montebello	314,470	3.4	18.5
Norwalk	312,066	-3.6	18.1

Labor Markets Remain Tight, Wages Up



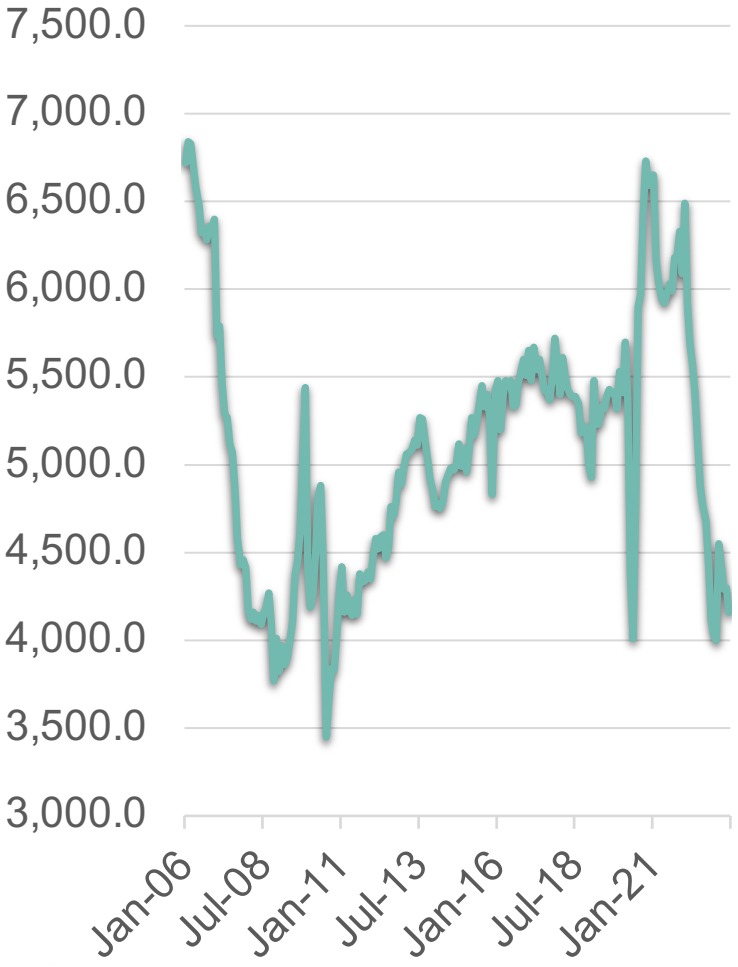
Production Up



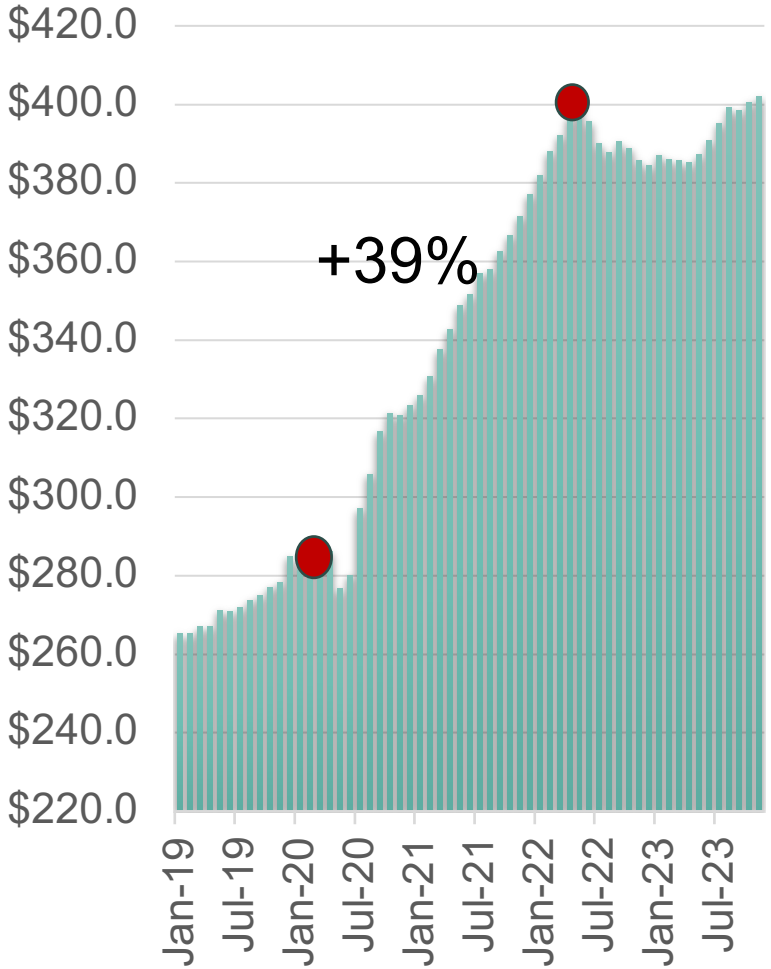


Housing: Sales down, yet prices, starts rising…

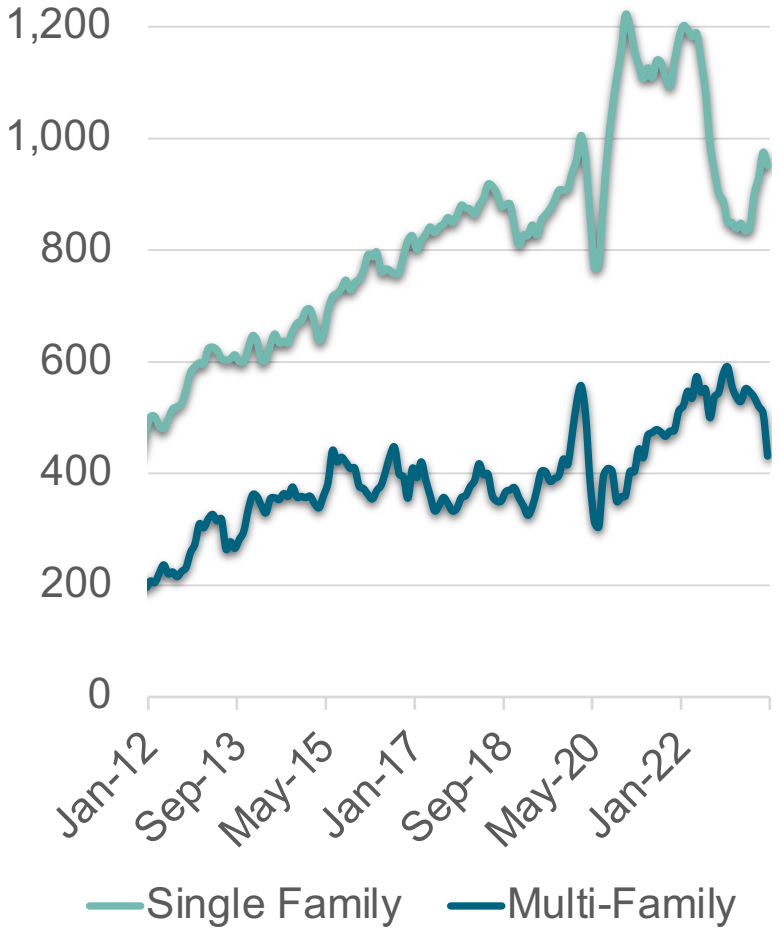
US Existing Home Sales



US Median Home Prices

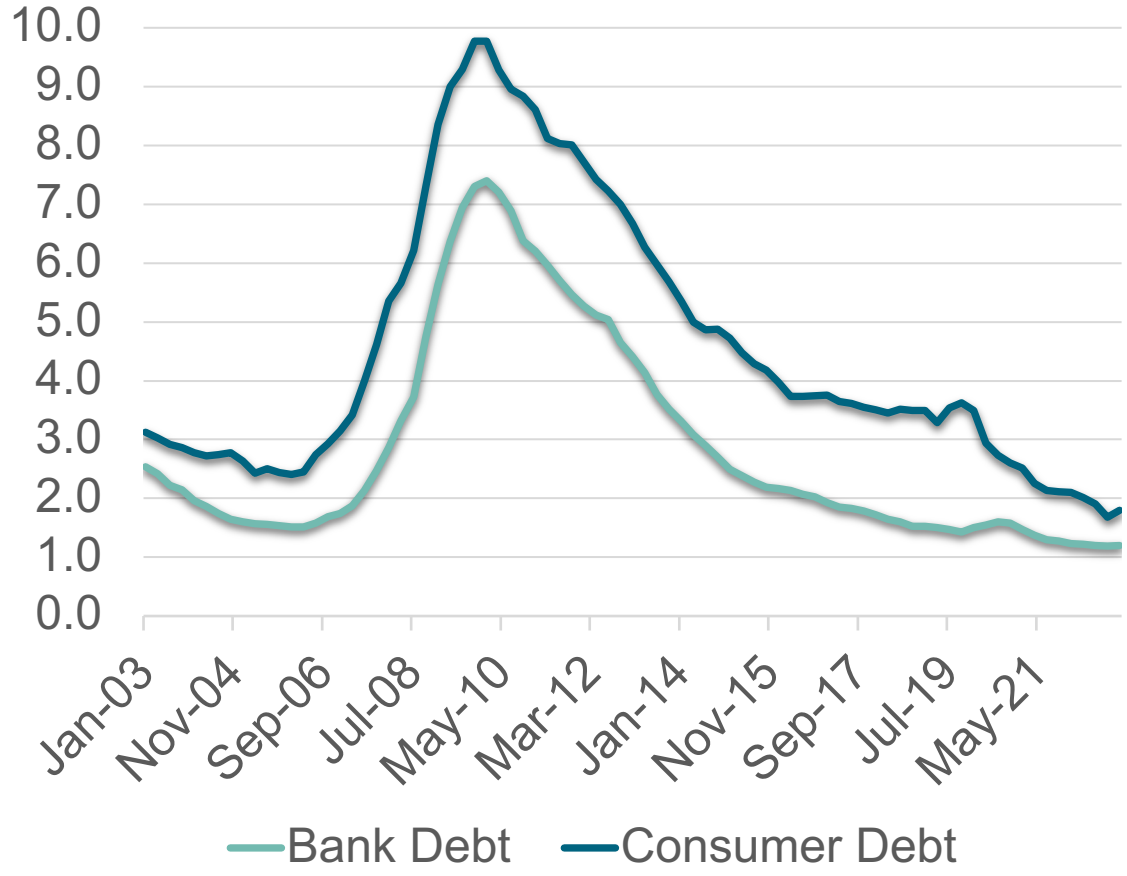


Housing Starts SAAR

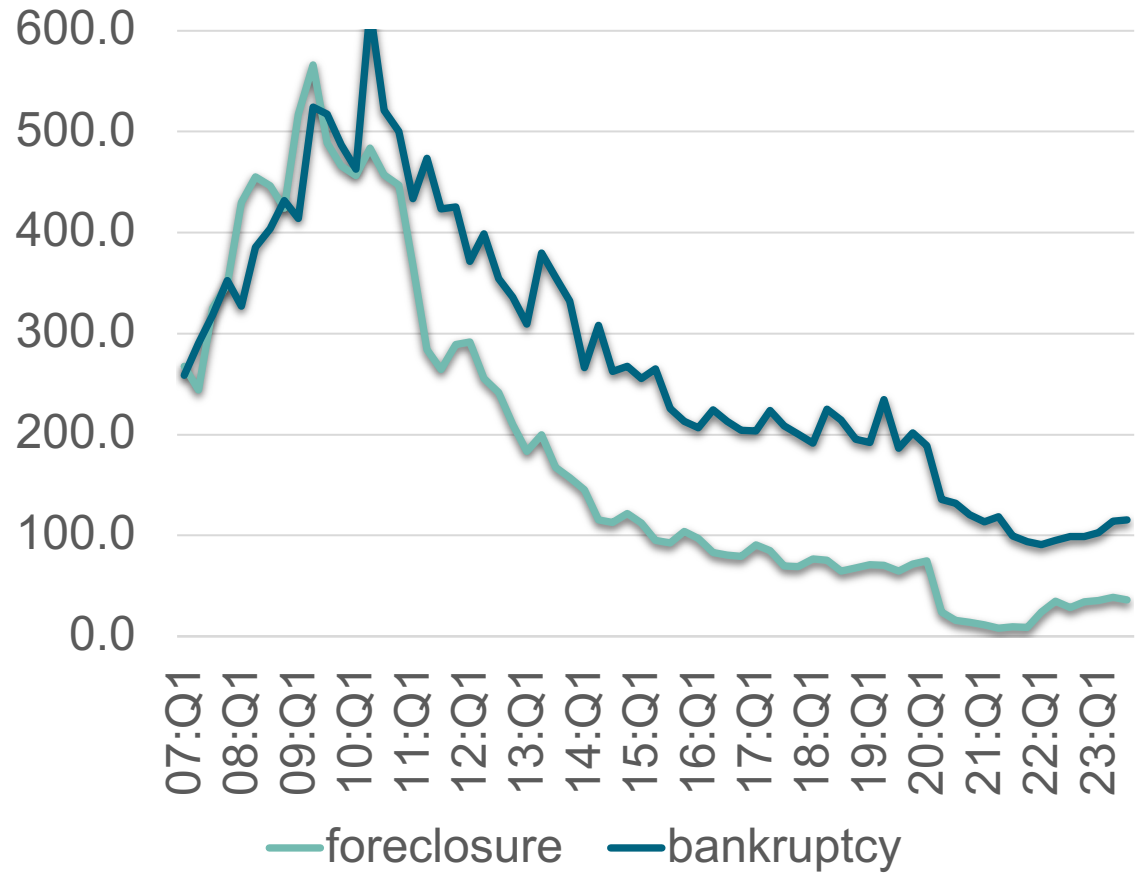


Credit markets clean

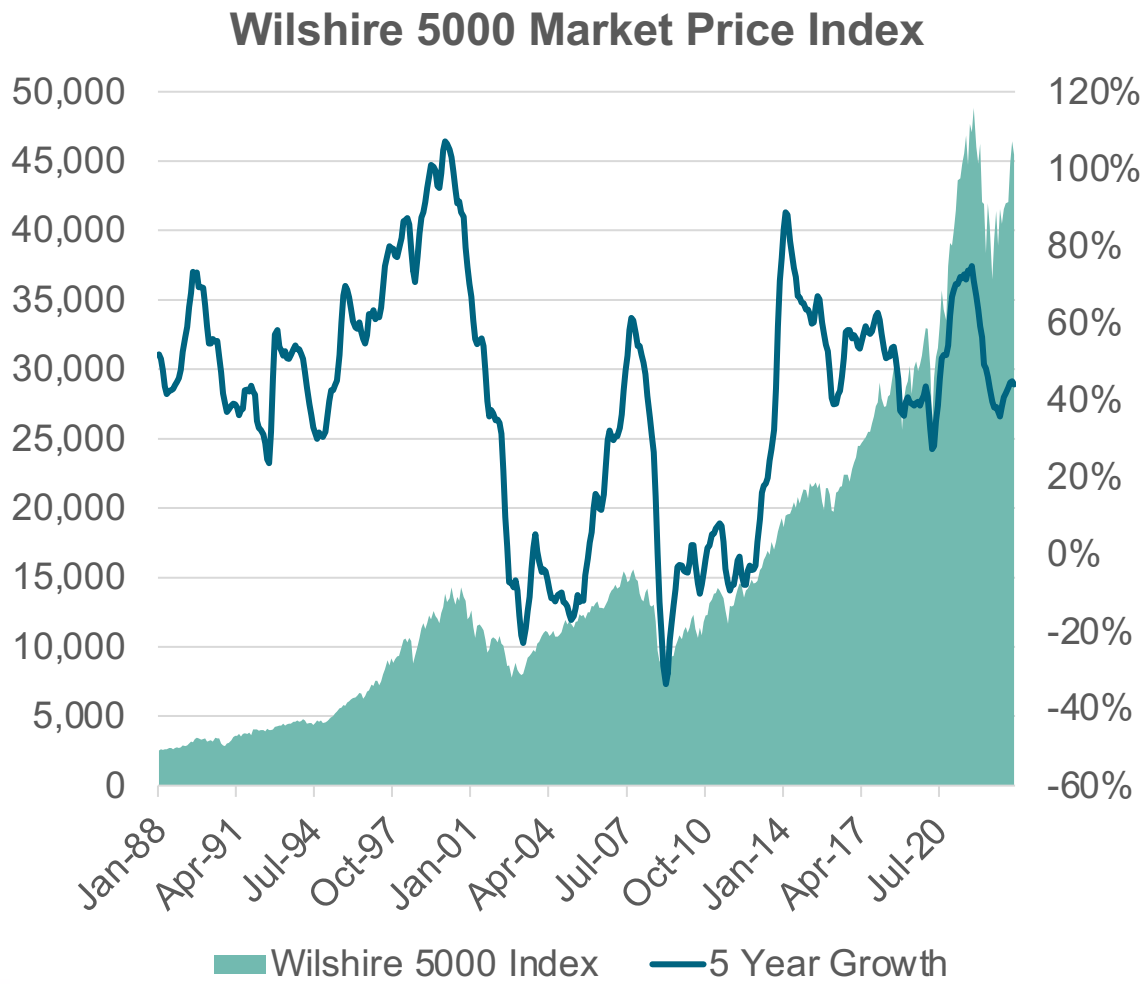
Loan Delinquencies (Share of Total Debt)

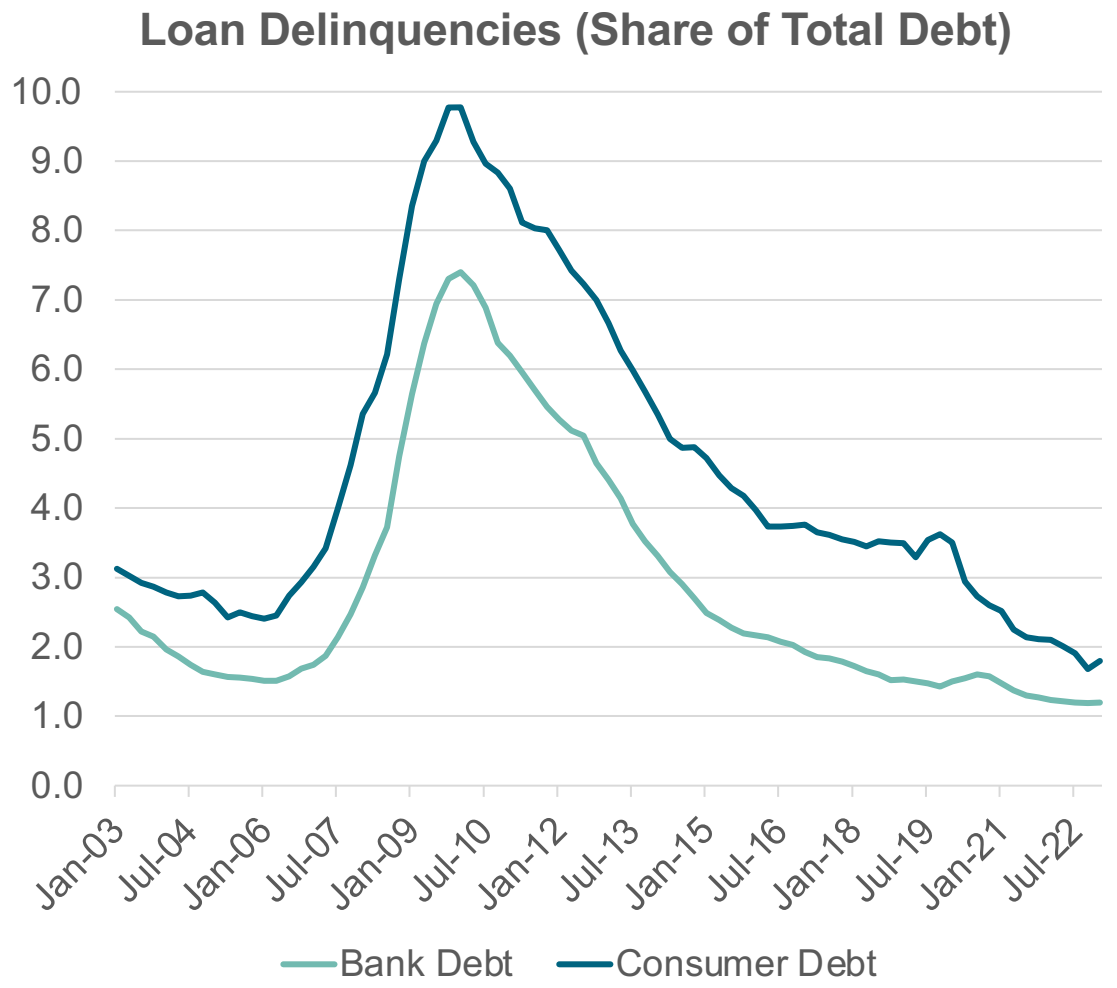


Household Distress (thousands / Quarter)



Stock market still bullish, credit markets clean



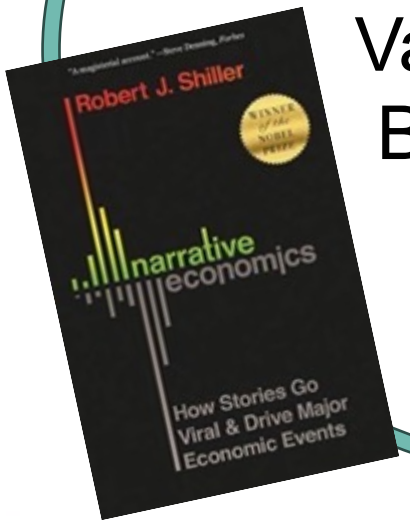


Beware the Narrative!

Social Narratives

Economic Reality

The Positive Value of Bitcoin



Ticketmaster fees are too high

The Unsustainable Federal Deficit

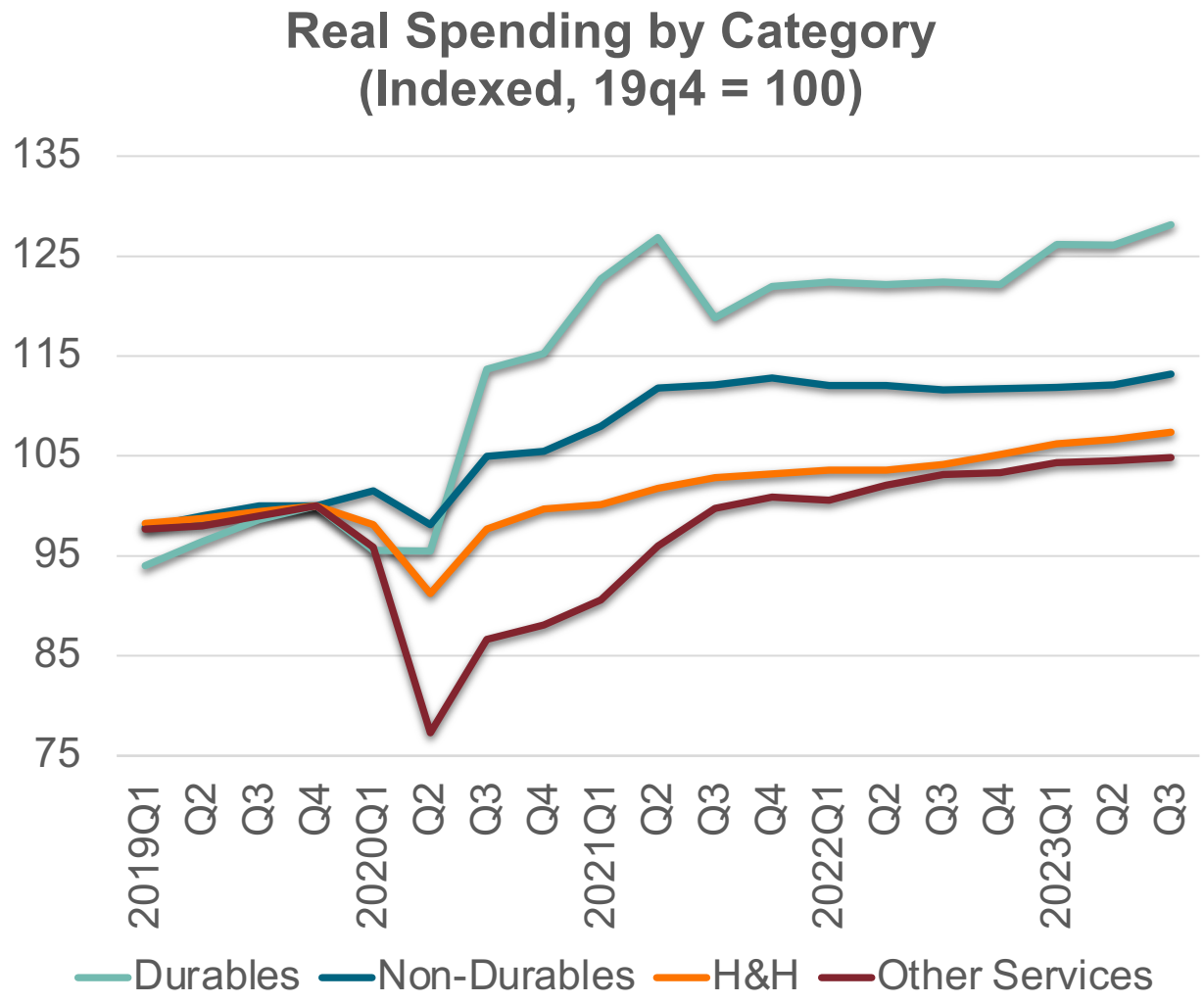
- ✓Narratives skewing interpretations of economic news
- ✓Narratives at the root of economic bubbles
- ✓Narratives driving bad policy choices

> “We need to incorporate the contagion of narratives into economic theory. Otherwise, we remain blind to a very real … mechanism for economic change..”
>
> —R. Shiller, *Narrative Economics*

Why did we have inflation?

- Pandemic Related Actual Lost Income: $1.2 Trillion
- Fiscal Stimulus: $6 Trillion, 5 to 1 stimulus to loss ratio, $50,000 per HH
- Deficit funded by $5 trillion in QE, causing a 40% surge in M2
- Asset price surge added $30 trillion more to household net worth ($240,000 / HH)
- Money + Demand = Inflation

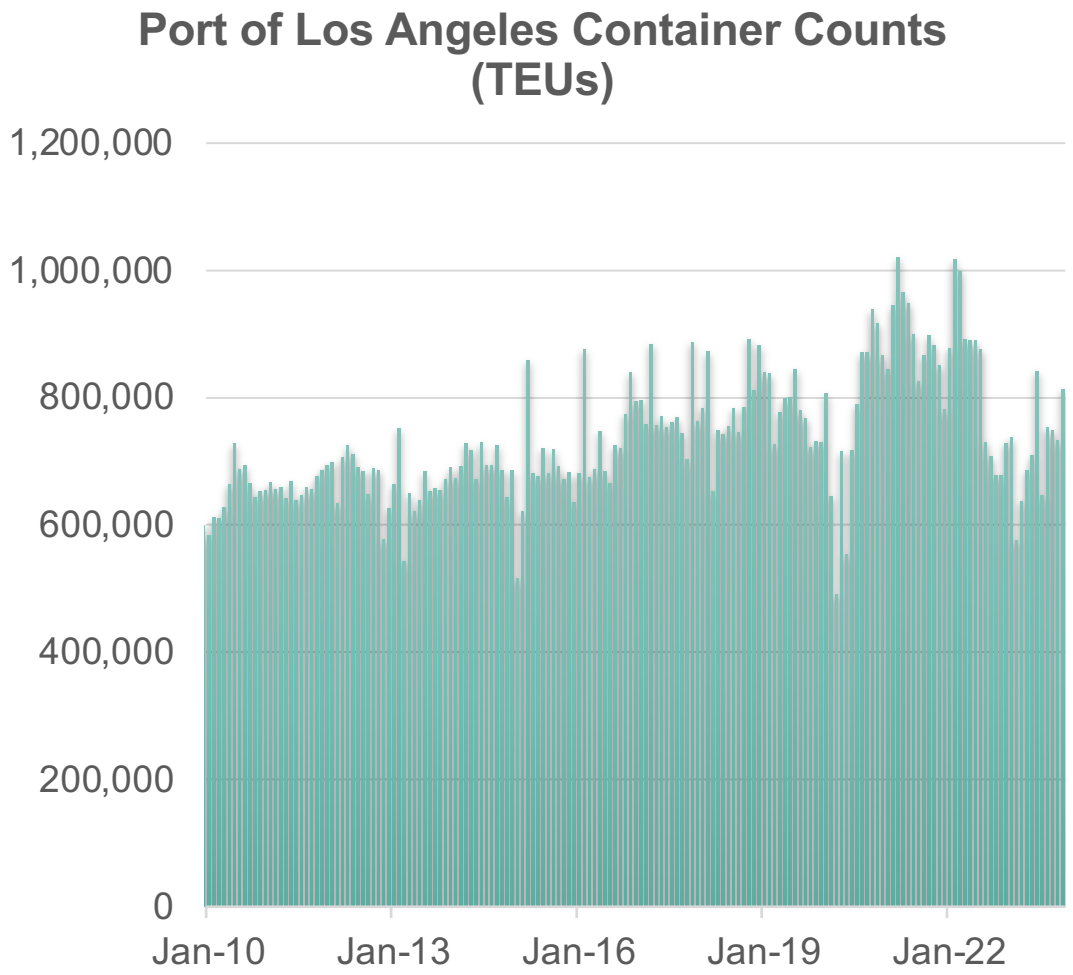
The consumer boom

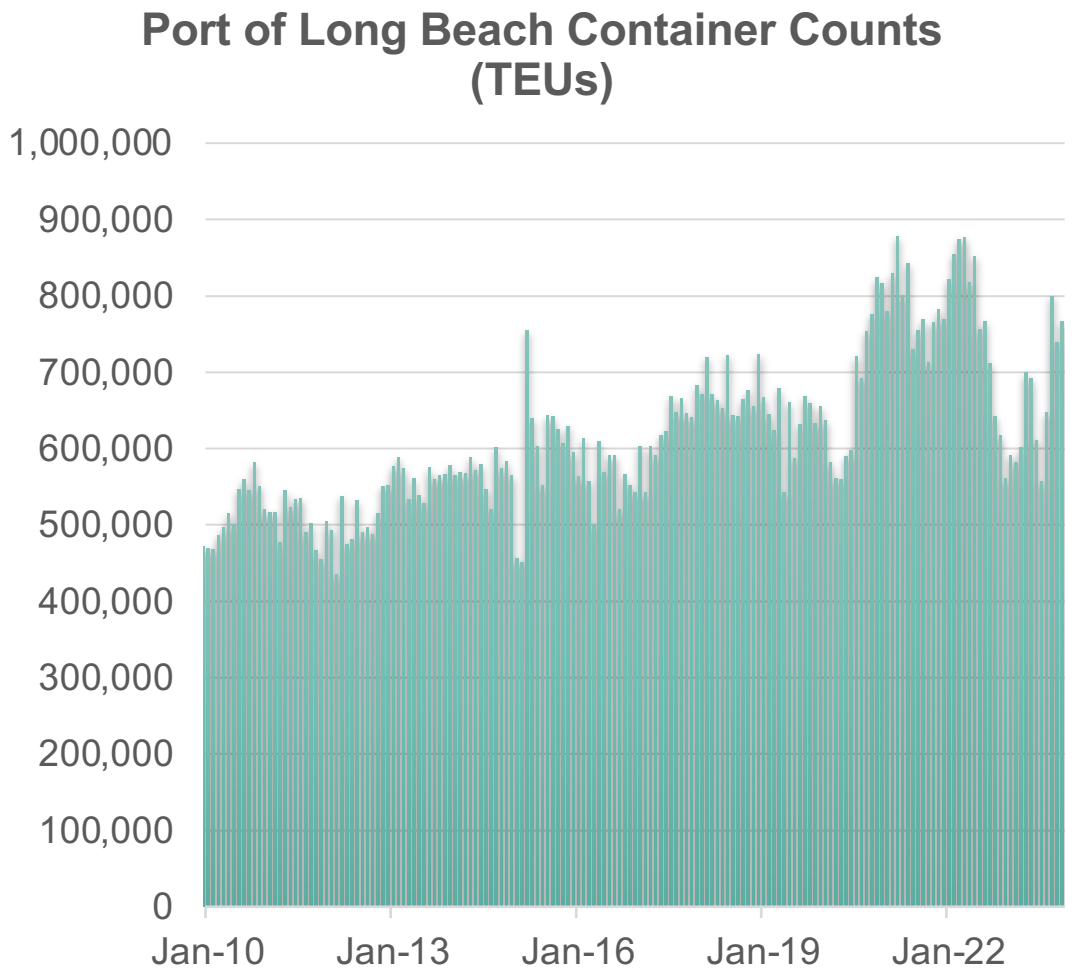


Nominal Retail Sales

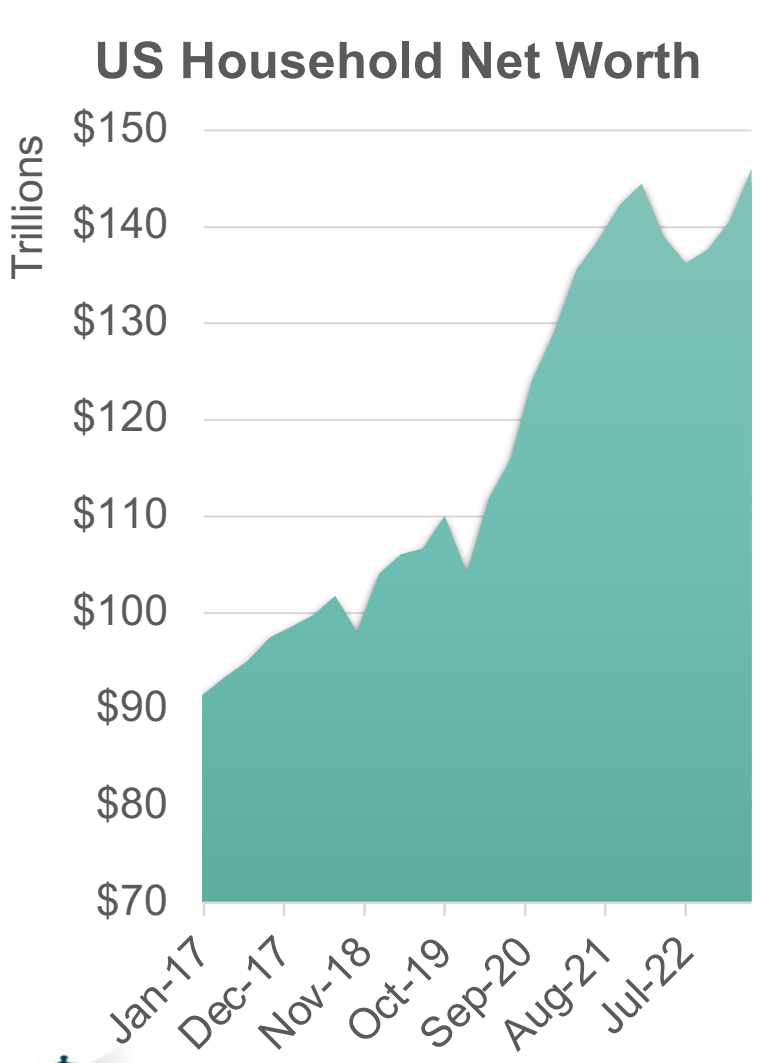
	Dec Sales	YoY Gr
Retail & food services Total	709,890	4.8%
Food services & drinking places	94,559	11.1%
Electronics & appliance stores	7,679	10.4%
Nonstore retailers	120,496	9.7%
Motor vehicle & parts dealers	136,507	8.3%
Clothing & clothing accessories	26,611	2.9%
General merchandise stores	74,032	2.2%
Food & beverage stores	83,124	1.0%
Building material & garden eq	41,665	-2.3%
Furniture & home furn stores	10,783	-5.0%
Gasoline stations	53,169	-8.4%

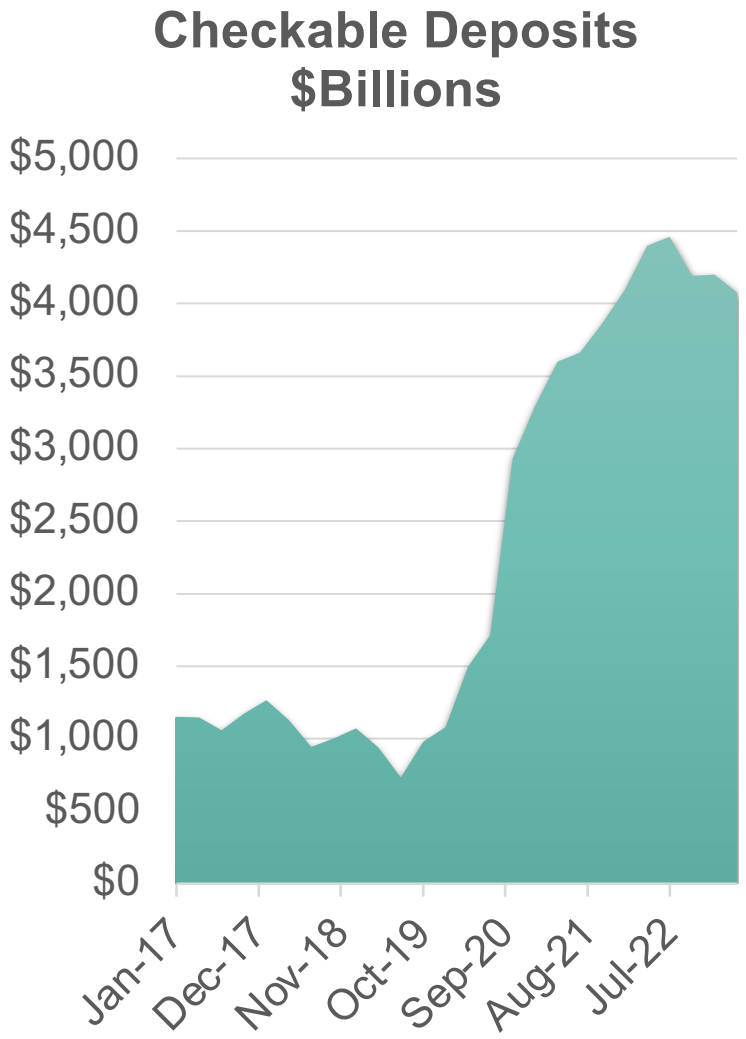
Container Counts

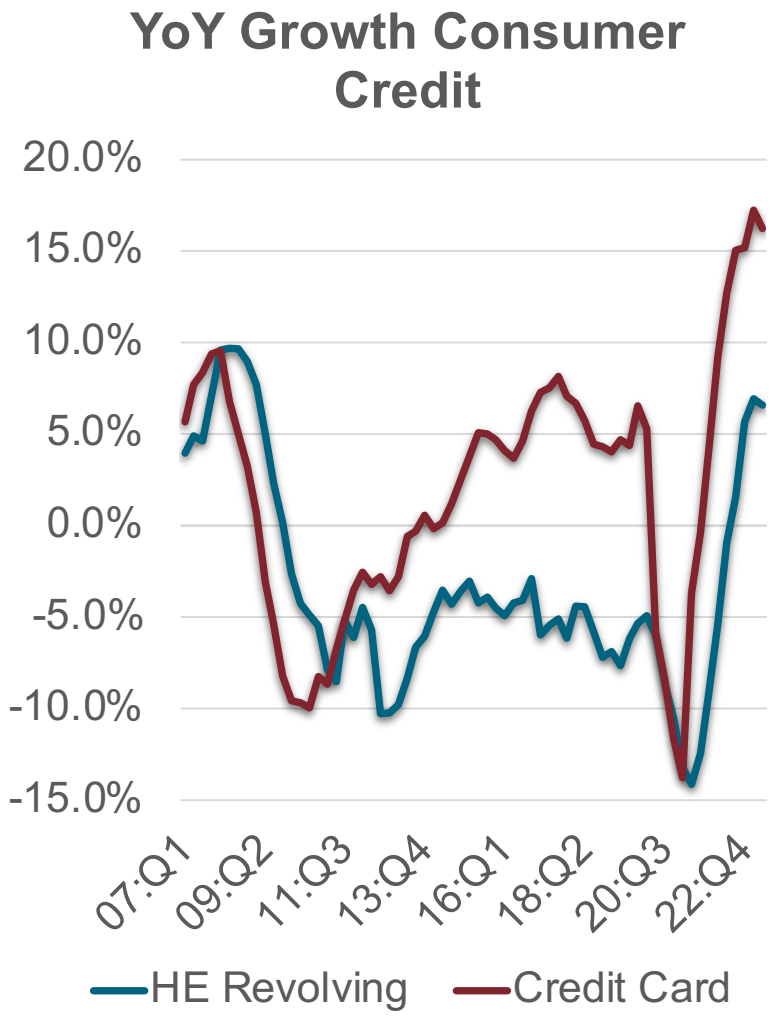




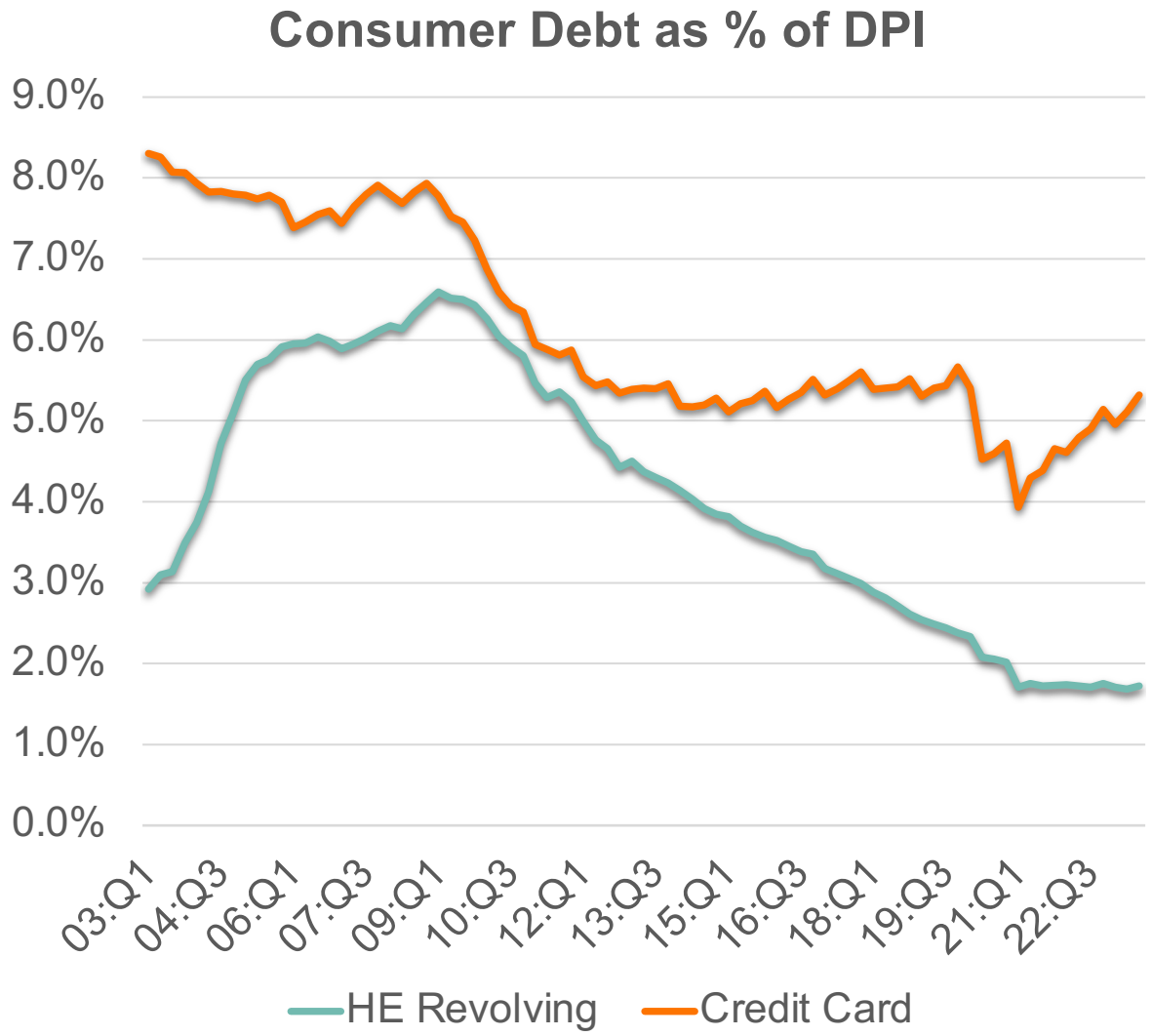
The wealth effect: Still in place

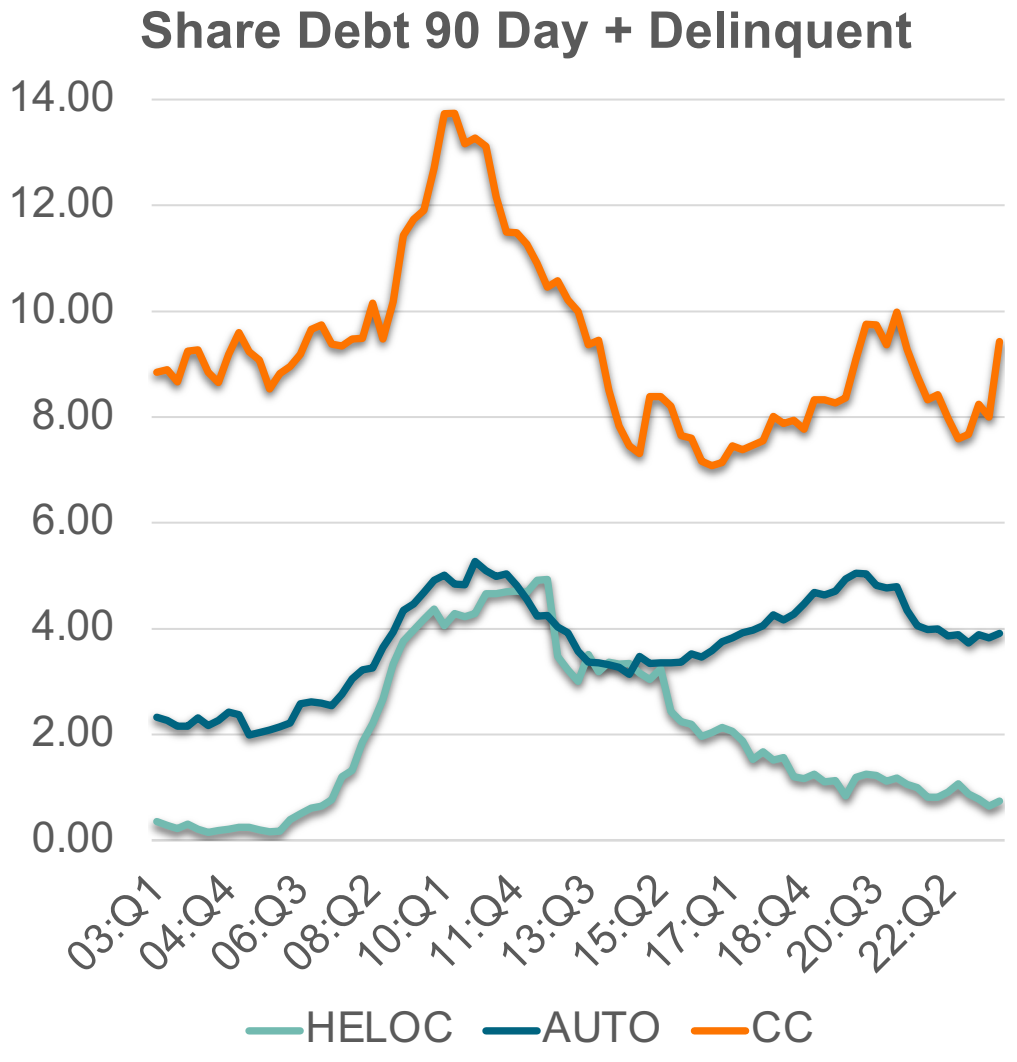






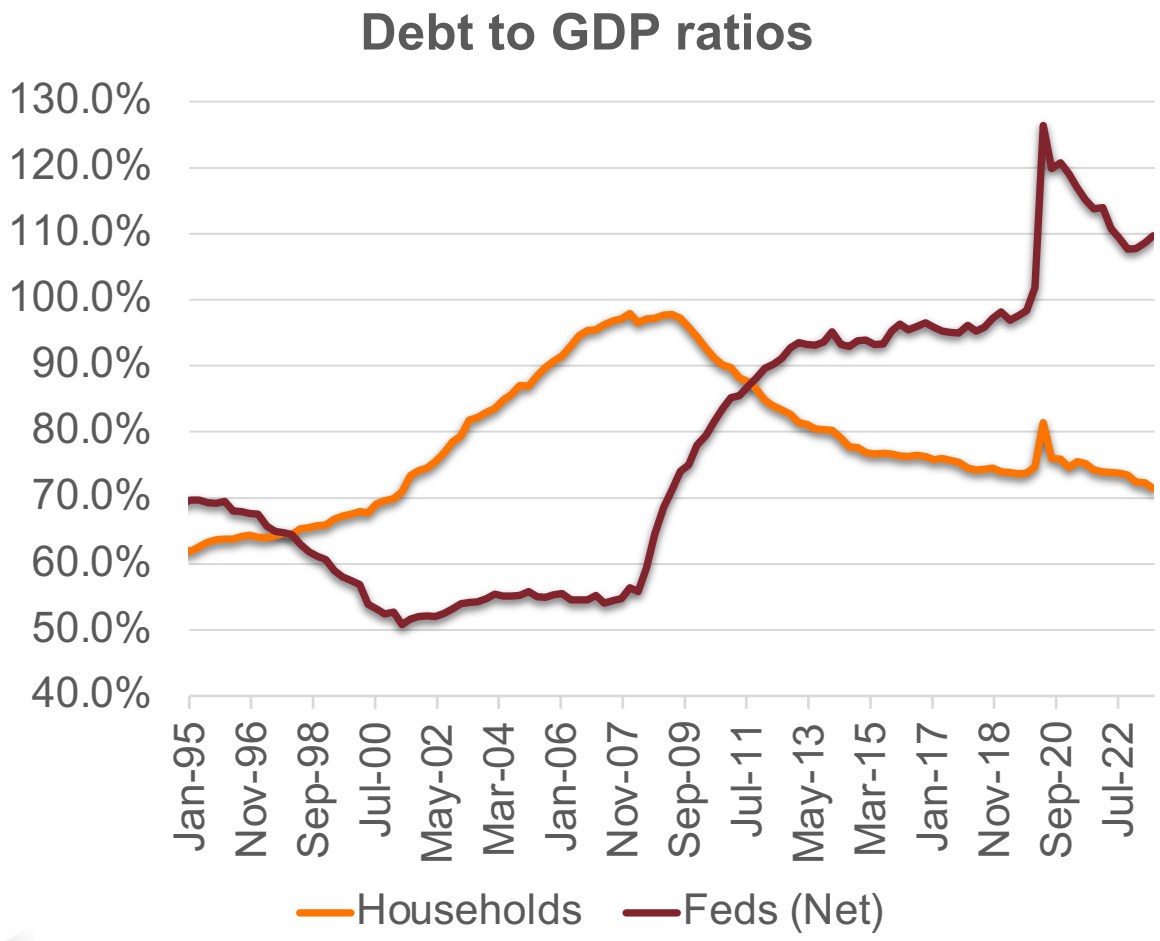
Consumer Debt: Not a problem… yet

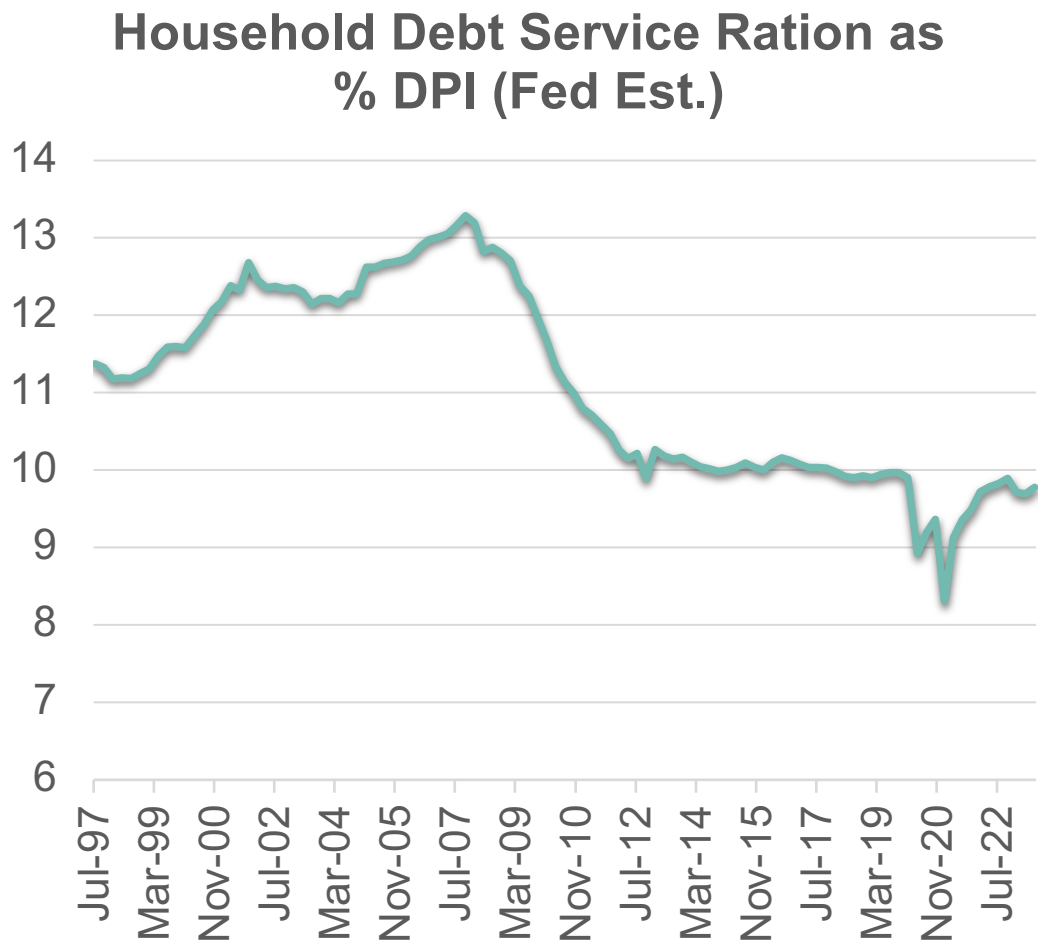




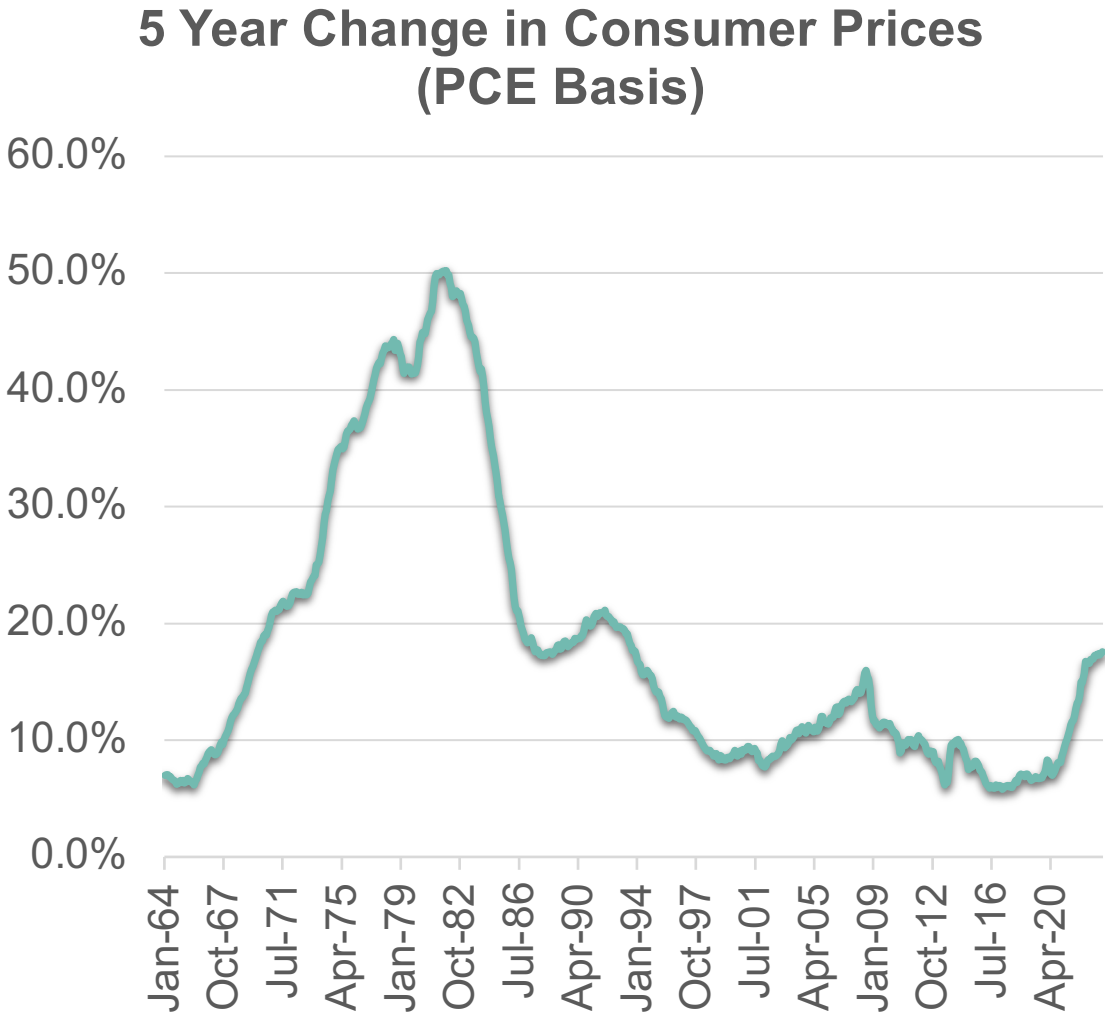
Why didn’t rate hikes hurt?

The household sector is fairly debt insensitive





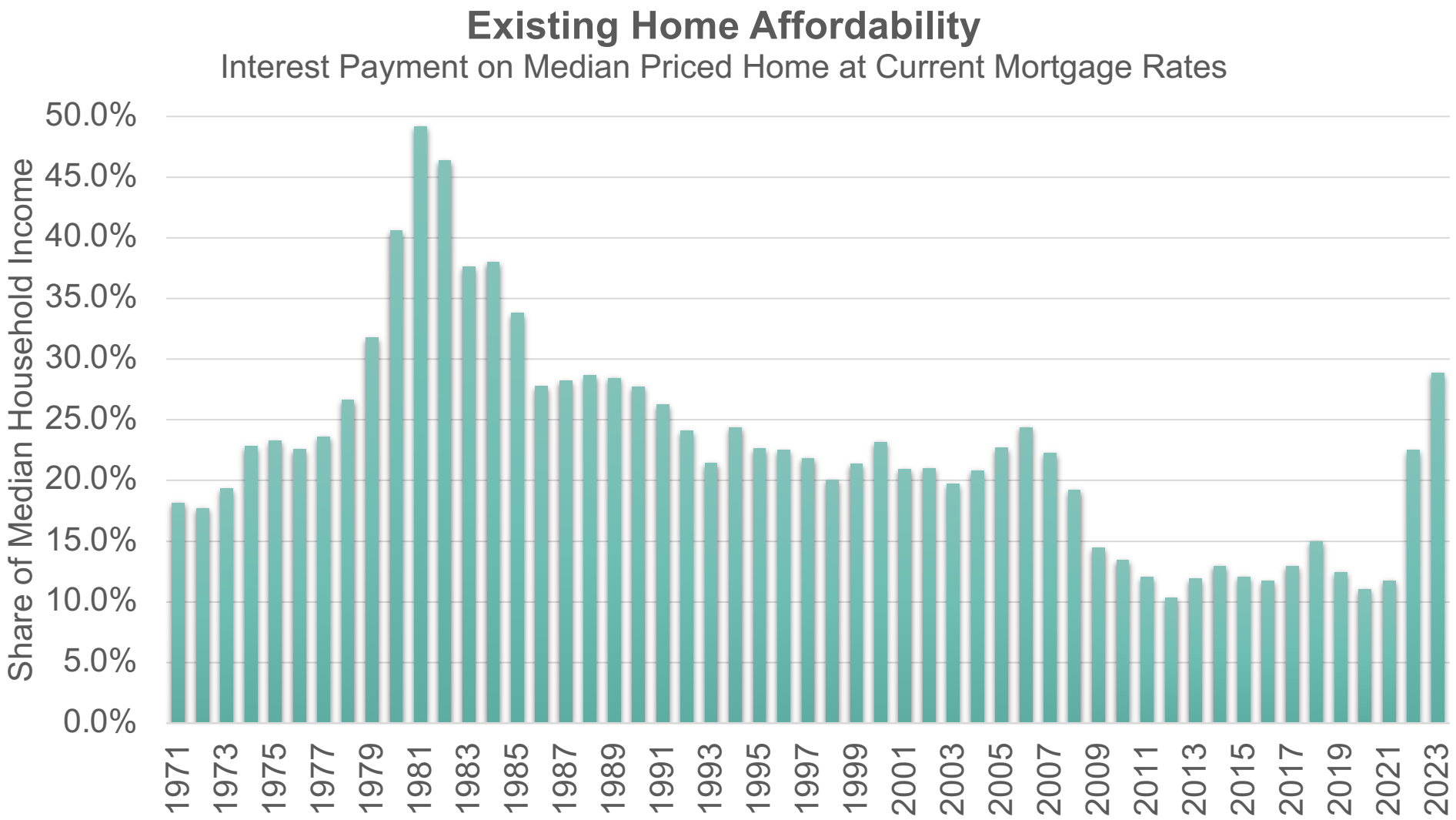
The Longer Run Context



But what about the cost of housing?

	1984-86		1984-86		2020-22		2020-22
Price	$76,003	Mortgage	11.3%	Price	$347,180	Mortgage	4.7%
DP	$15,201	Int	$7,397	DP	$69,436	Int	$10,567
Income	$23,647	Income	$23,647	Income	$71,123	Income	$71,123
DP / Inc	64.3%	Int / Inc	31.3%	DP / Inc	97.6%	Int / Inc	14.9%

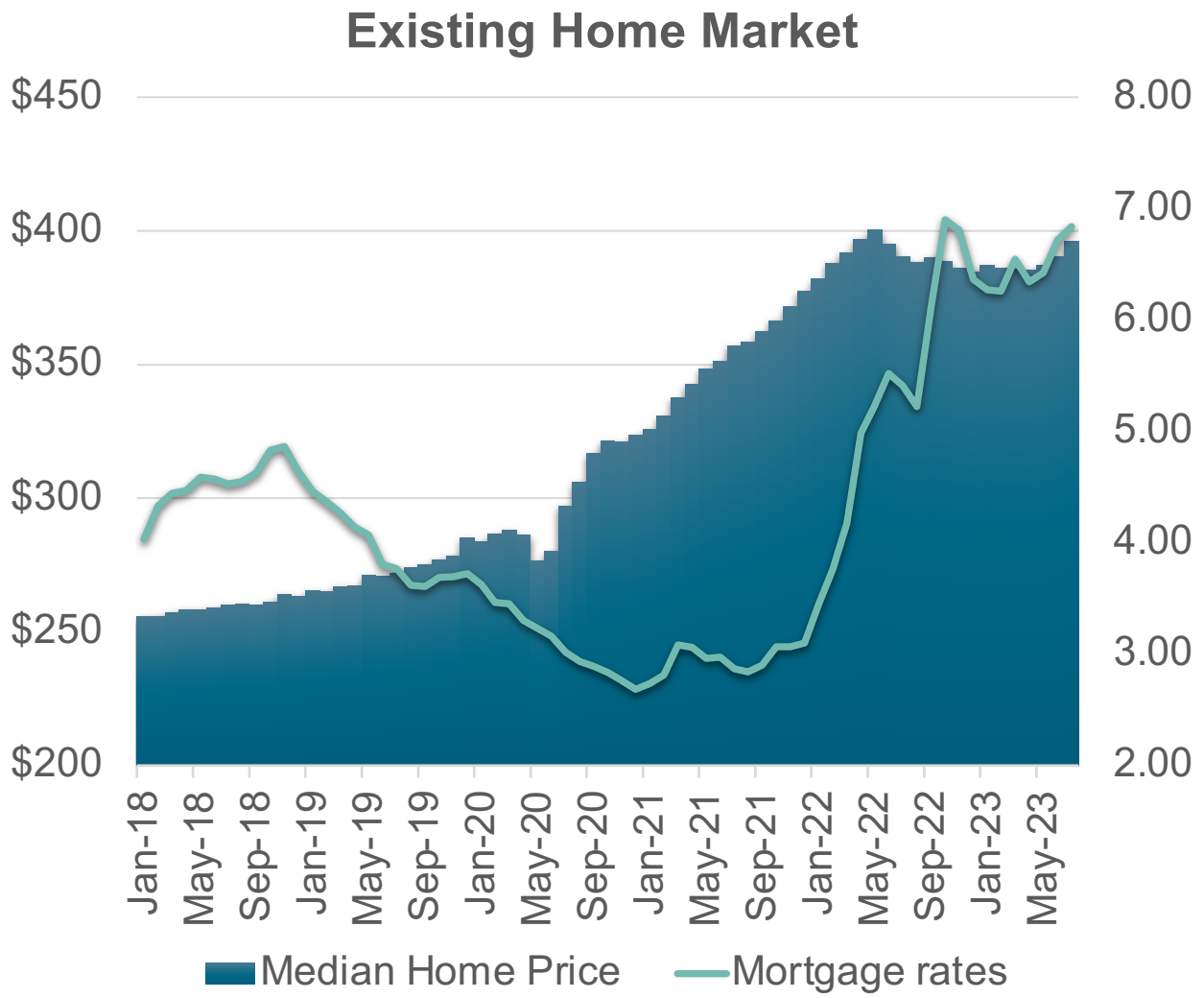
Not the Story…



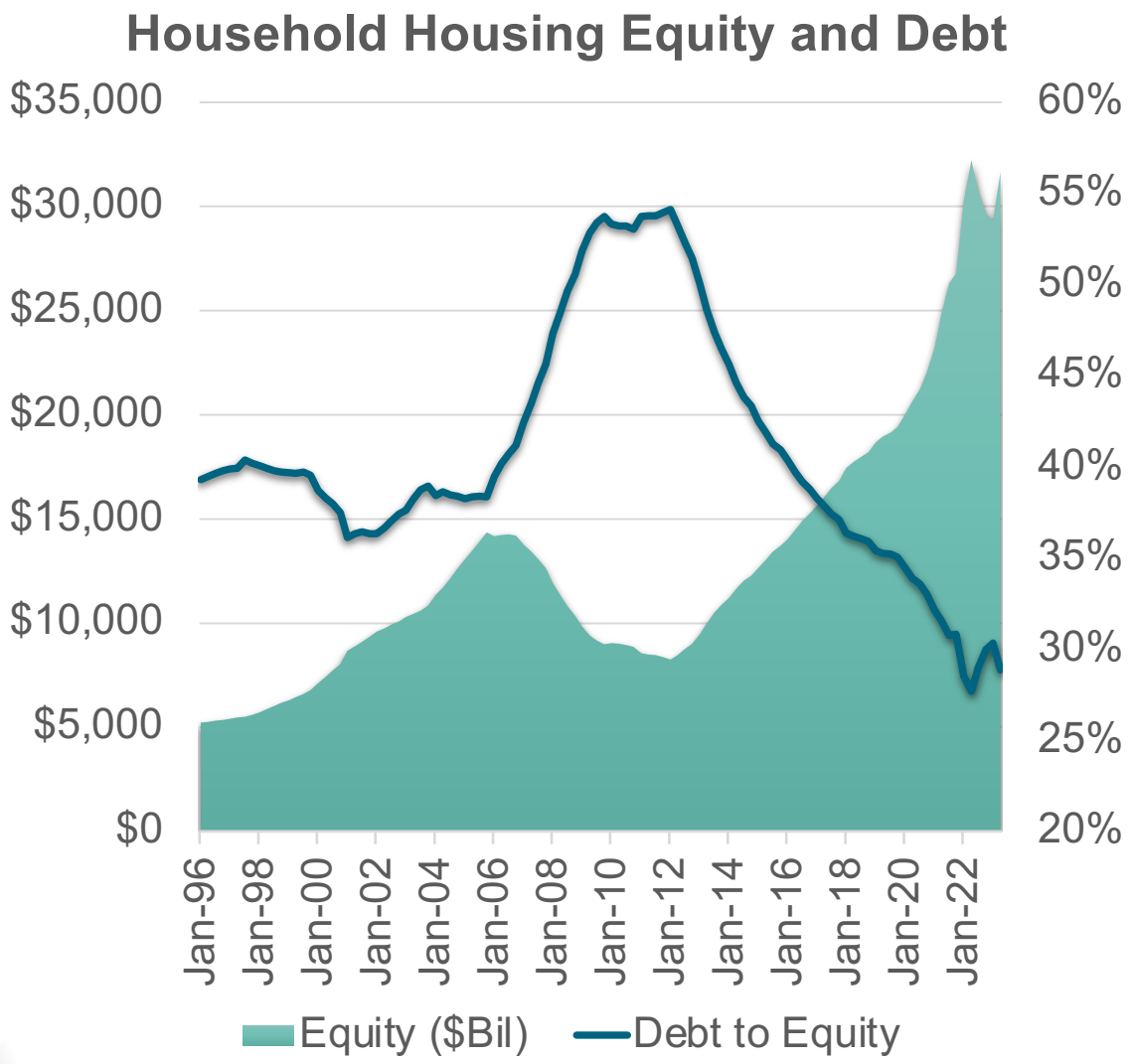
Housing: A Rate Whiplash

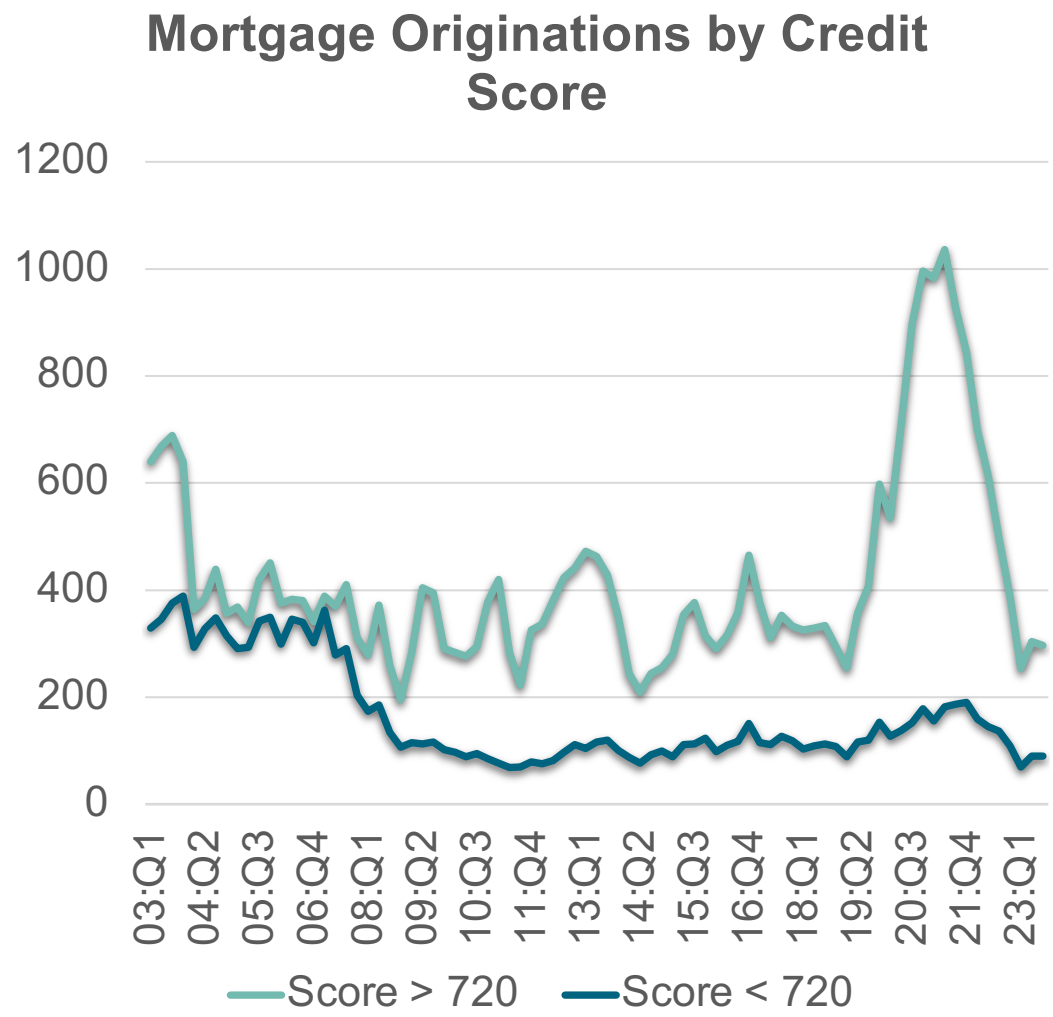
Case Shiller Home Price Appreciation
July 20 – July 22

Tampa	64.0%	Los Angeles	37.9%
Phoenix	62.0%	SF	35.1%
Miami	61.4%	New York	34.9%
Dallas	54.2%	Boston	34.6%
Charlotte	49.5%	Portland	33.6%
LV	49.2%	Cleveland	30.9%
SD	49.1%	Detroit	29.4%
Atlanta	45.8%	Chicago	27.4%
Seattle	43.9%	DC	26.0%
Denver	40.3%	Minneapolis	24.6%

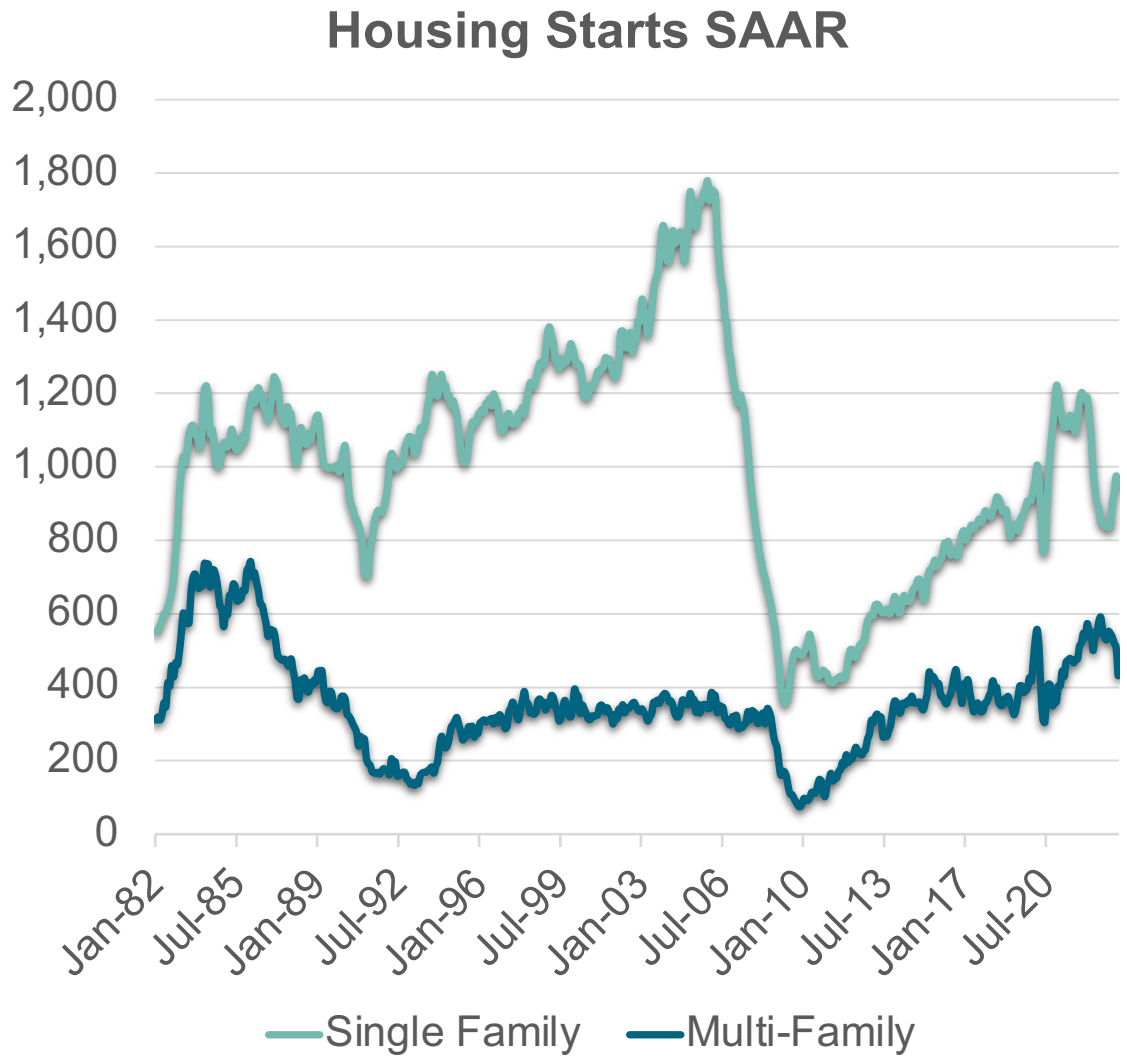


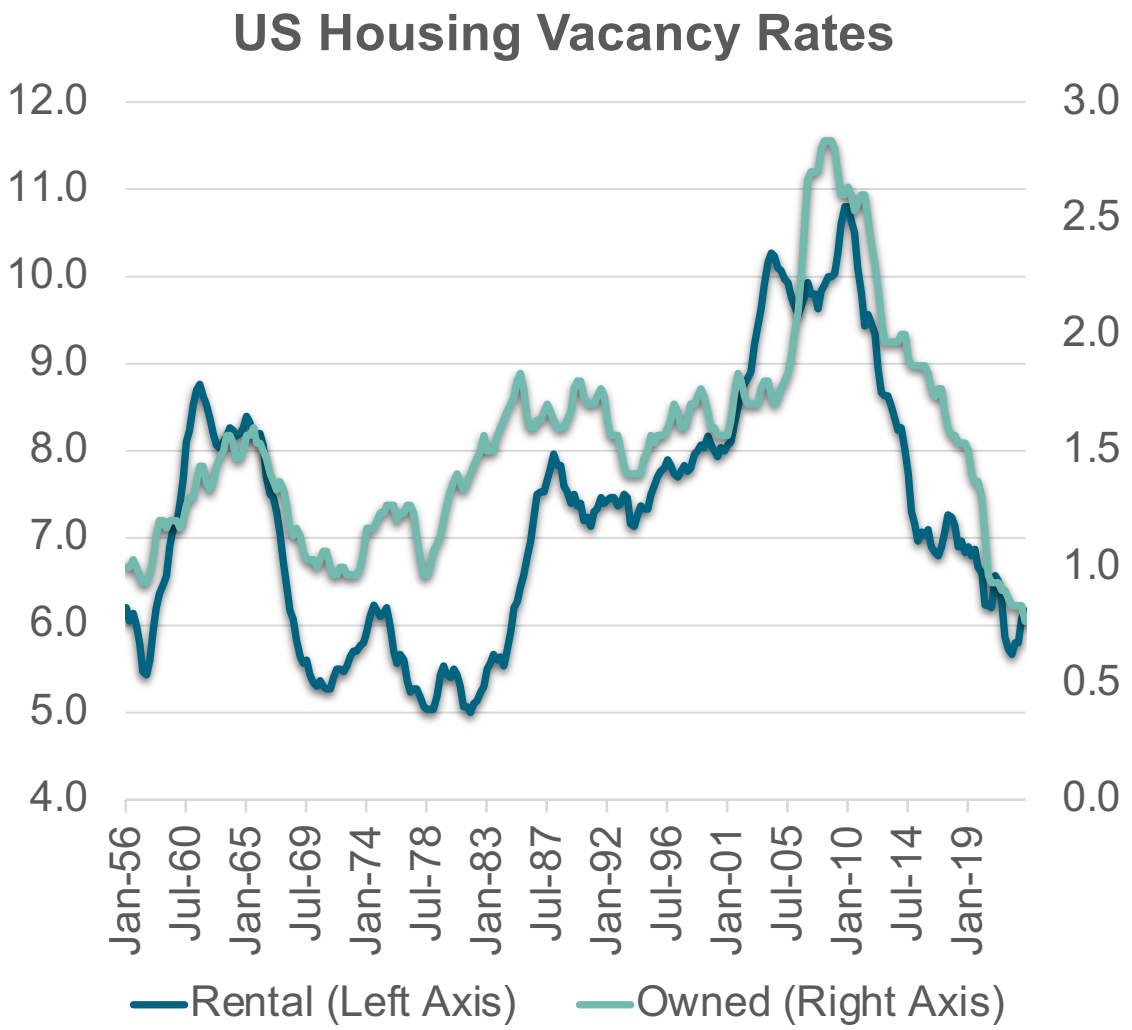
Strong Housing Fundamentals



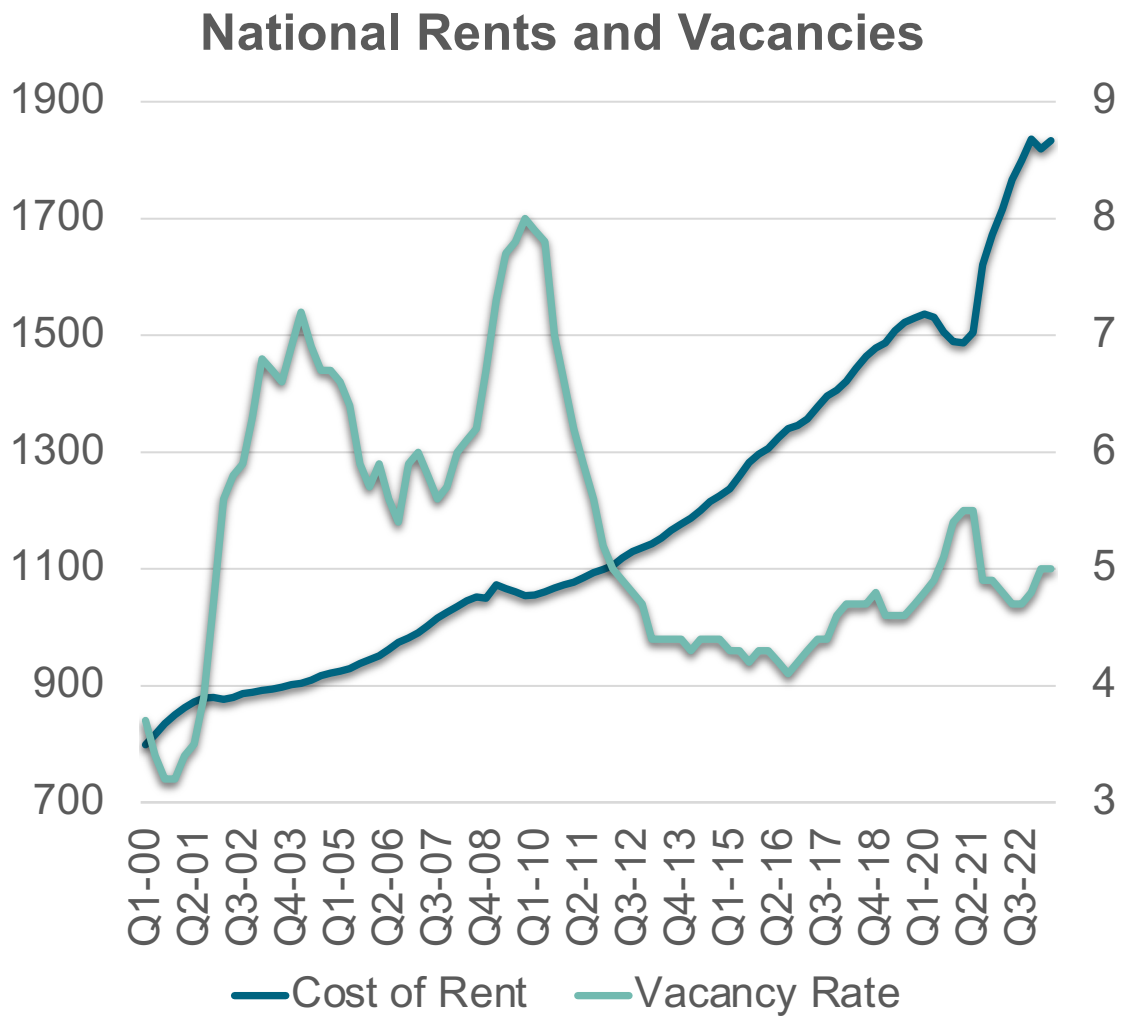


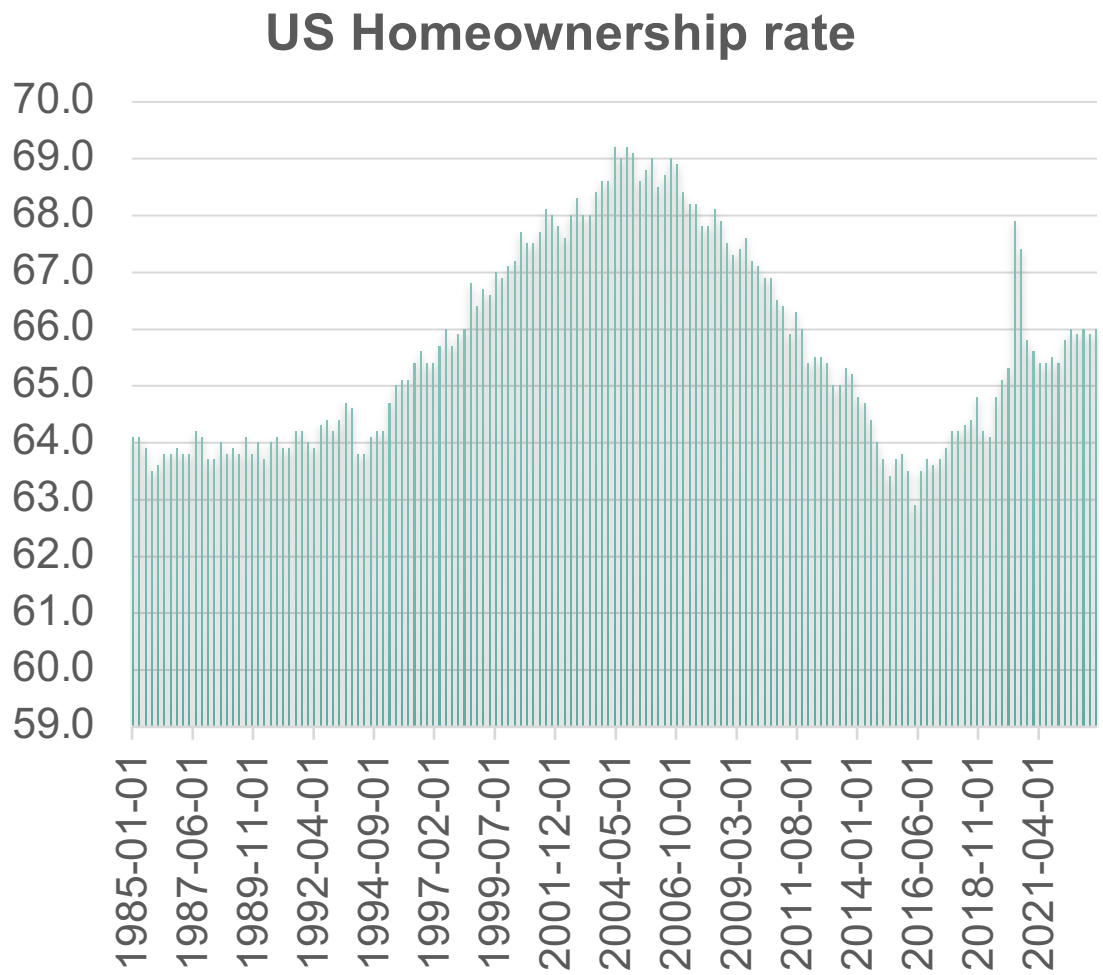
The Supply Conversation



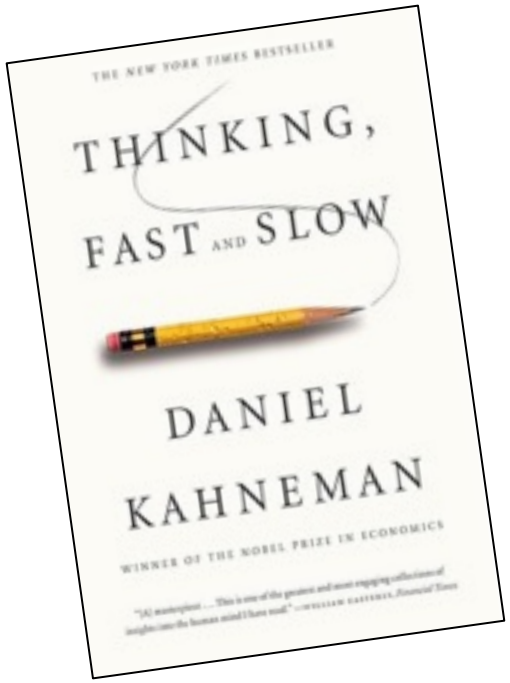


Entry Problem Driving MF





How do narratives go astray?



"People have two modes of thought: "System 1" is fast, instinctive and emotional; "System 2" is slower, more deliberative, and more logical."

"System 1 is gullible and biased to believe, System 2 is in charge of doubting and unbelieving, but System 2 is sometimes busy, and often lazy"

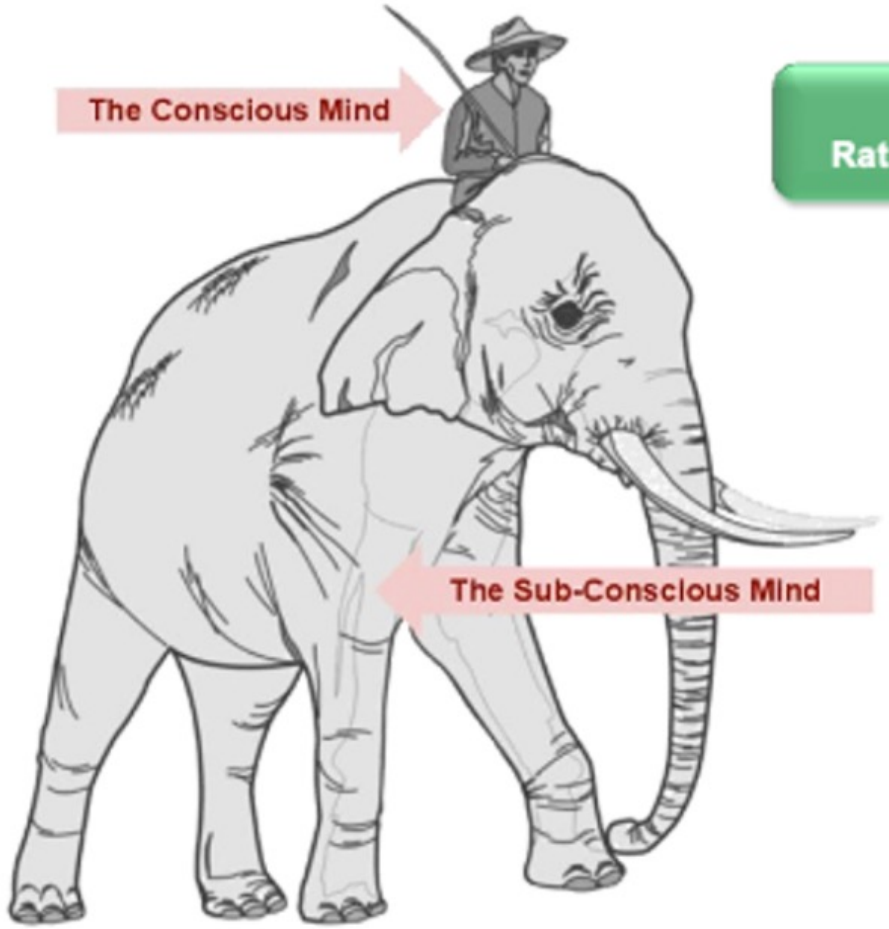
— D. Kahneman, *Thinking Fast and Slow*

Are the horizontal lines parallel?

<u>*Some* Examples of Cognitive Biases</u>

Anchoring bias
Apophenia
Availability heuristic
Cognitive dissonance
Confirmation bias
Egocentric bias
Extension neglect
False priors
Framing effect
Logical fallacy
Prospect theory
Self-assessment
Truth judgment

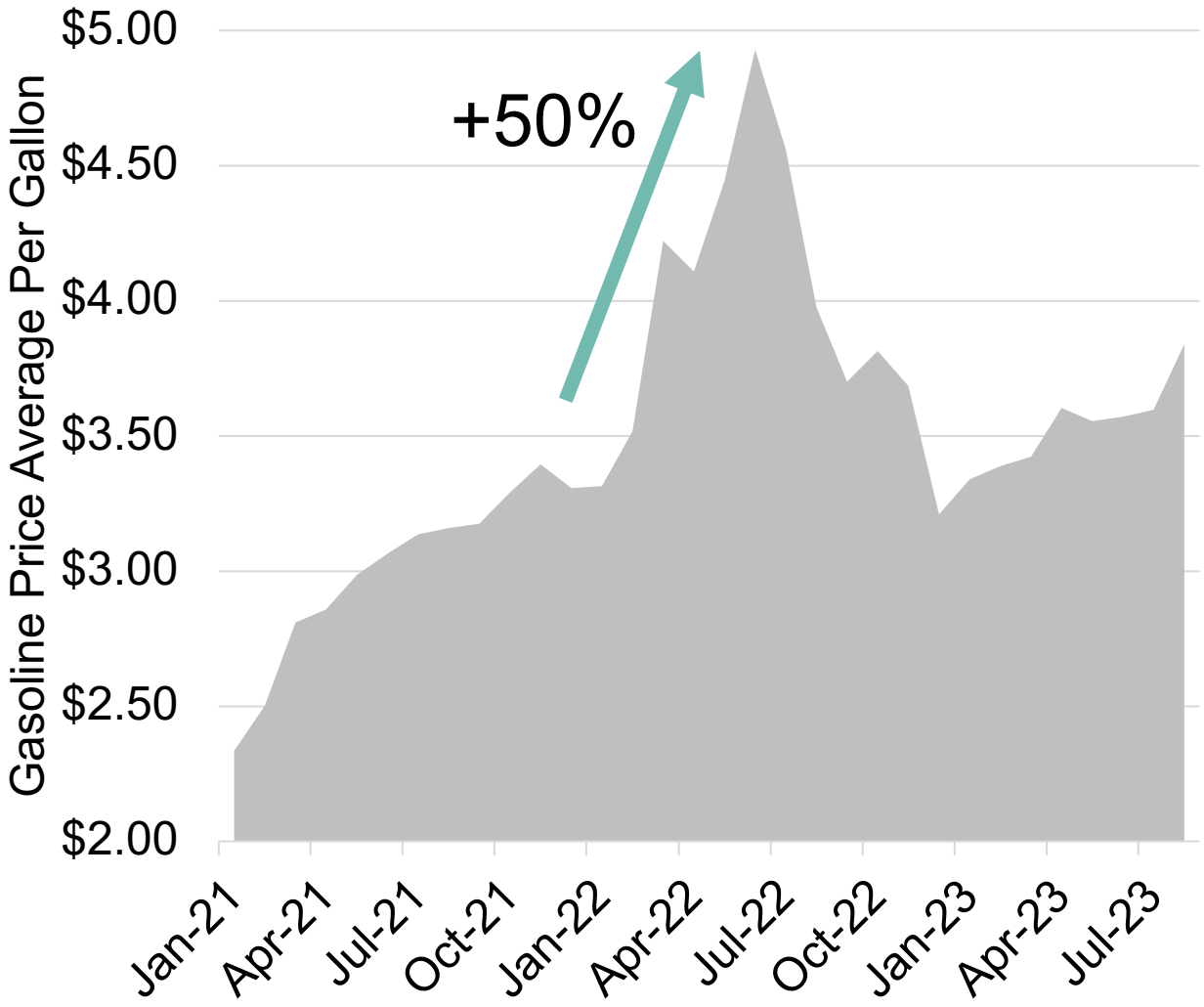
We don't think as much as we think we think

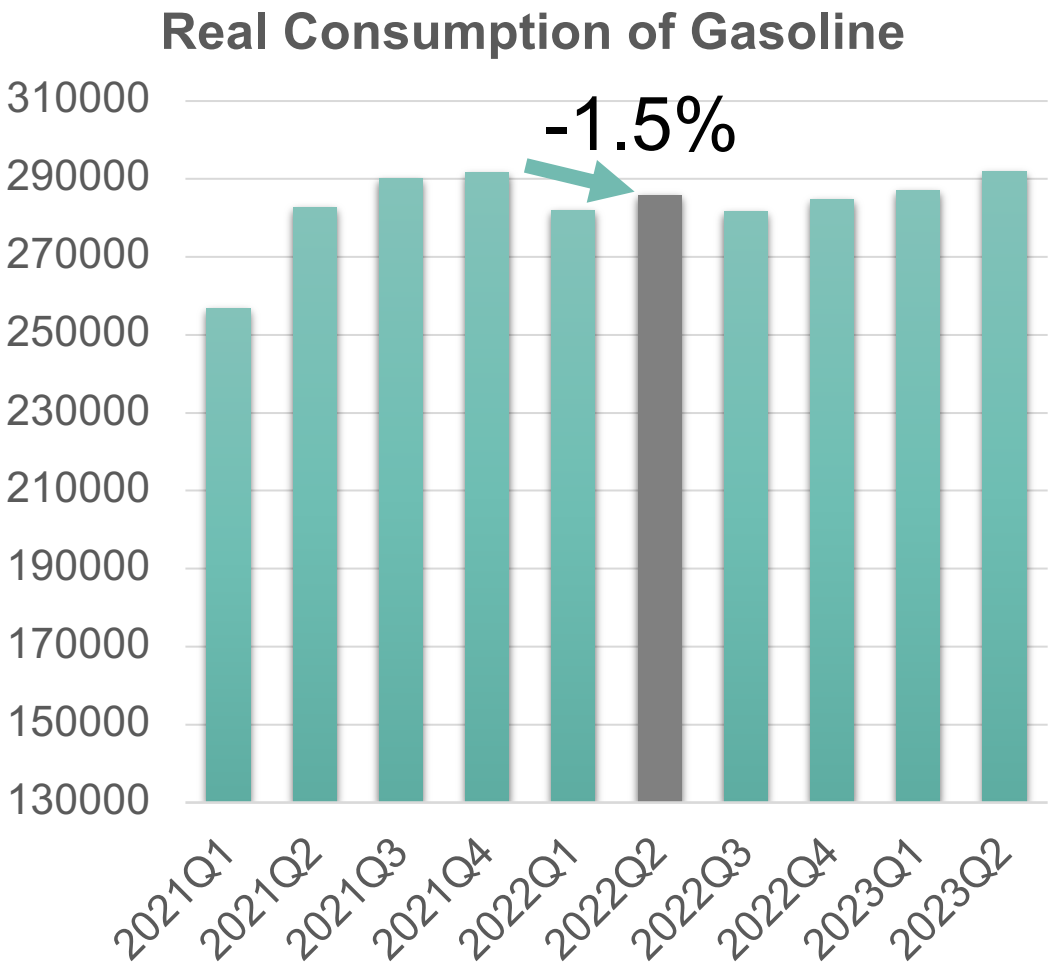


System 2:
Rational, analytical

System 1 :
Emotional, instinctive

Reality: Inflation is caused by demand





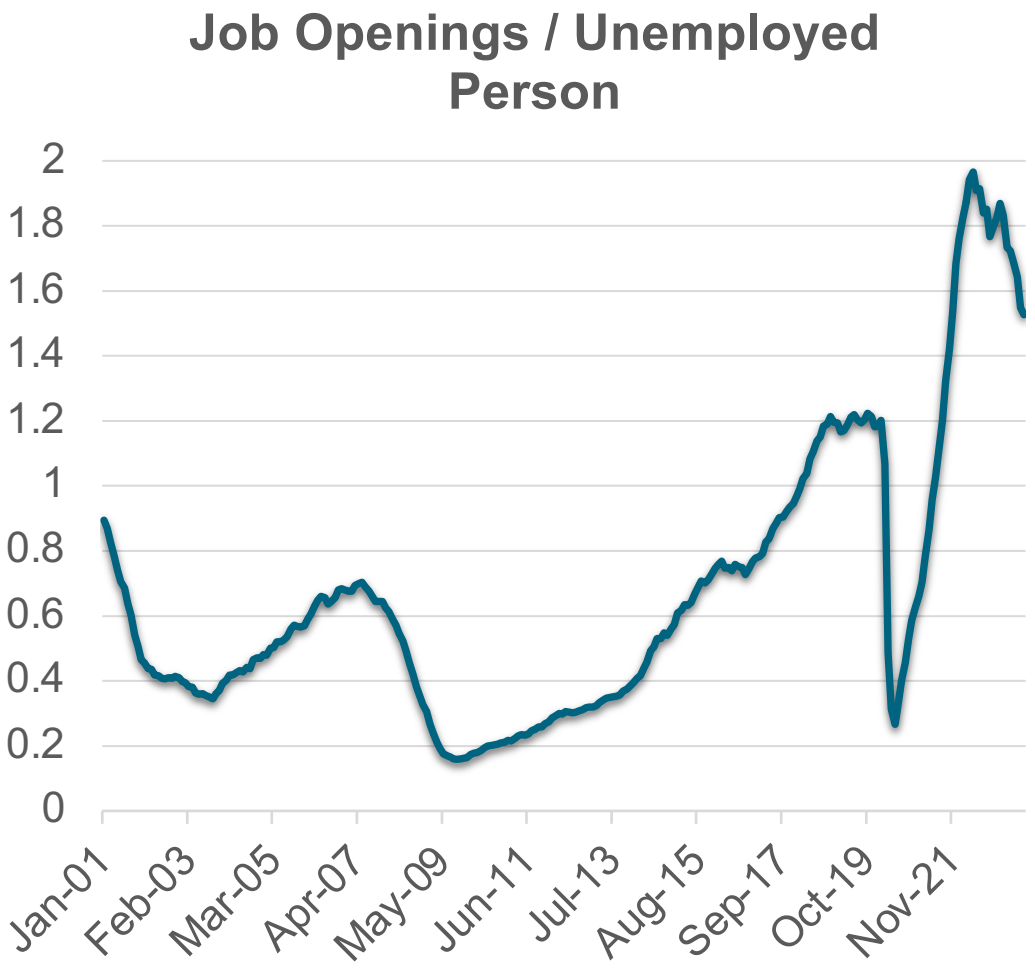
The narrative on inflation

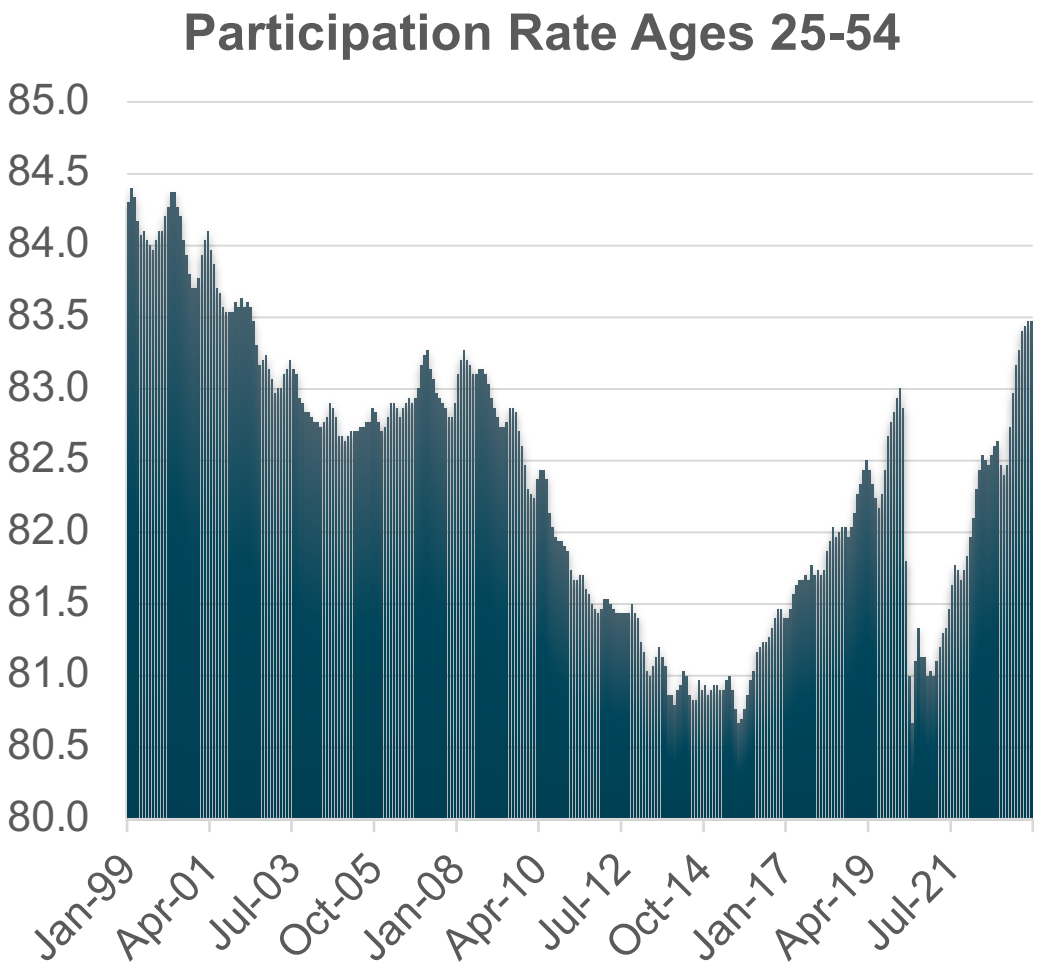
85% of Americans Are Feeling Impact of Inflation in Day-to-Day Lives, Finds New Survey

NEWS PROVIDED BY
L.E.K. Consulting →
05 Dec, 2022, 09:30 ET

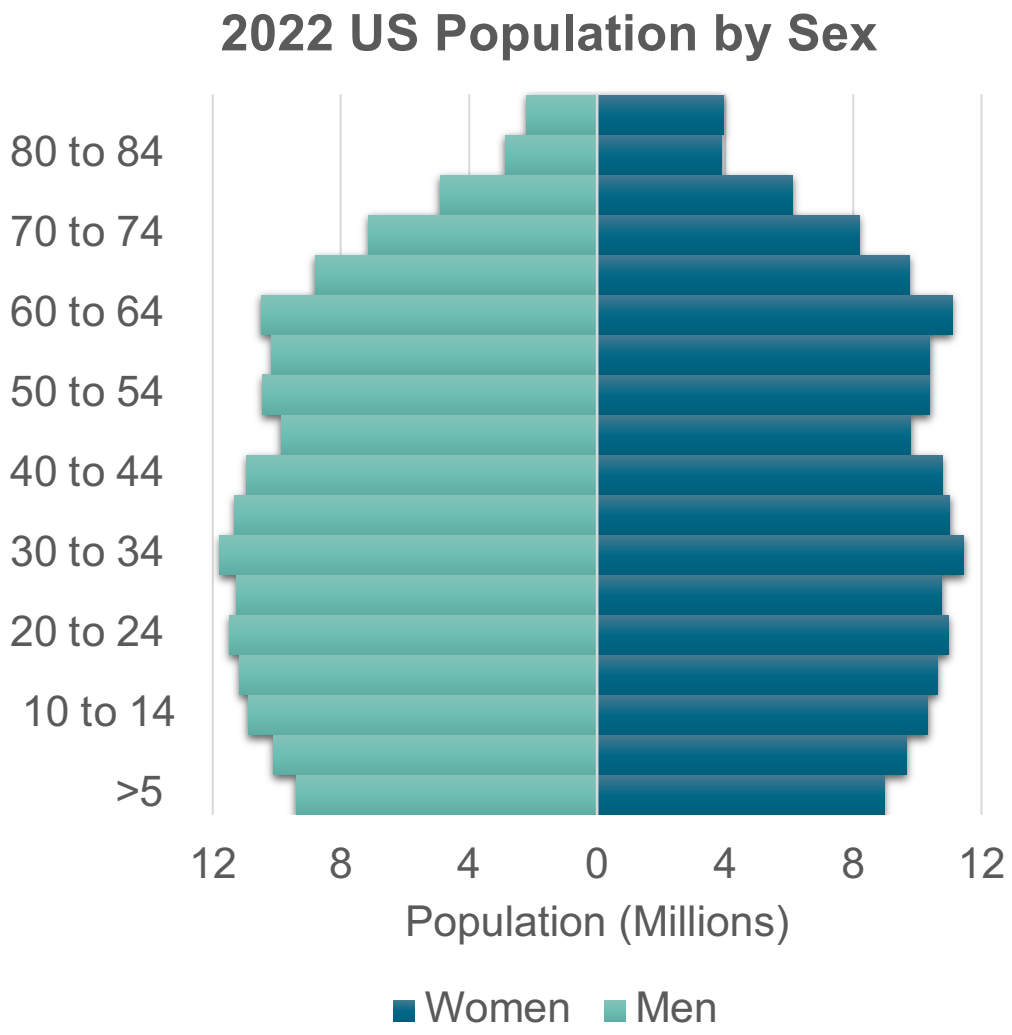
- About 90% of Americans said that inflation has had an impact on their spending over the past year when it comes to food and beverage, including 54% who said the impact has been significant.
- A similar number – 88% – said inflation has impacted their spending at restaurants.
- About 89% said inflation has had an impact on their motor vehicle spending, such as gasoline – including 56% who said it's had a significant impact.
- Eighty-six percent said inflation has impacted their spending on travel over the past year (45% said significantly).

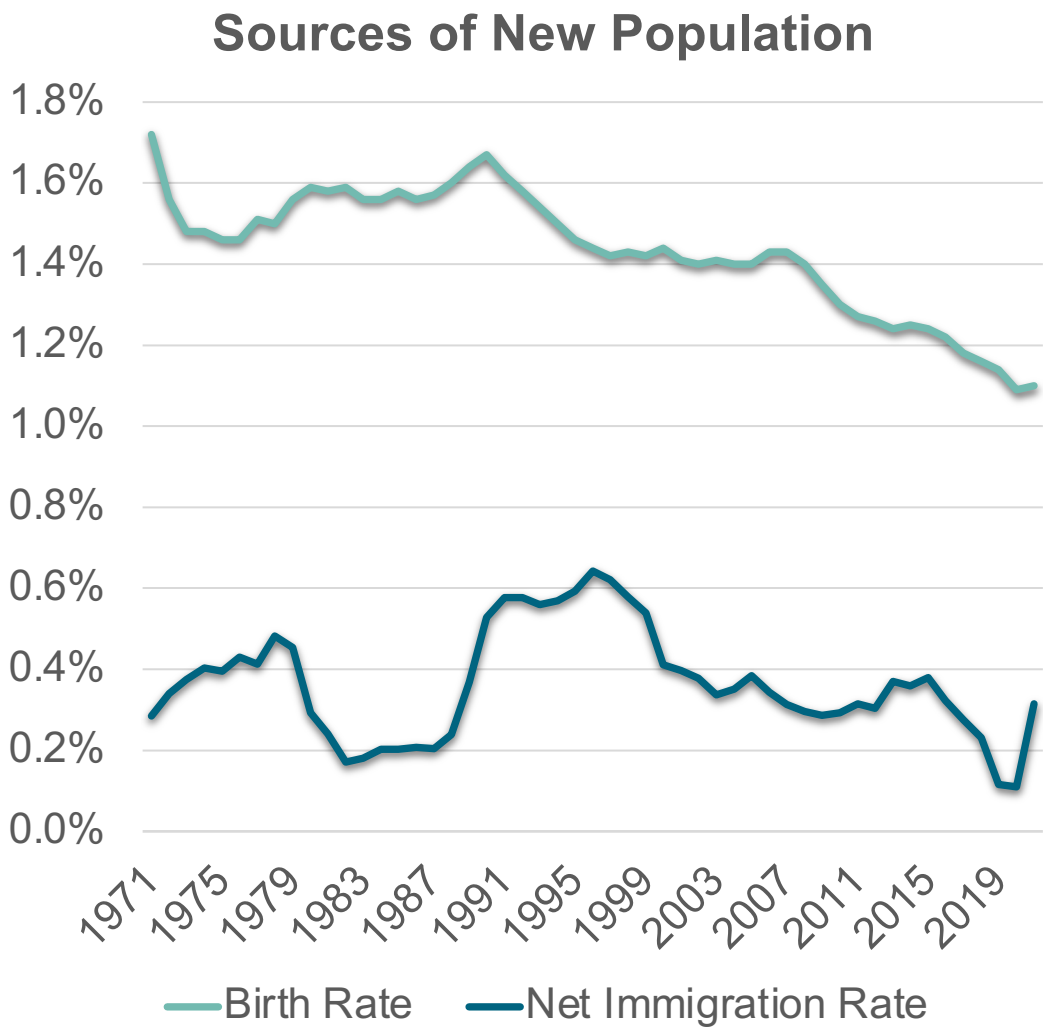
The deeper issue? Labor supply, not consumer demand



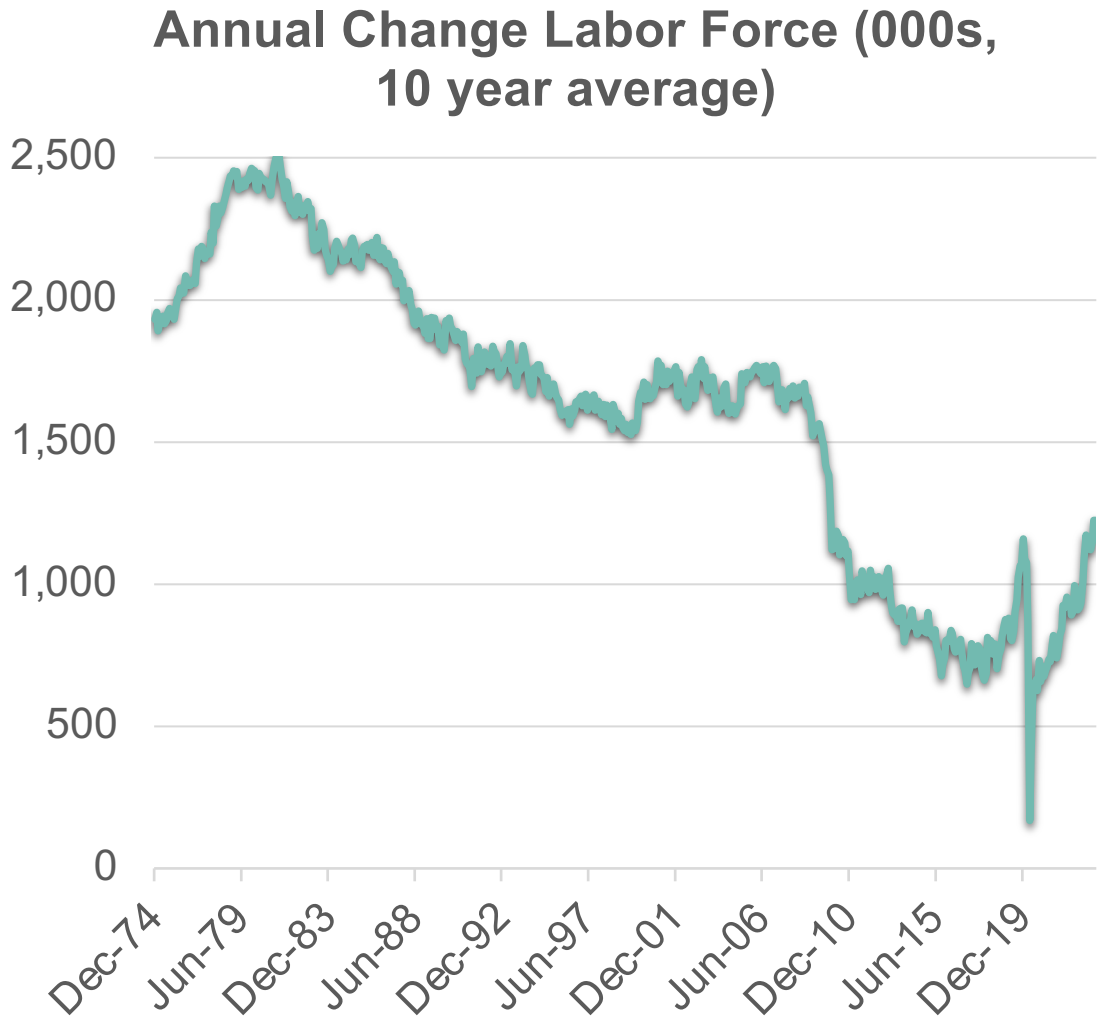


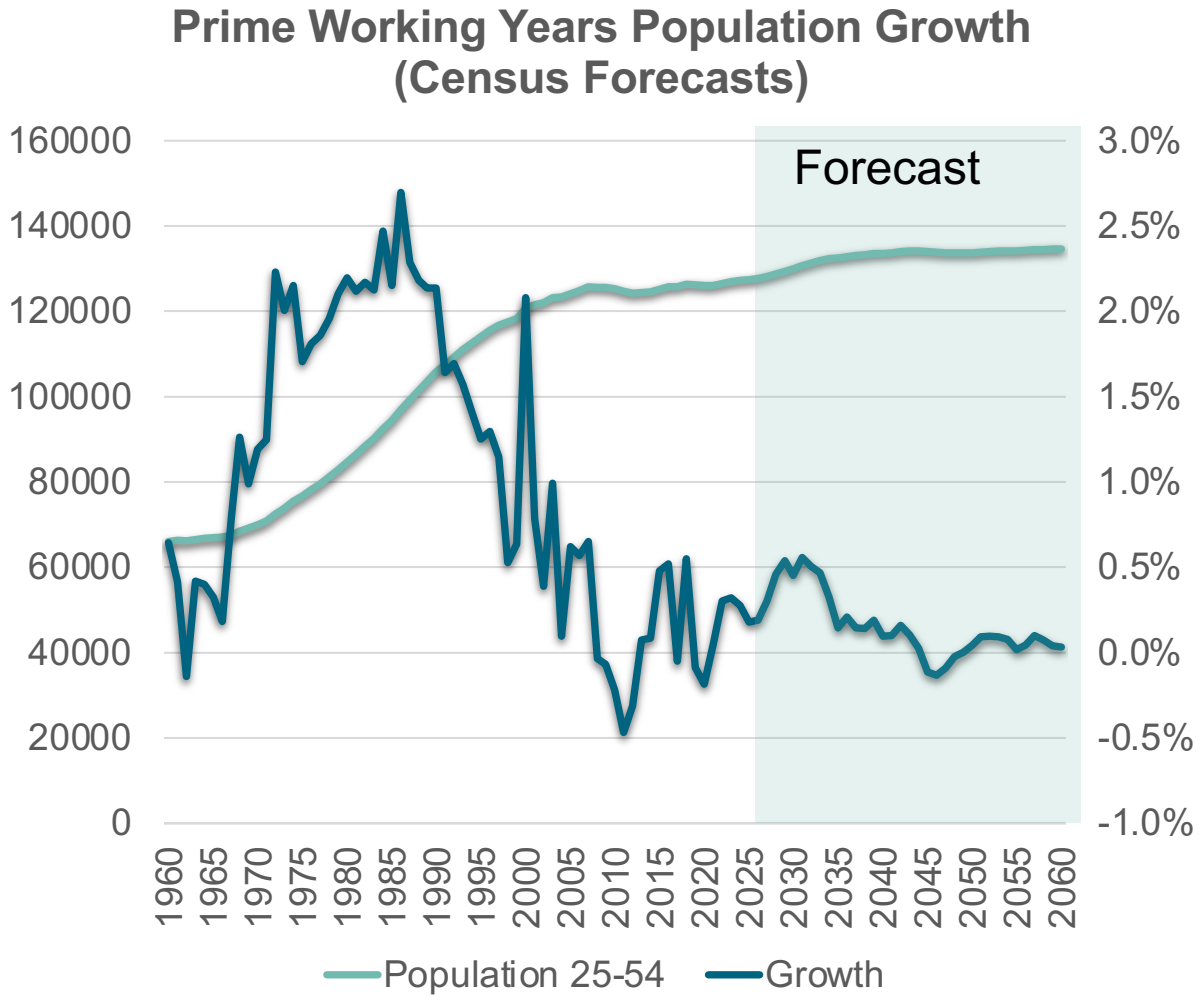
The Era of Labor Shortages is Here





Labor Supply

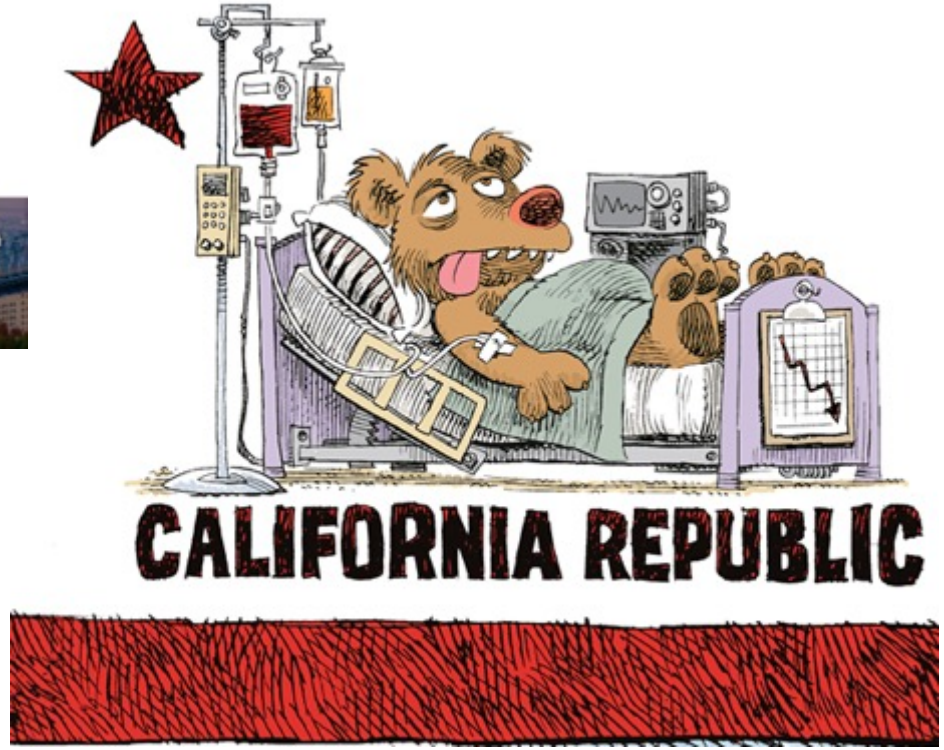




The Regional Narrative

≡ Chief Executive

	Rank 2023	Rank 2022
California	50	50
New York	49	49
Illinois	48	48
New Jersey	47	47
Oregon	46	45
Washington	45	46
Massachusetts	44	44
Hawaii	43	42
Connecticut	42	43
Alaska	41	36
Minnesota	40	41



> So many stores shuttered in downtown SF. Feels post-apocalyptic... The philosophy that led to this bleak outcome will be the end of civilization if extended to the world."
>
> Elon Musk, Twitter CEO.

OPINION

California's Corporate Exodus

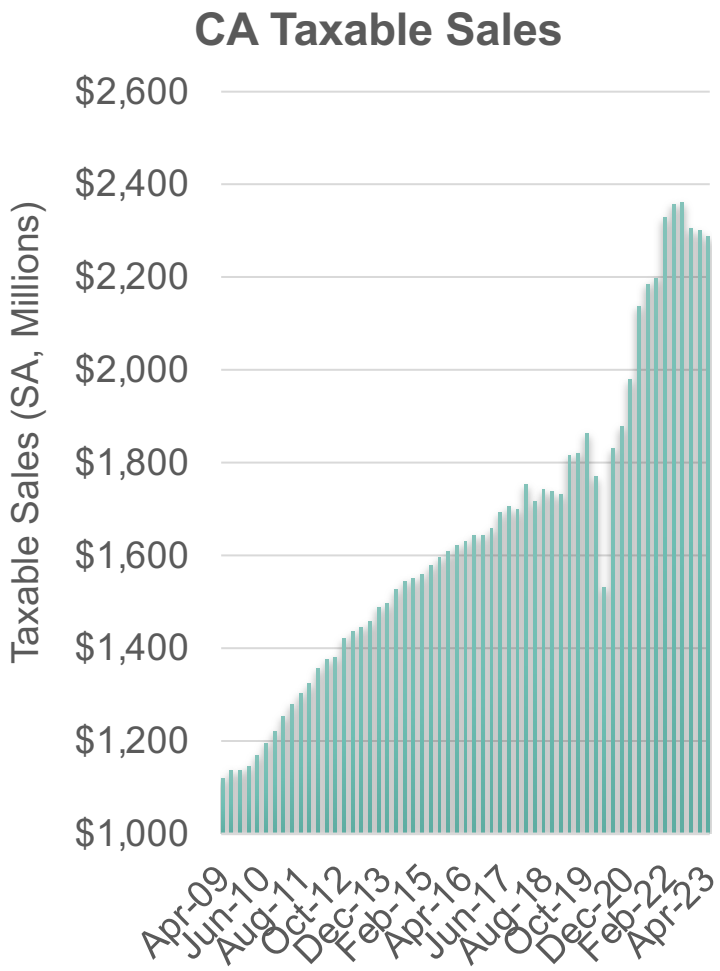
A new report documents the accelerating business flight from the state.

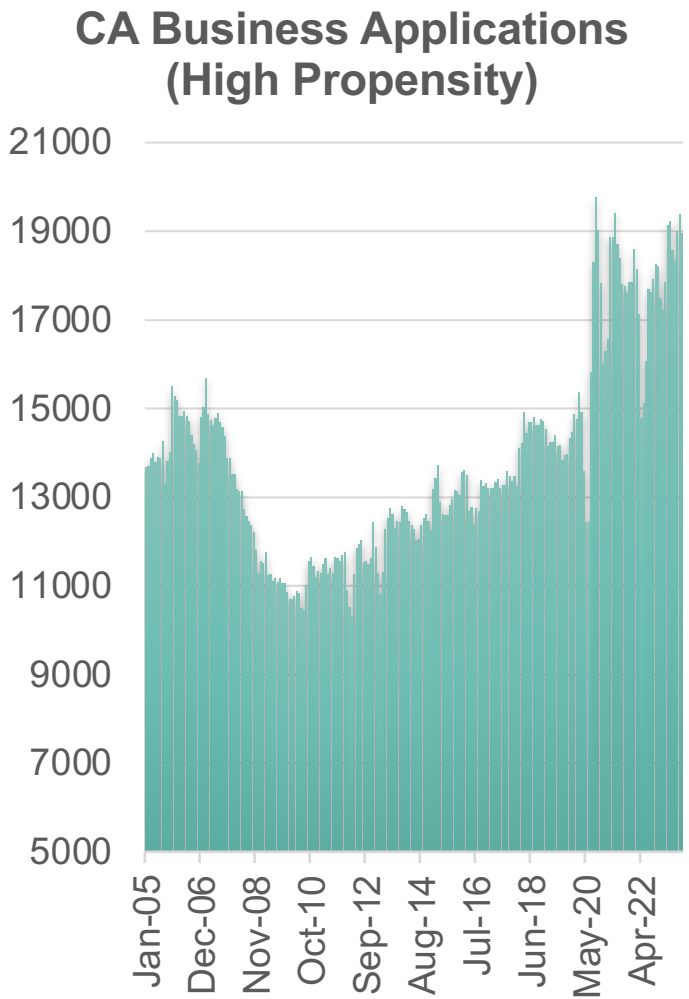
By The Editorial Board

Follow

Oct. 26, 2022 12:26 pm ET

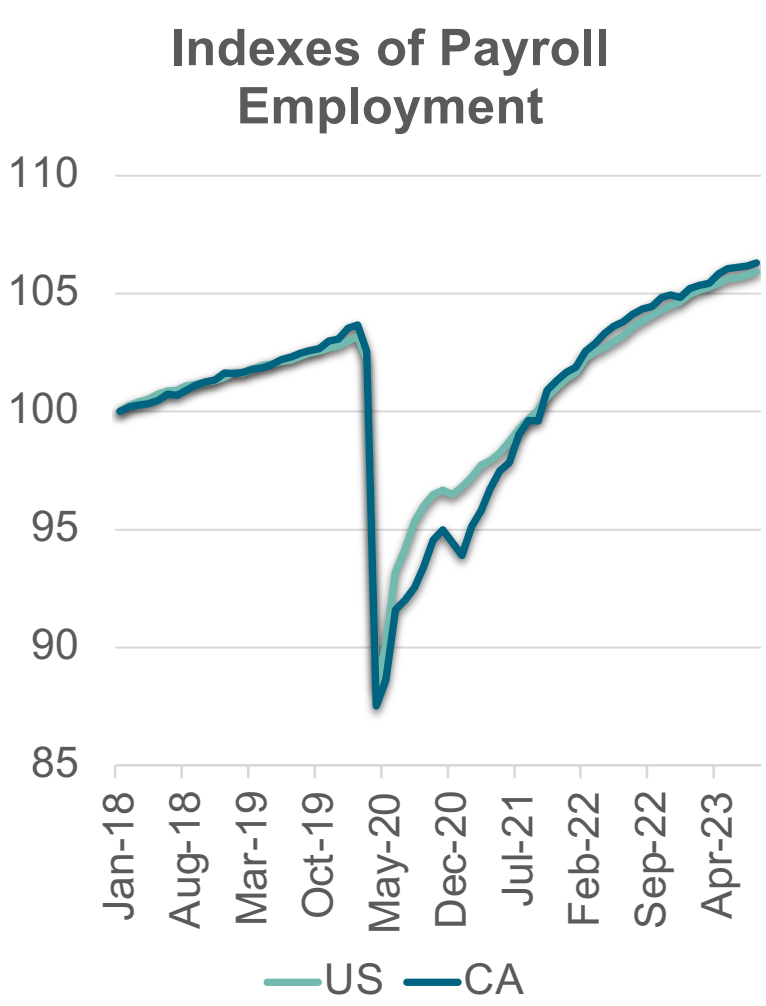
CA Business Activity

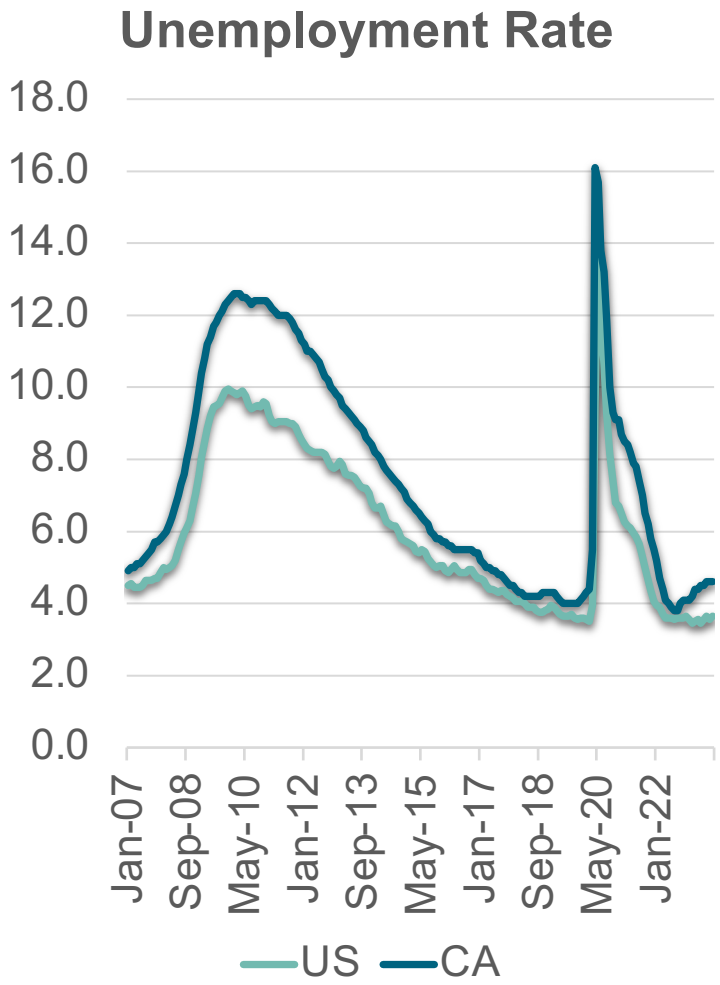


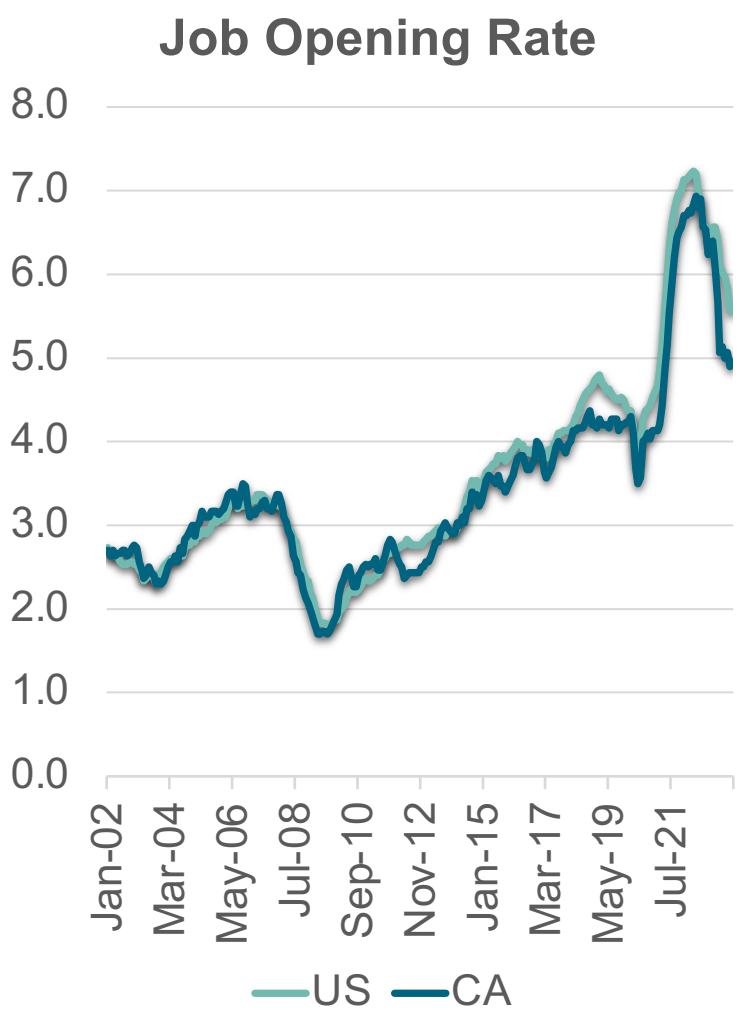


Change 2019 – 2023		
	US	CA
Real GDP Growth	8.0%	9.1%
Change in Payroll Jobs	3.6%	3.8%
Nominal Per Capita Income Growth	23.3%	25.5%
Average Annual Earnings Growth	4.5%	4.9%
Home Price Appreciation	47.5%	43.6%
Change in Unemployment Rate	0.3	0.8

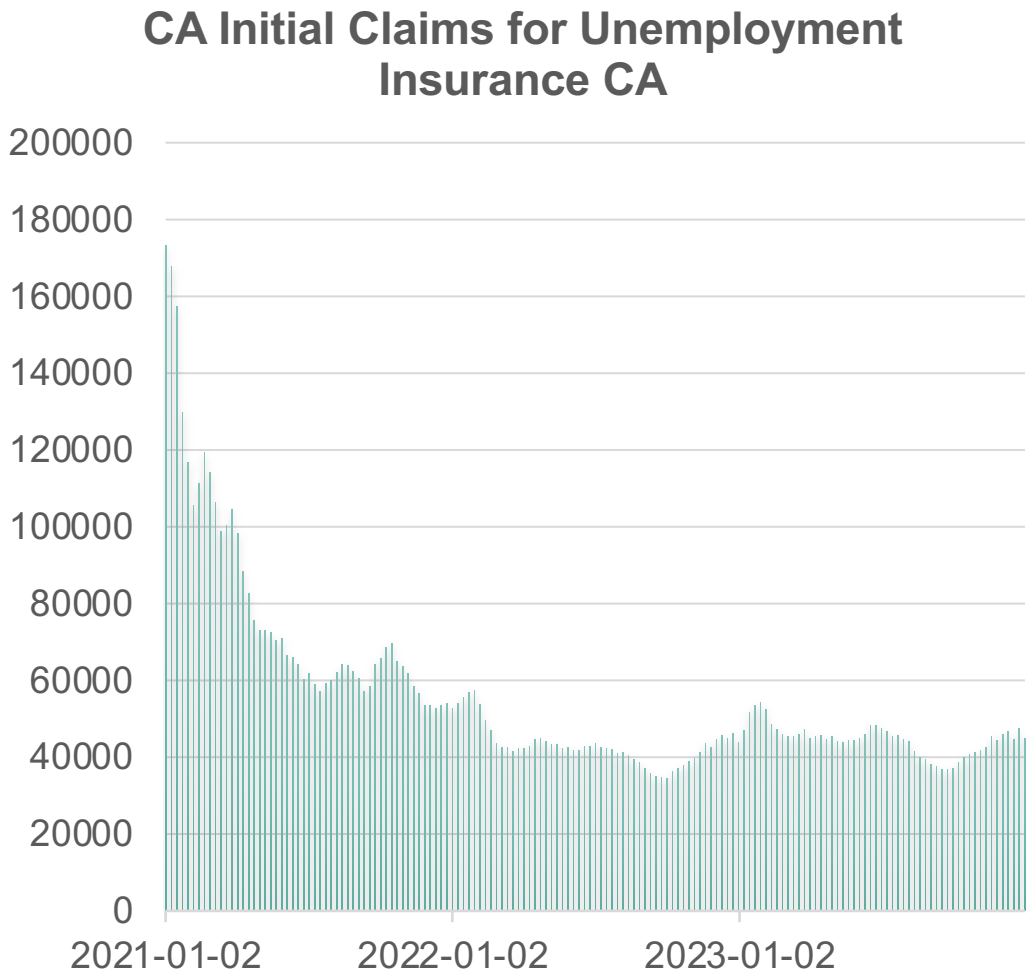
The California Situation

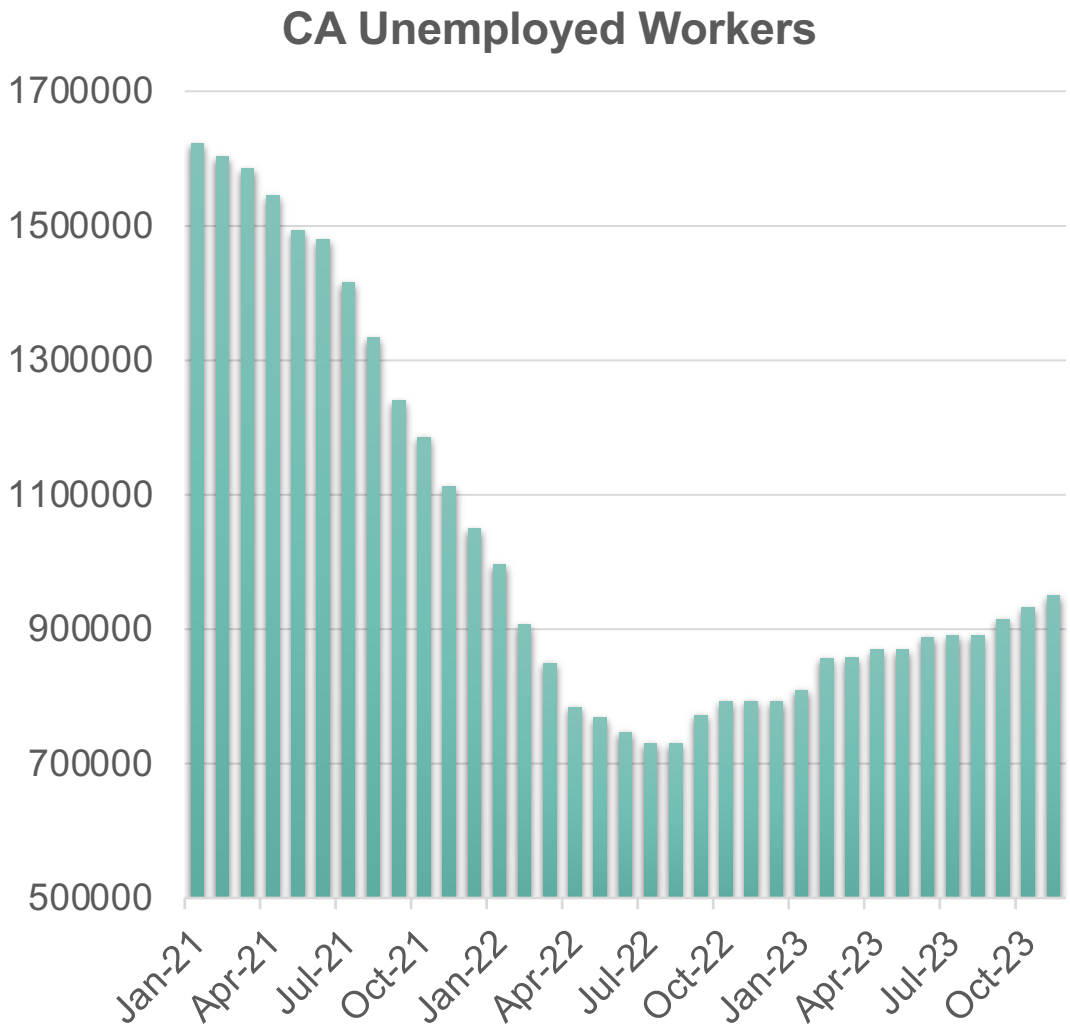




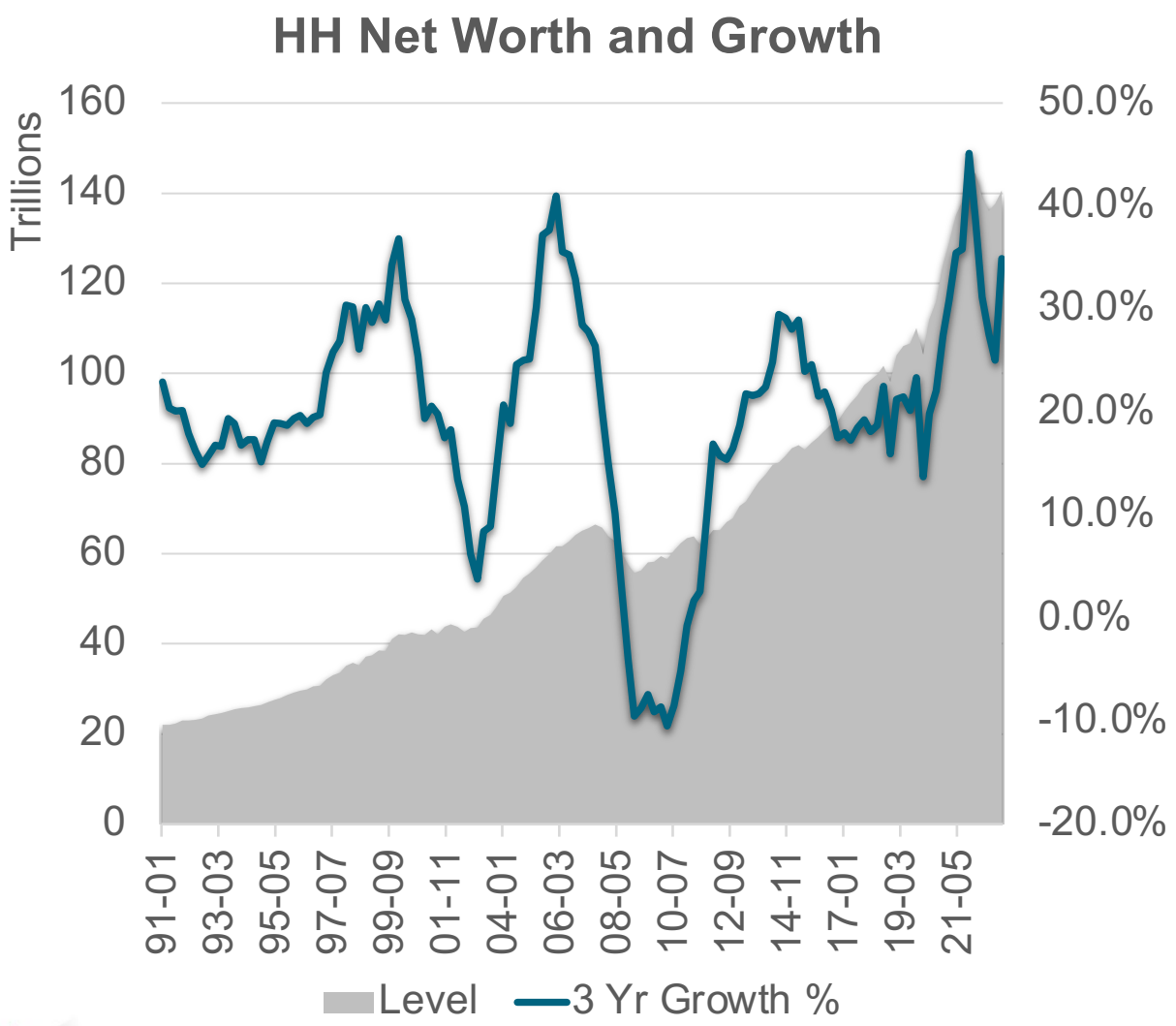


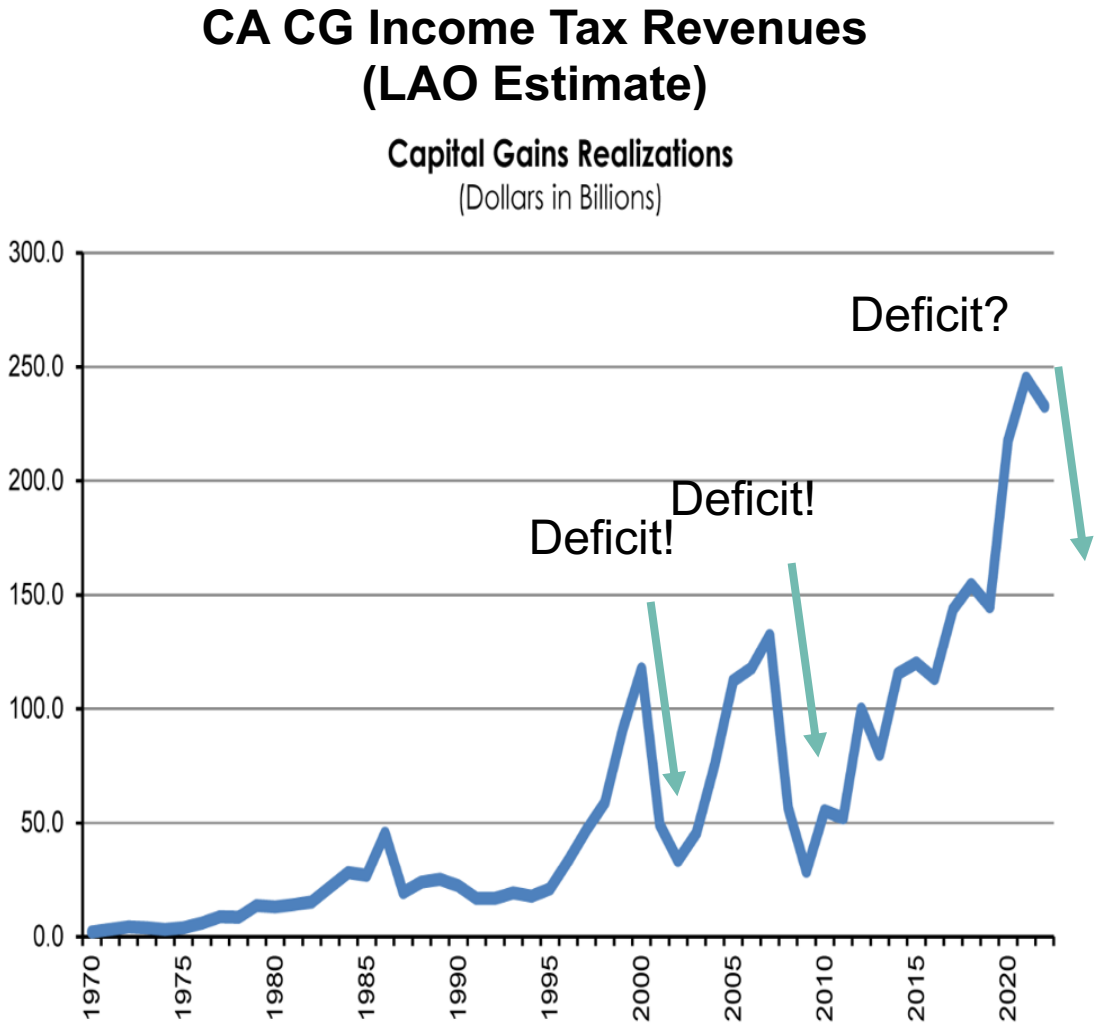
State Unemployment Up?





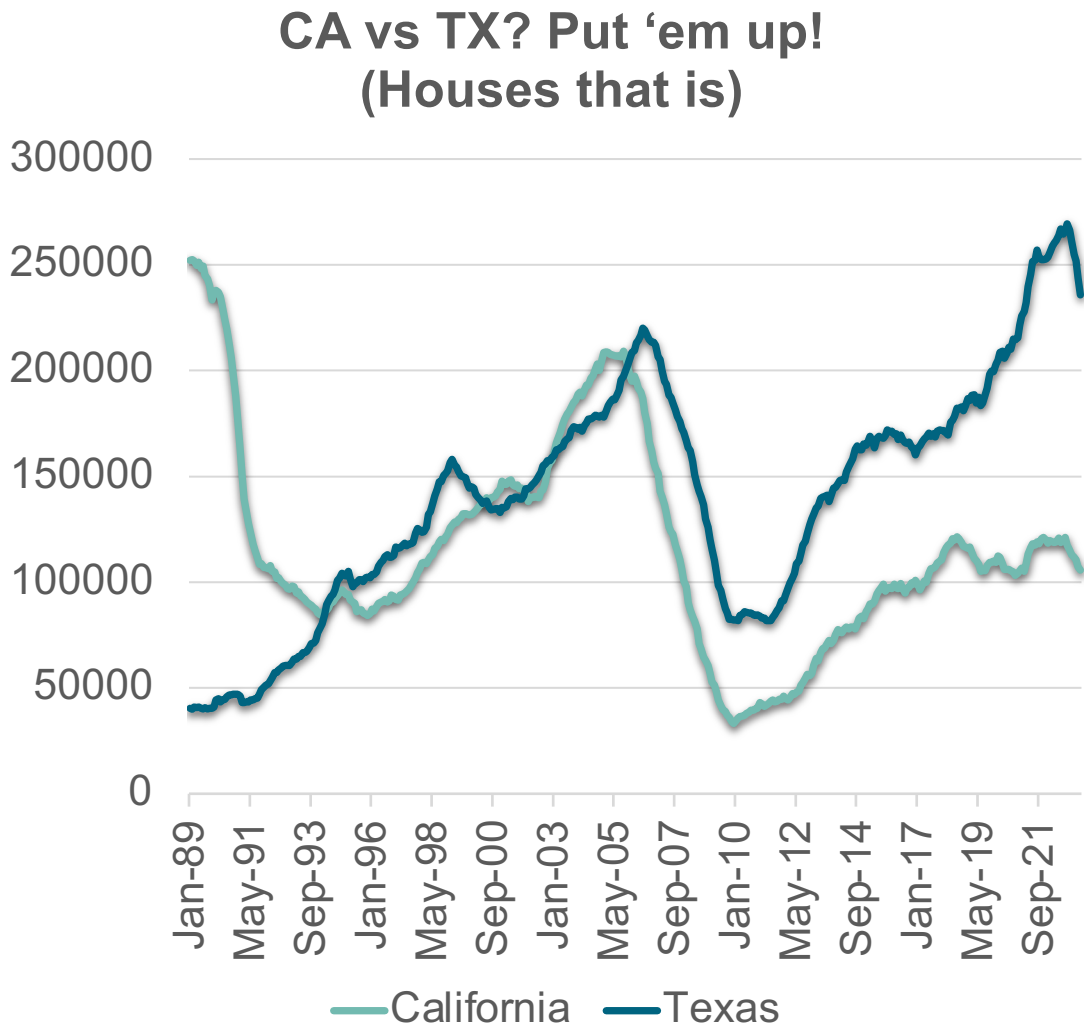
On Bubbles and Budgets!



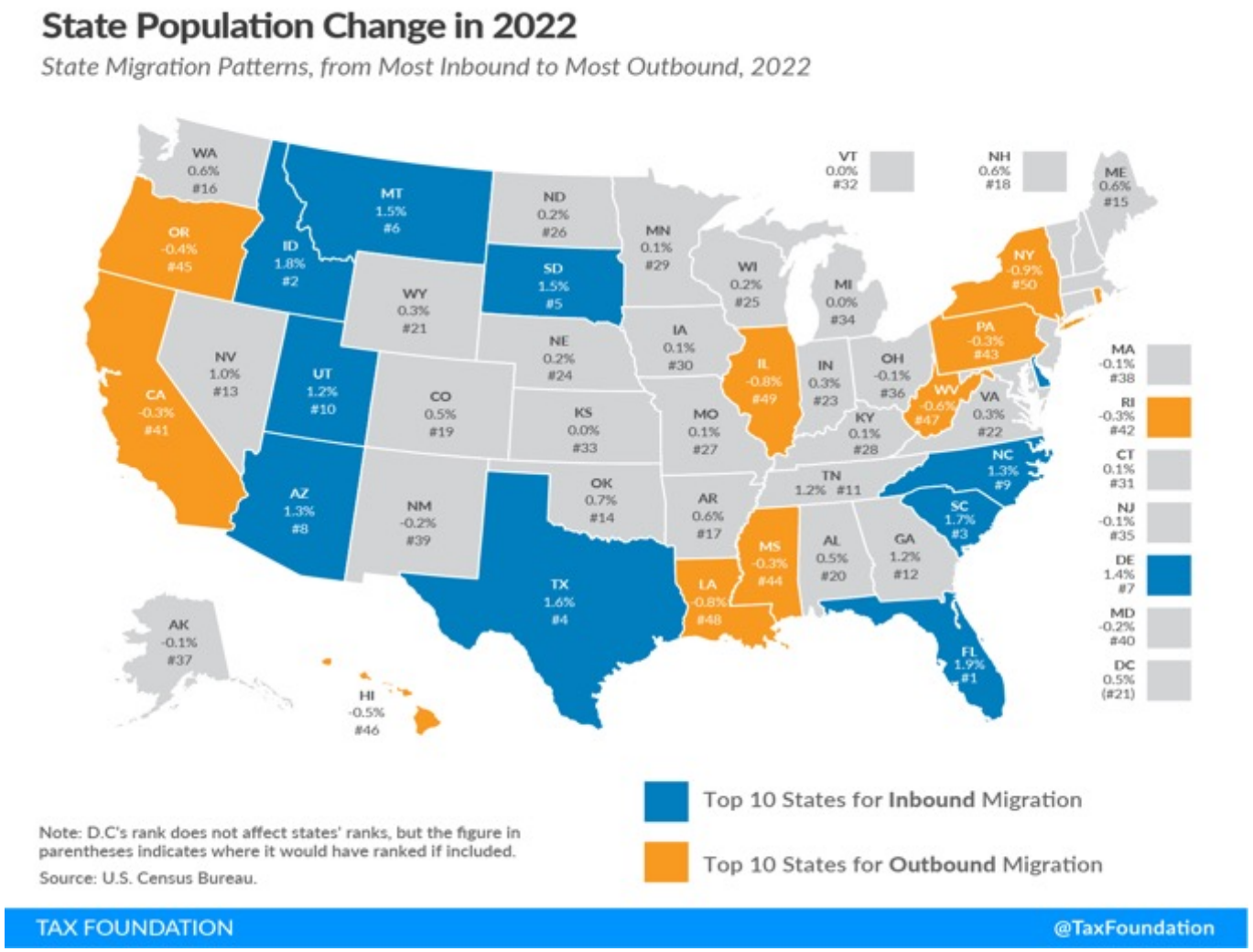


State Labor Supply & Housing

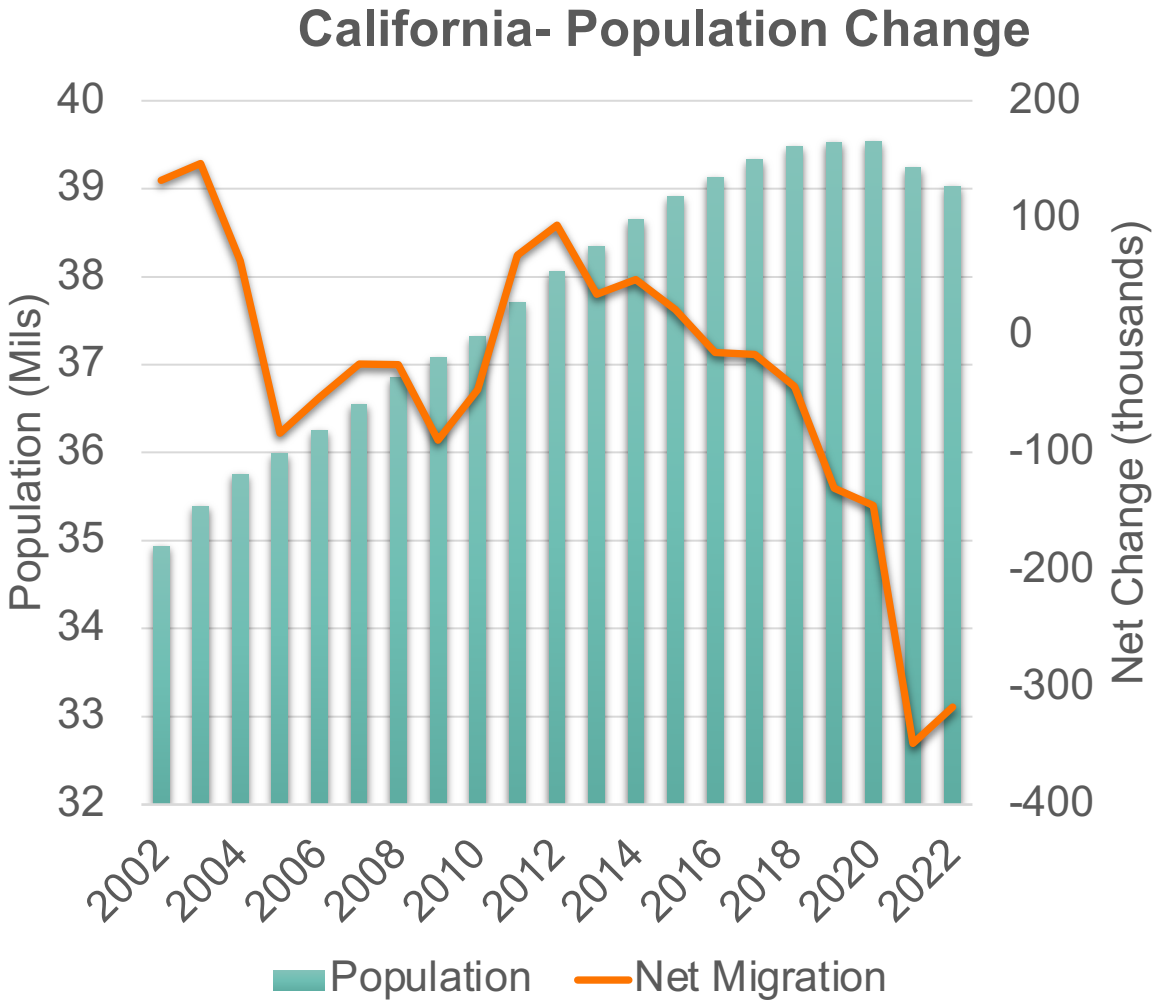
	02-12	12-22	Rank
Utah	14.3%	29.3%	1
Idaho	12.6%	23.1%	2
Arizona	13.8%	18.4%	3
Colorado	12.3%	16.4%	4
Texas	17.7%	16.0%	5
Florida	16.0%	15.3%	6
Washington	11.9%	15.0%	7
Nevada	20.5%	13.4%	8
Nebraska	6.3%	4.6%	24
Minnesota	2.7%	4.3%	25
California	7.2%	4.1%	26
Hawaii	8.1%	4.0%	27
New Jersey	5.3%	3.6%	28
Vermont	3.1%	-3.3%	48
Maine	3.3%	-3.7%	49
Wyoming	12.7%	-3.9%	50
Mississippi	3.1%	-6.0%	51

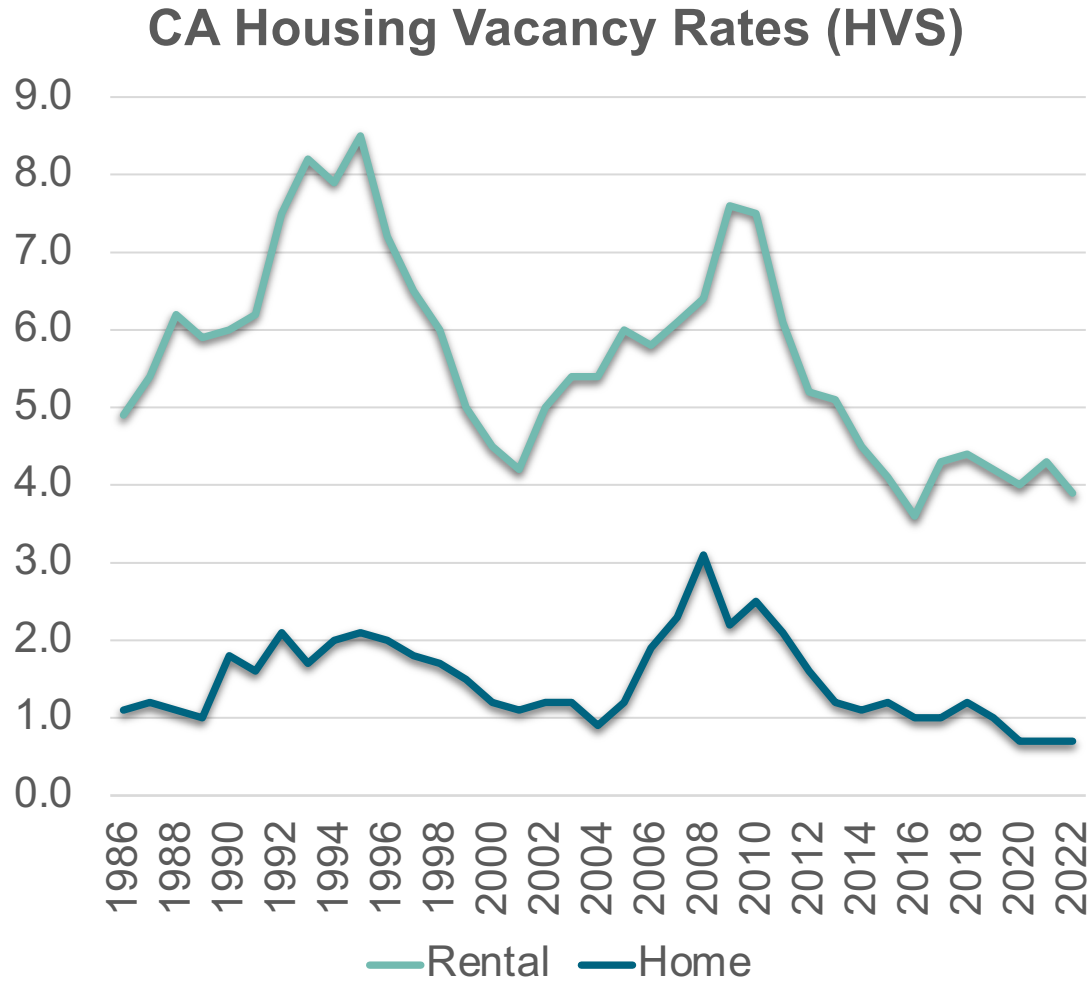


Population = Growth



Fleeing? Or being Pushed?

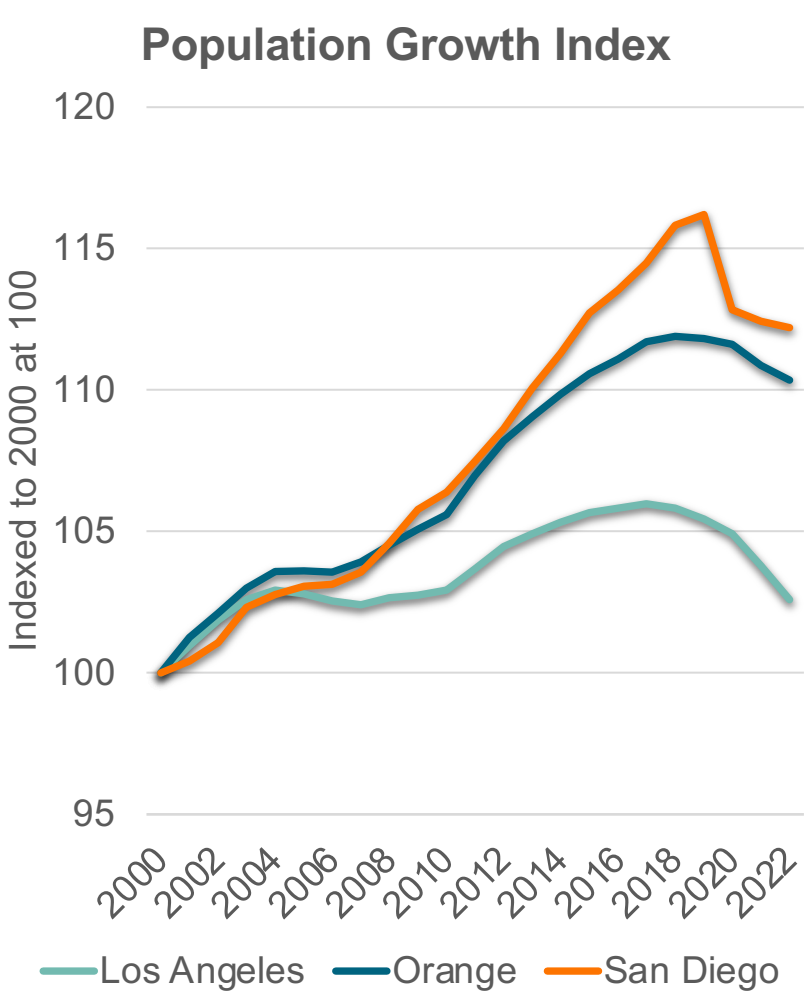


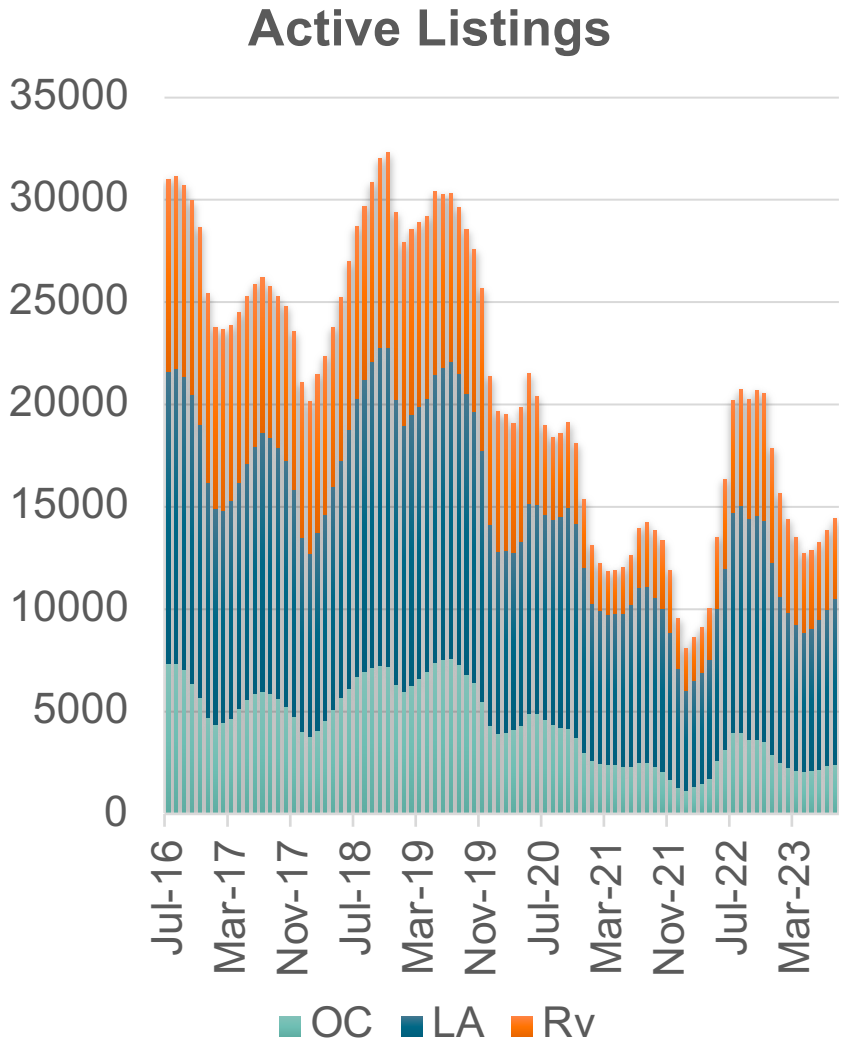


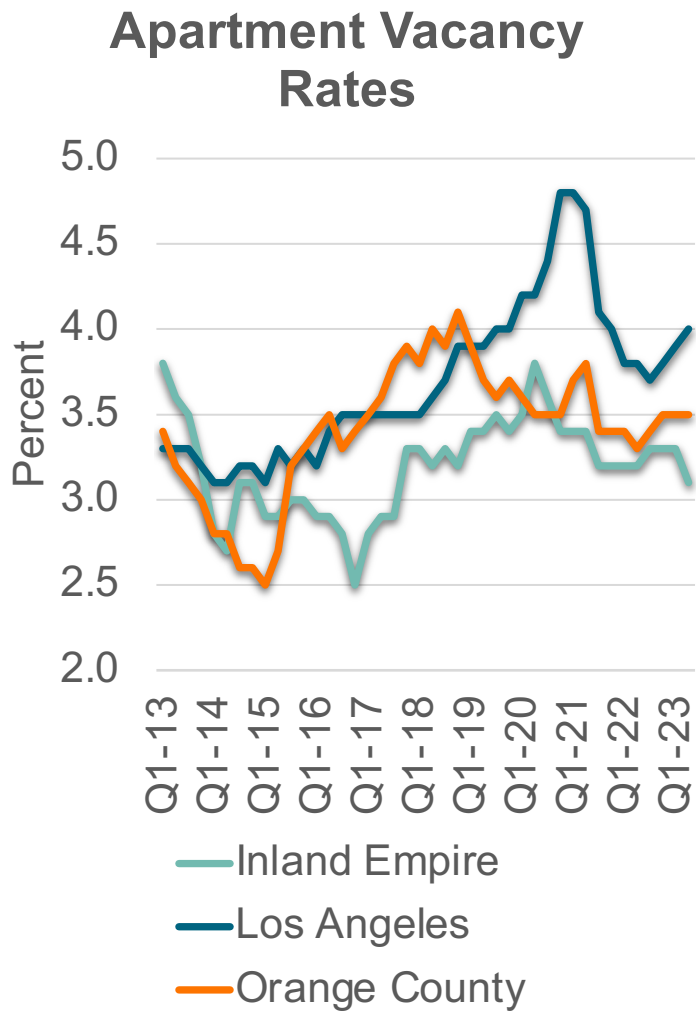
What is driving the problem?

	Population				Households		
	2015	2023			2015	2023	
Los Angeles	9,942,636	9,542,781	-4.0%		3,487,551	3,664,182	5.1%
Orange	3,093,821	3,085,670	-0.3%		1,069,646	1,149,943	7.5%
Riverside	2,282,072	2,399,217	5.1%		822,911	872,930	6.1%
San Bernardino	2,073,288	2,144,993	3.5%		709,385	747,011	5.3%
	Housing Vacancy				PPH		
	2015	2023			2015	2023	
Los Angeles	6.1%	5.2%	-0.9%		3.04	2.75	-9.5%
Orange	5.4%	5.1%	-0.3%		3.06	2.83	-7.5%
Riverside	13.6%	10.1%	-3.5%		3.21	3.06	-4.7%
San Bernardino	11.8%	8.8%	-3.1%		3.31	3.15	-5.0%

Local Dynamics

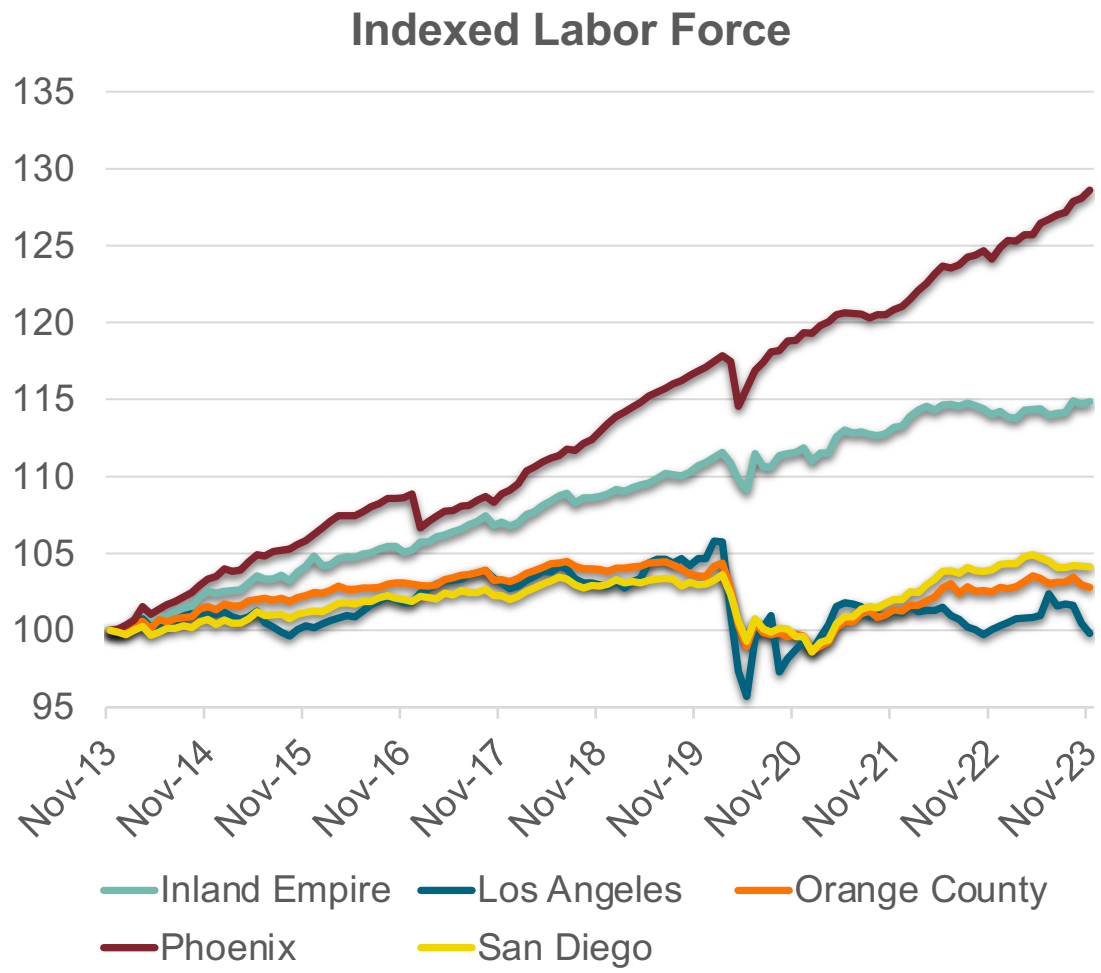




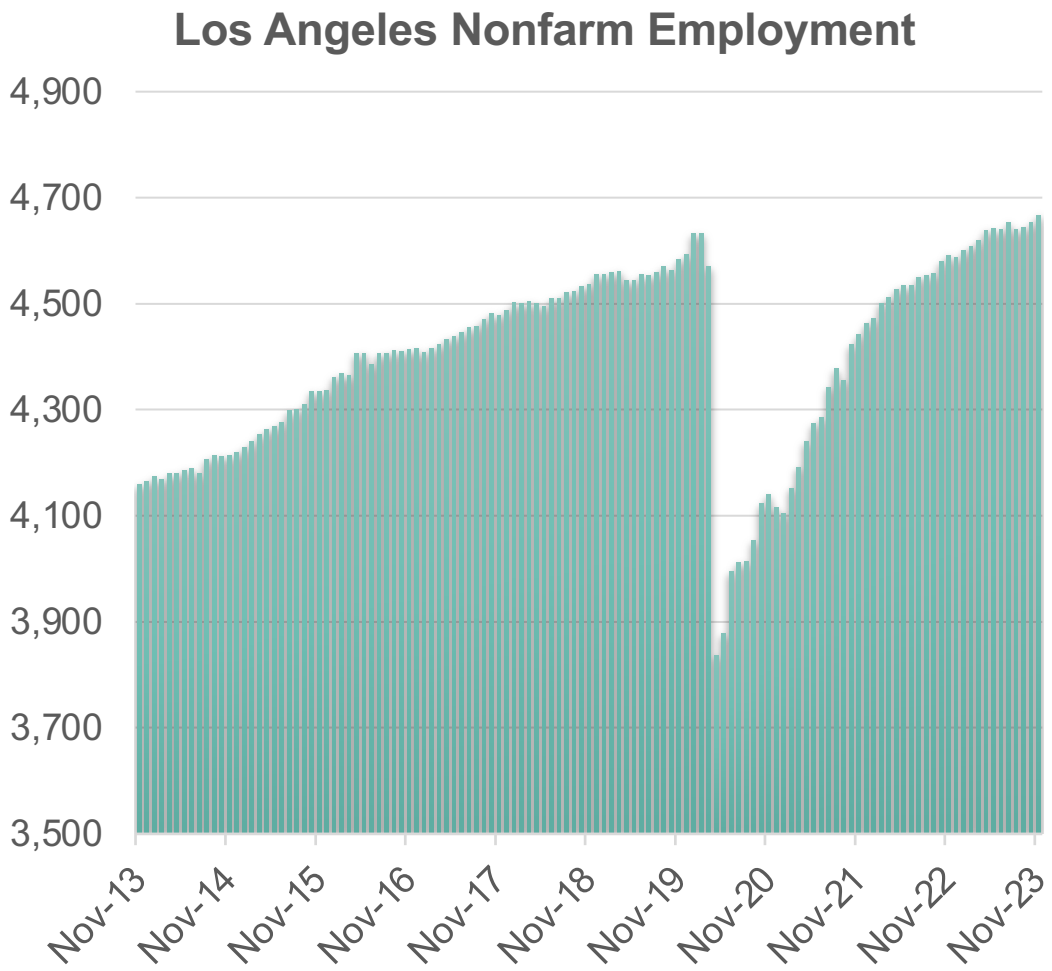


Labor Force

Location	Nov-23 LF (000s)	1-Year Chg. (%)	Chg. since Feb-20 (%)
Dallas	4,472.90	4.3	10.7
Phoenix	2,685.70	3.6	8.7
Houston	3,638.00	3.3	5.4
Seattle	2,314.00	3.2	5
Las Vegas	1,208.20	4.4	4.4
Denver	1,747.60	1.2	4.2
Inland Empire	2,169.40	0.7	2.9
Sacramento	1,138.30	0.8	2.5
San Diego	1,598.70	0.2	0.5
Orange County (MD)	1,597.10	0.3	-1.5
Oakland (MD)	1,383.20	0.4	-1.9
San Francisco (MD)	1,027.00	-0.4	-2.4
Los Angeles (MD)	4,941.20	-0.3	-5.9



Los Angeles Industry Employment

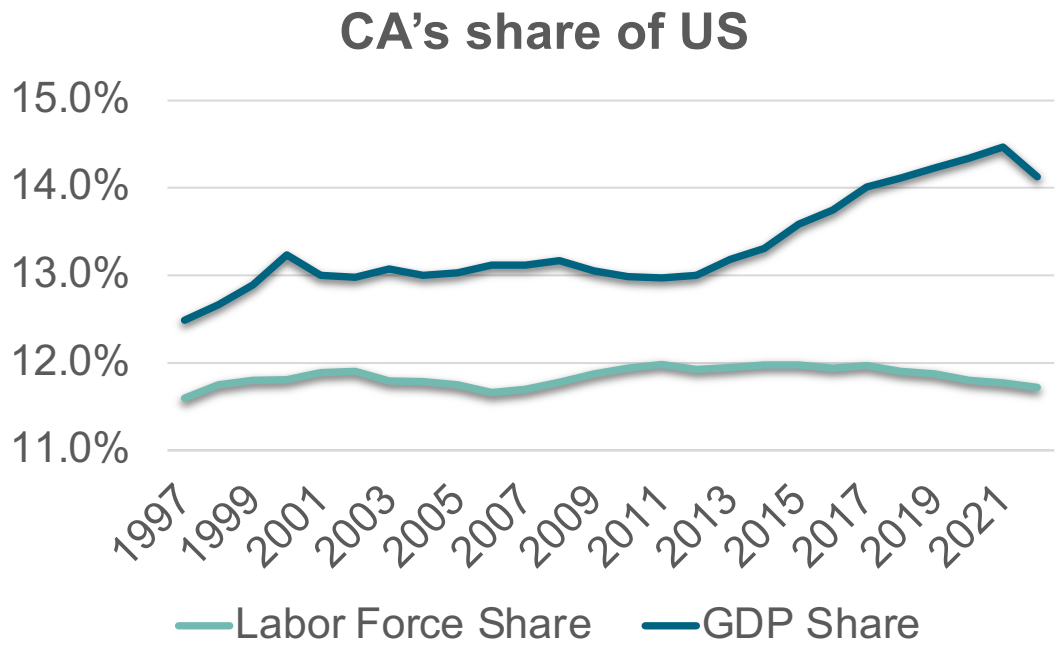


Los Angeles (MD) Industry	Nov-23 Emplt (000s)	1-Year Chg. (000s)	1-Year Chg. (%)	Chg. Since Feb-20 (%)	LQ
Total Nonfarm	4,667.1	75.2	1.6	0.7	1.0
Health Care	804.9	46.9	6.2	10.8	1.1
Leisure & Hospitality	557.3	33.4	6.4	0.0	1.0
Education	147.0	8.9	6.4	7.8	1.4
Retail Trade	415.0	7.8	1.9	0.5	1.0
Prof Sci Tech	334.1	7.8	2.4	7.2	0.9
Logistics	235.8	7.6	3.3	9.5	1.1
Construction	154.2	3.9	2.6	-0.8	0.6
Other Services	158.9	3.2	2.1	-2.8	1.0
Financial Activities	219.3	2.4	1.1	-2.9	1.0
Government	577.6	1.5	0.3	-3.0	0.9
Management	62.5	0.8	1.2	-5.4	1.0
Natural Resources	1.6	0.0	-0.1	-13.4	0.3
Wholesale Trade	197.7	-5.3	-2.6	-10.5	1.2
Manufacturing	320.3	-6.0	-1.8	-5.8	0.9
Admin Support	277.3	-14.3	-4.9	-0.1	0.9
Information	203.6	-23.3	-10.3	-10.1	1.4

California Skill Shifts

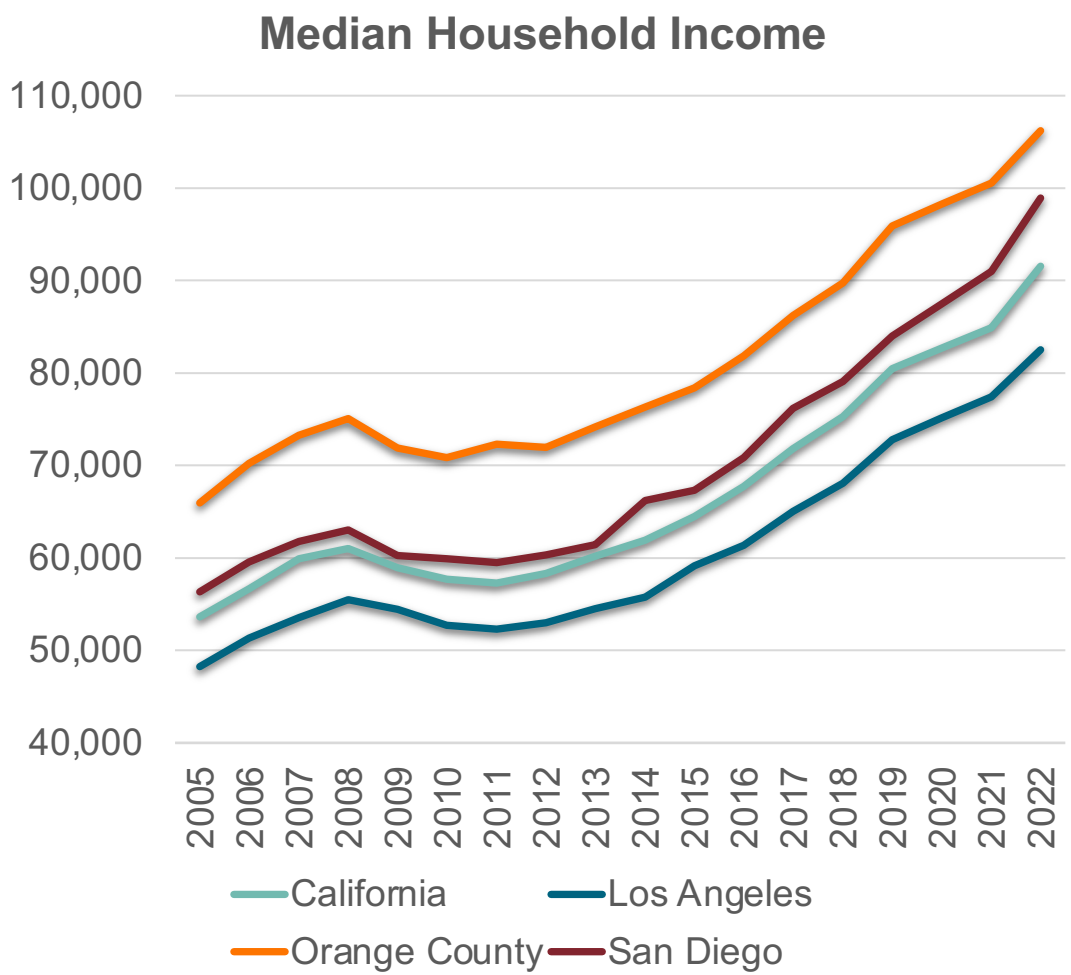
Net Migration by Educational Attainment (Total from 2019-2022)

Education	AZ	CA	CO
Net Migration	**109,116**	**-71,099**	**109,061**
Less Than HS	-64,750	-185,830	-17,652
HS Grad	32,261	-39,856	-13,481
Some College	-32,376	-352,870	-39,336
BA	101,014	166,445	120,066
Grad	72,967	341,012	59,464



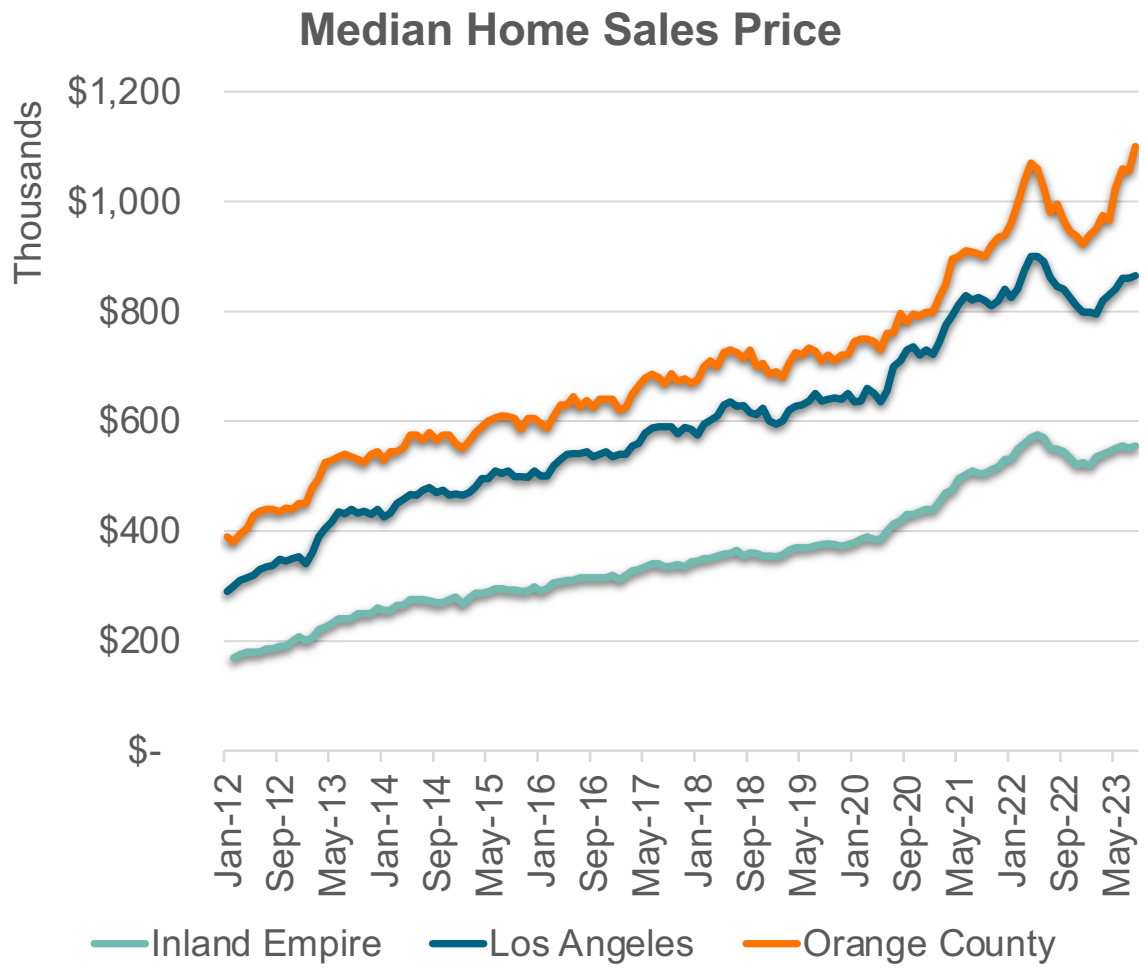
Change LF by Edu	Los Angeles		Orange	
	2022	Change 12-22	2022	Change 12-22
< HS	19.4%	-3.4%	13.5%	-2.5%
HS	20.5%	-0.1%	17.2%	-0.7%
SC	24.4%	-2.1%	25.6%	-3.2%
Bach	22.7%	2.9%	27.5%	3.6%
Grad/Prof	12.9%	2.7%	16.2%	2.9%

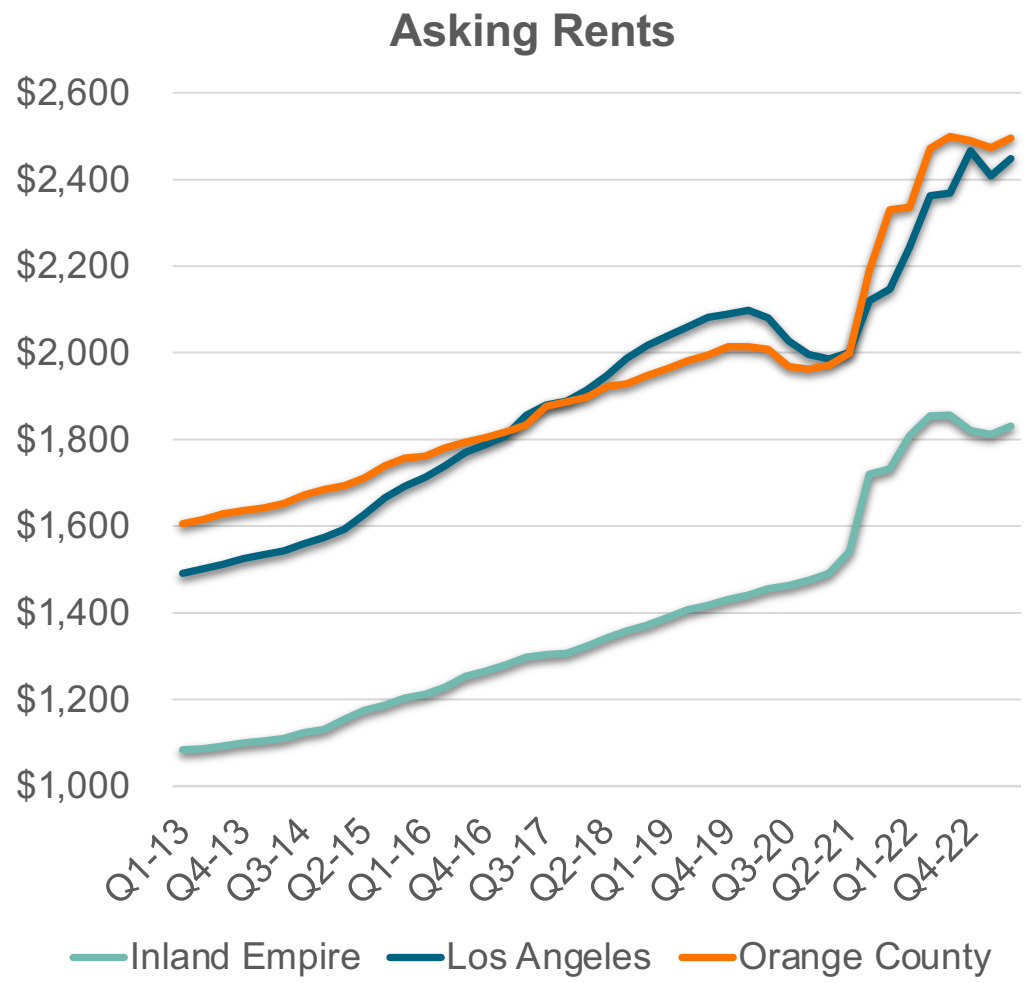
Median Household Income



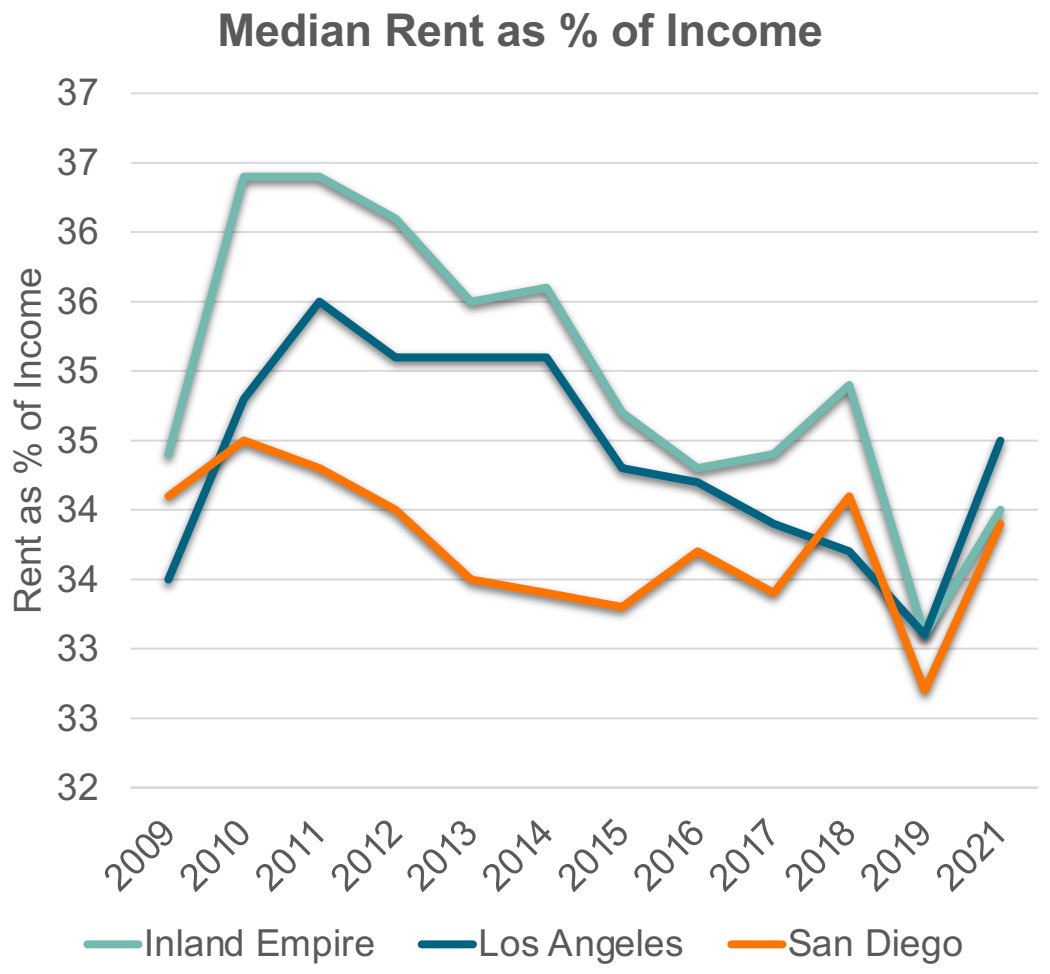
Location	Median Income 2022 ($)	5-Year Growth (%)
Los Angeles County	82,516	26.9
South Gate	70,939	40.9
Whittier	91,457	37.5
Compton	68,355	35.0
Long Beach	80,493	32.9
Lynwood	64,481	32.1
Lakewood	109,309	30.9
Norwalk	94,851	26.9
Bellflower	74,131	23.1
Downey	85,089	17.9

Housing Costs



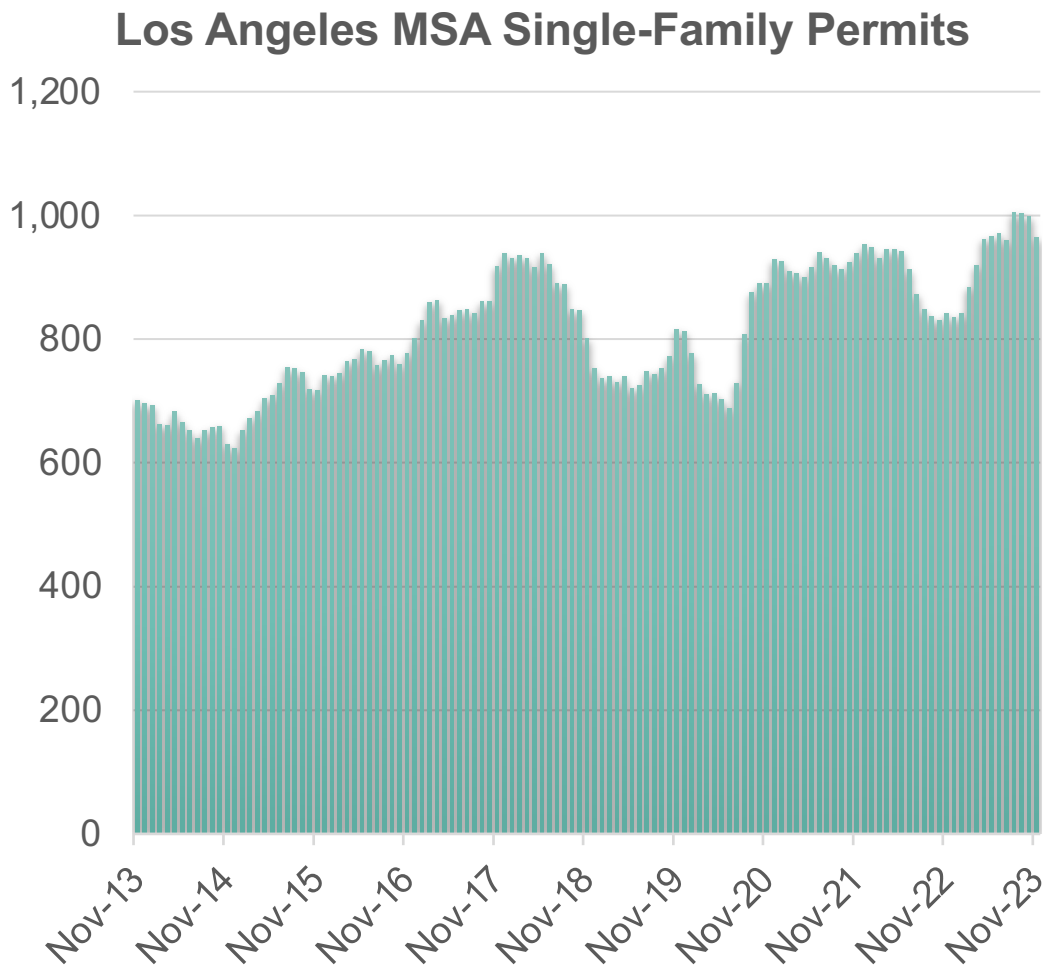


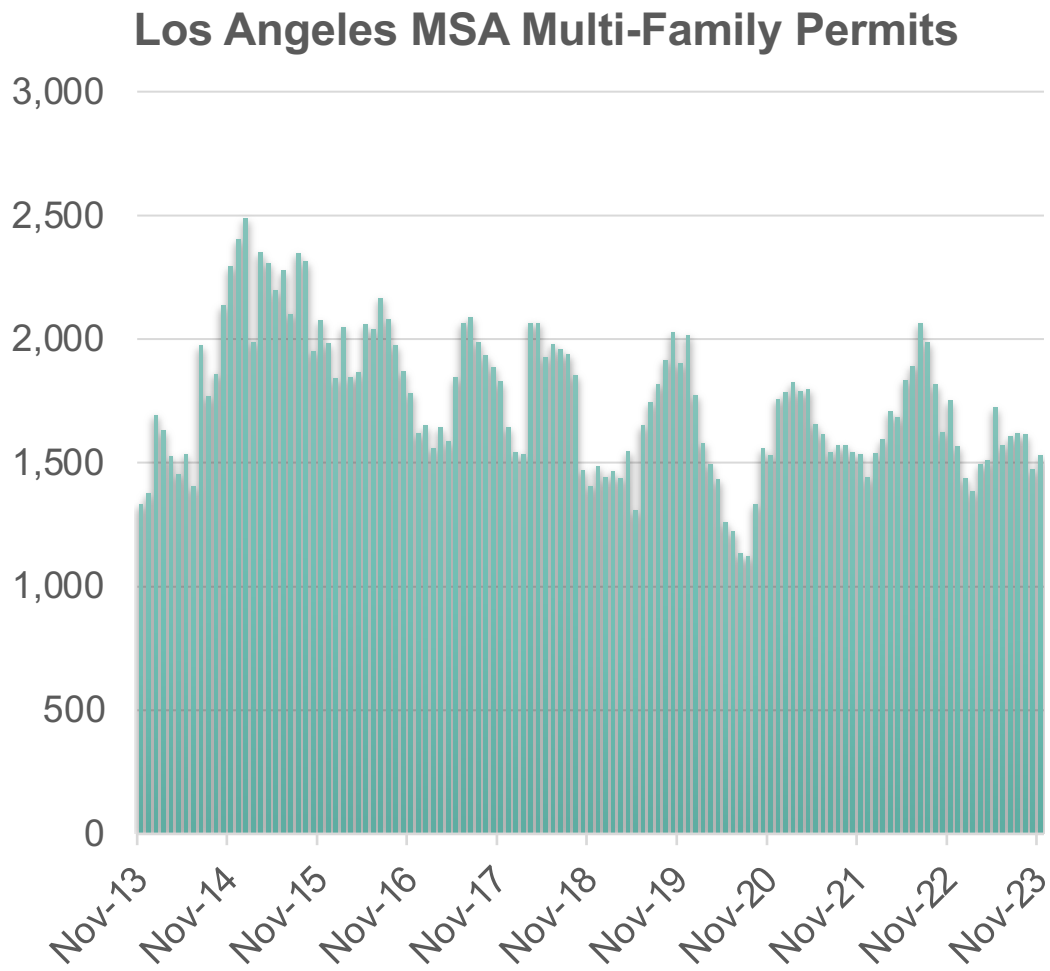
Supply, not affordability…



Share Cost Burdened: Renters	2017	2022
Dallas	46%	53%
Fresno	56%	56%
Inland Empire	59%	60%
Las Vegas	49%	58%
Los Angeles MSA	58%	58%
Phoenix	47%	54%
Salt Lake City	44%	49%
San Diego	57%	58%
Seattle	48%	50%

Single-Family Permits



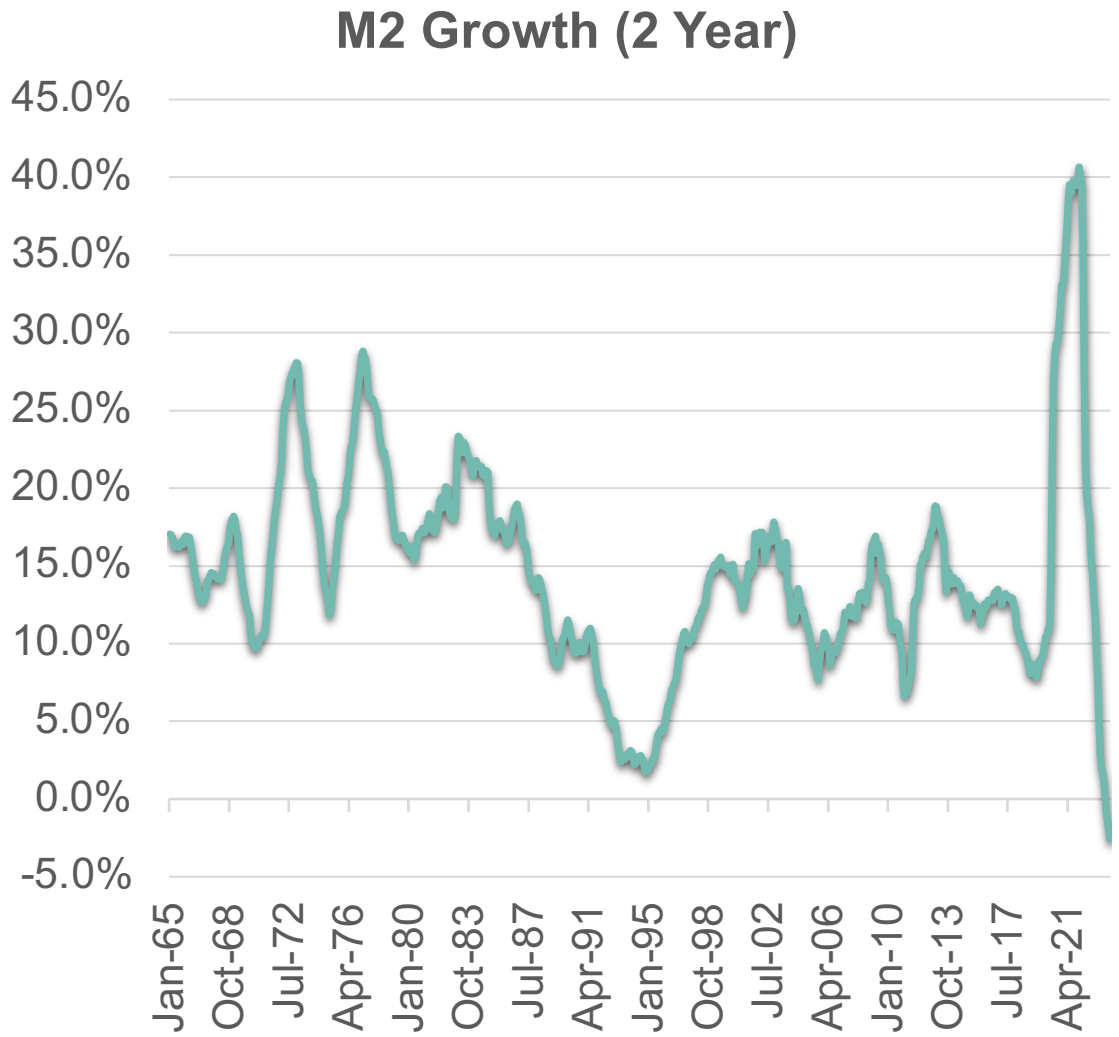


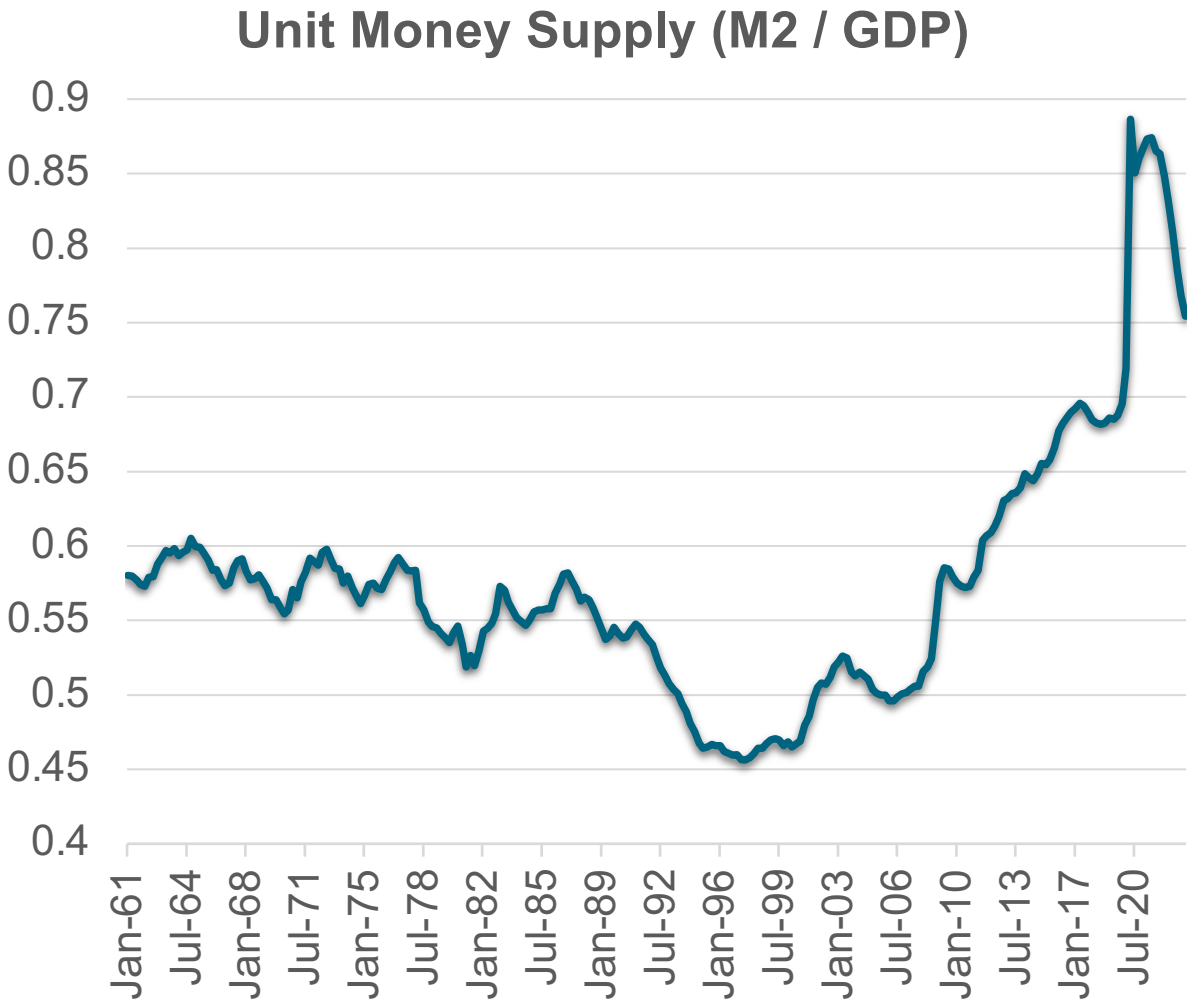
Where is the Fed?

The Federal Reserve Narrative

- US inflation due to some exogenous shock
- Inflation is now being driven by inflation expectations
- Inflation is causing substantial harm to American households
- The Fed must fight inflation and it is worth the loss of some jobs / higher unemployment

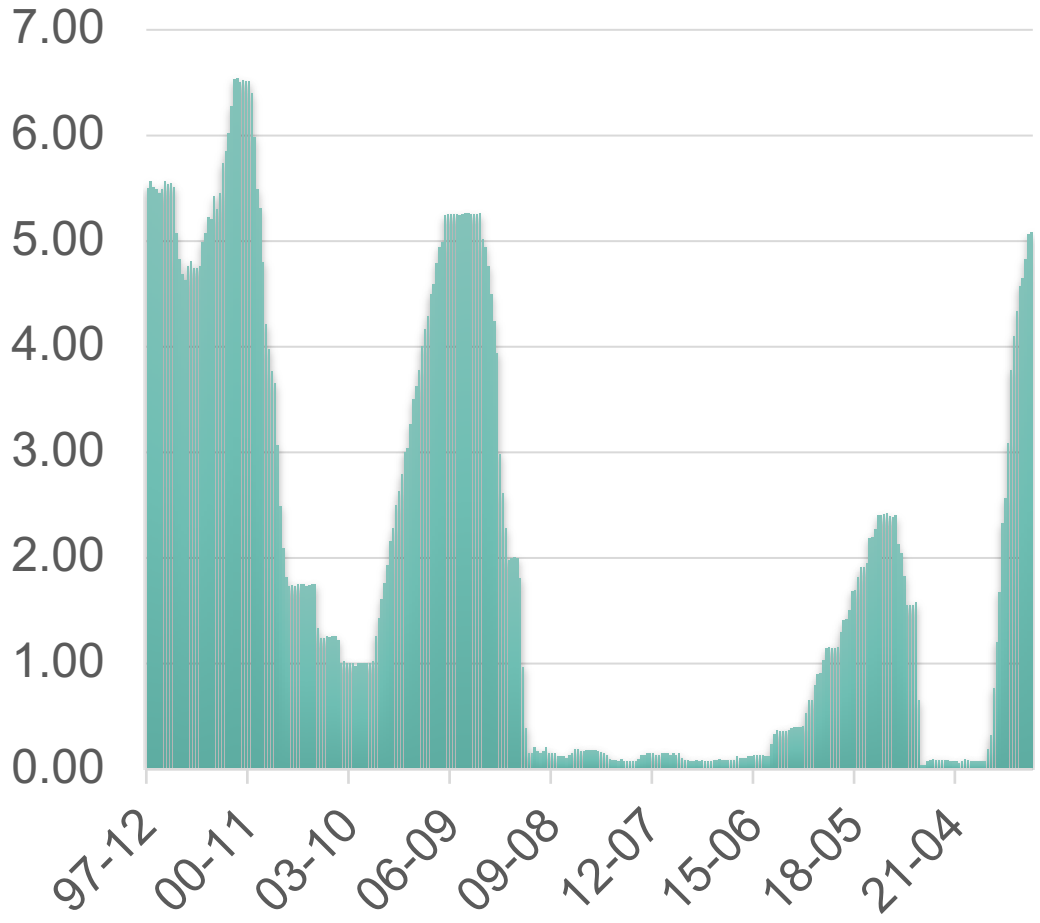
How far can inflation go?



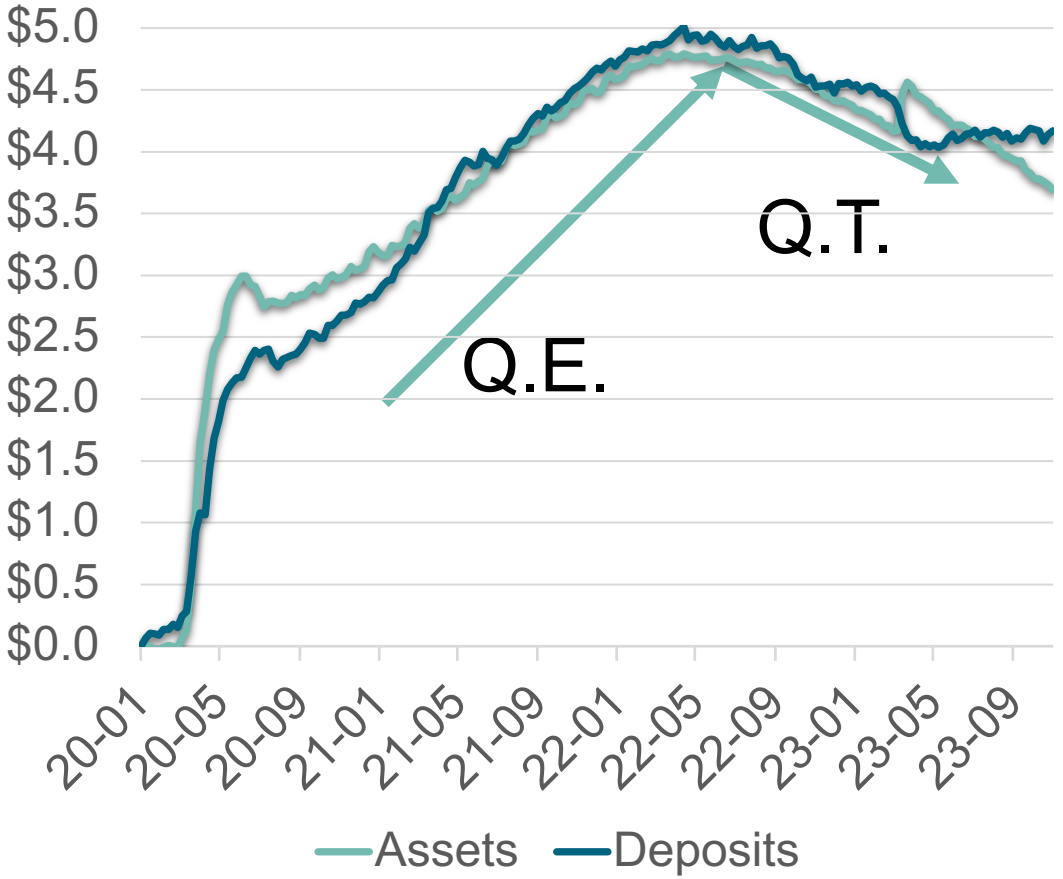


The Fed Response

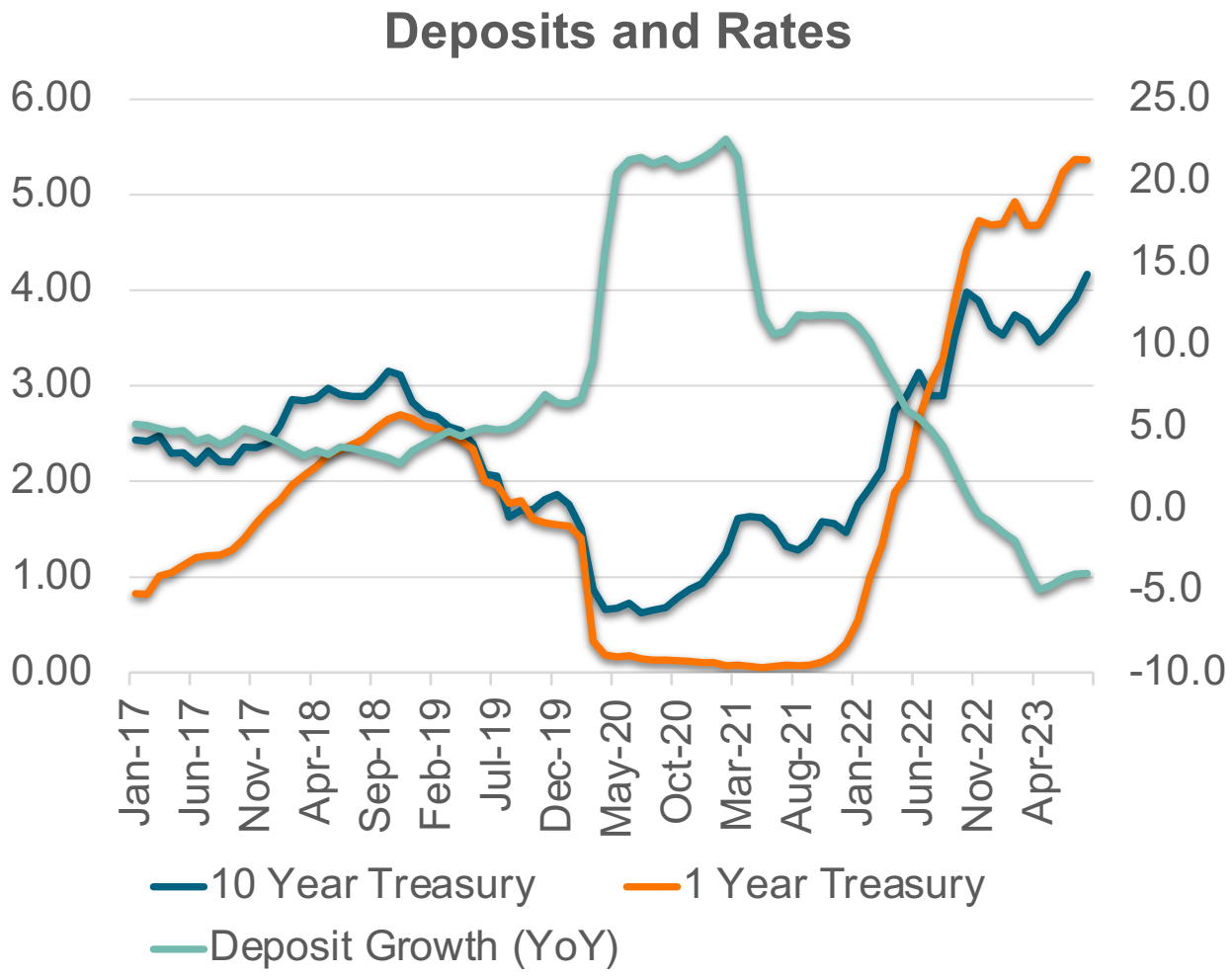
Stage 1: Federal Funds Rate



Stage 2: Quantitative Tightening (Cumulative Trillions)



Bank Failures? Forced to Buy High, Sell Low



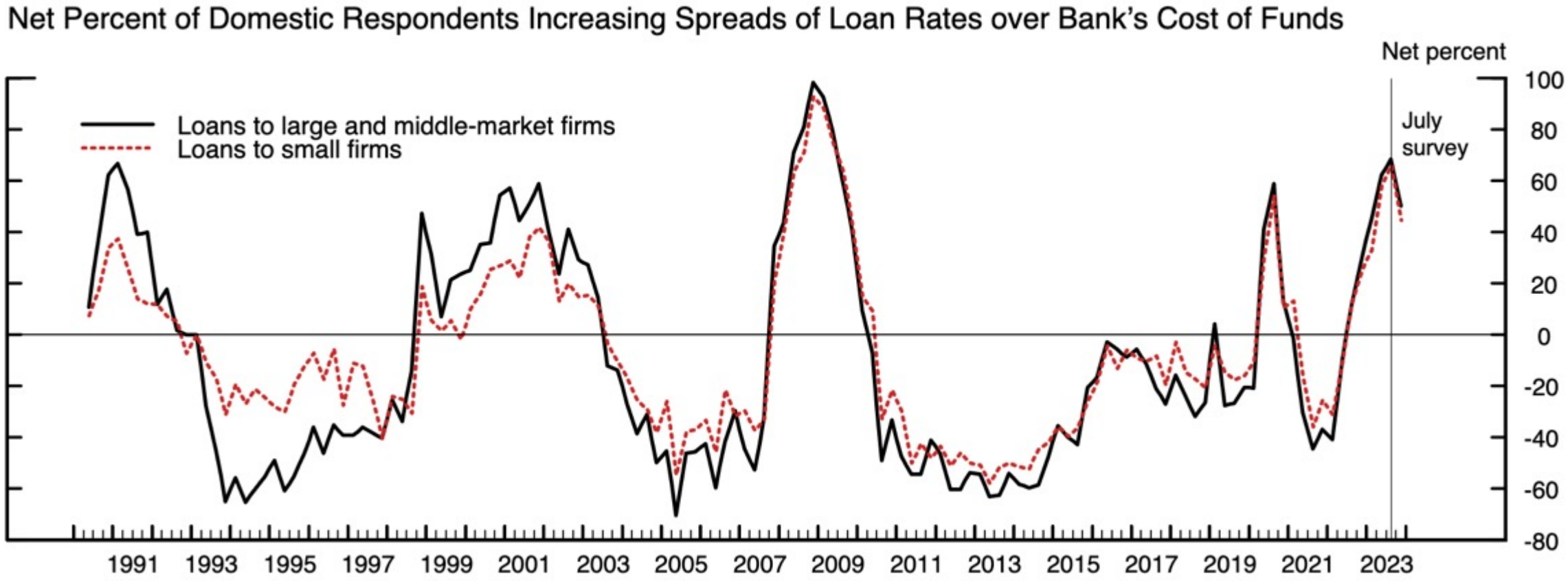
- *Conducting the nation's monetary policy … in pursuit of full employment and stable prices.*
- *Supervising and regulating banks … to ensure the safety and soundness of the nation's banking and financial system.*

Error #1: Panic over full employment has negatively impacted price stability

Error #2: Panic over price stability has negatively impacted the credit system

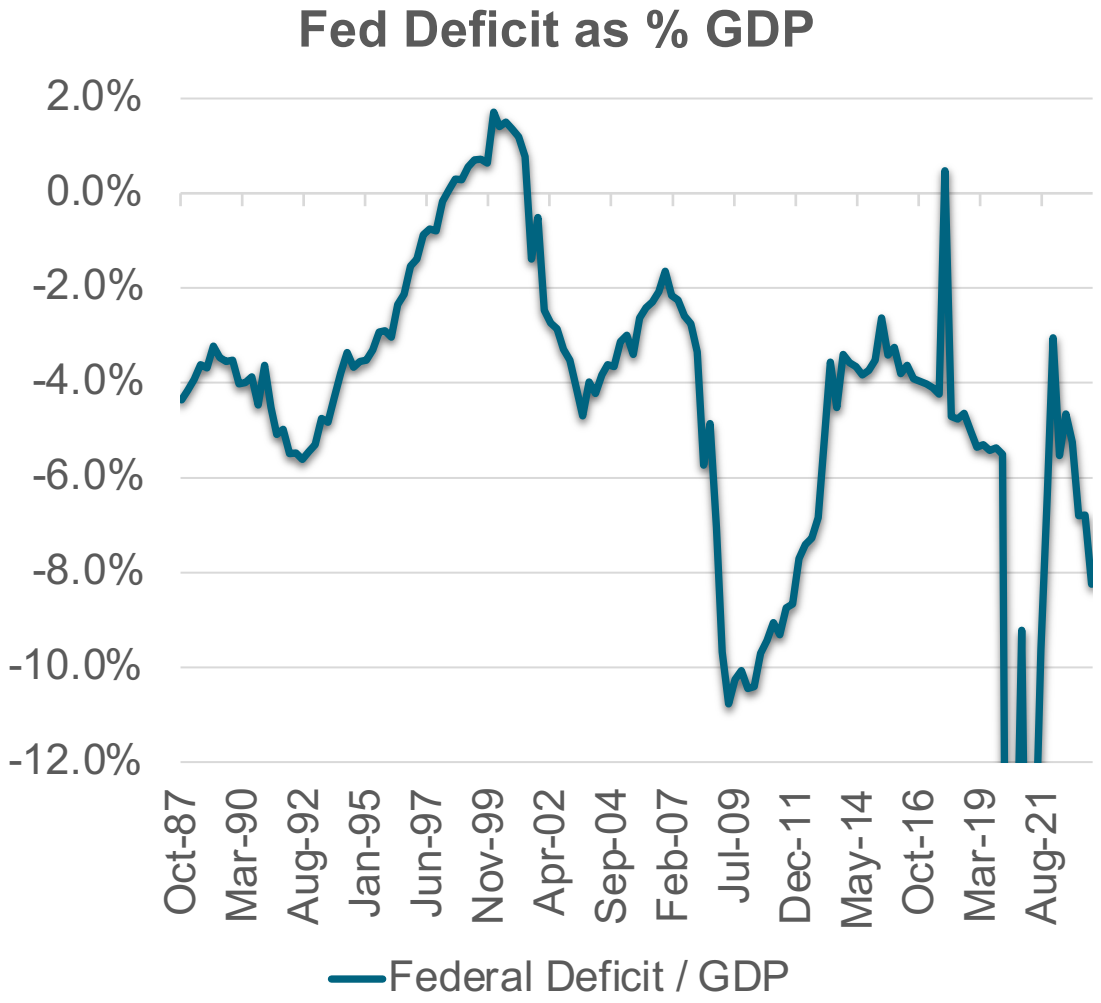
Credit shortage issues

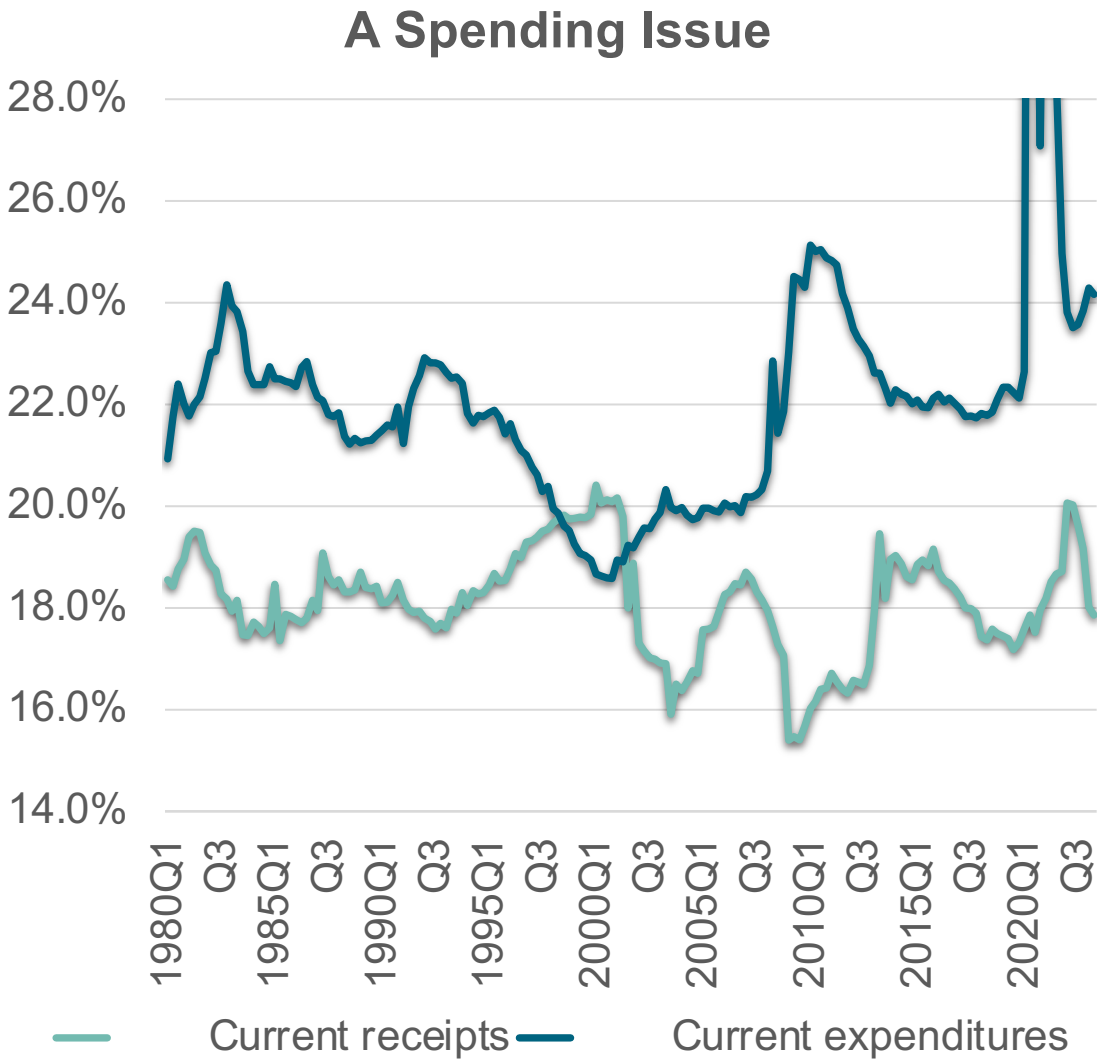
Interest Rates



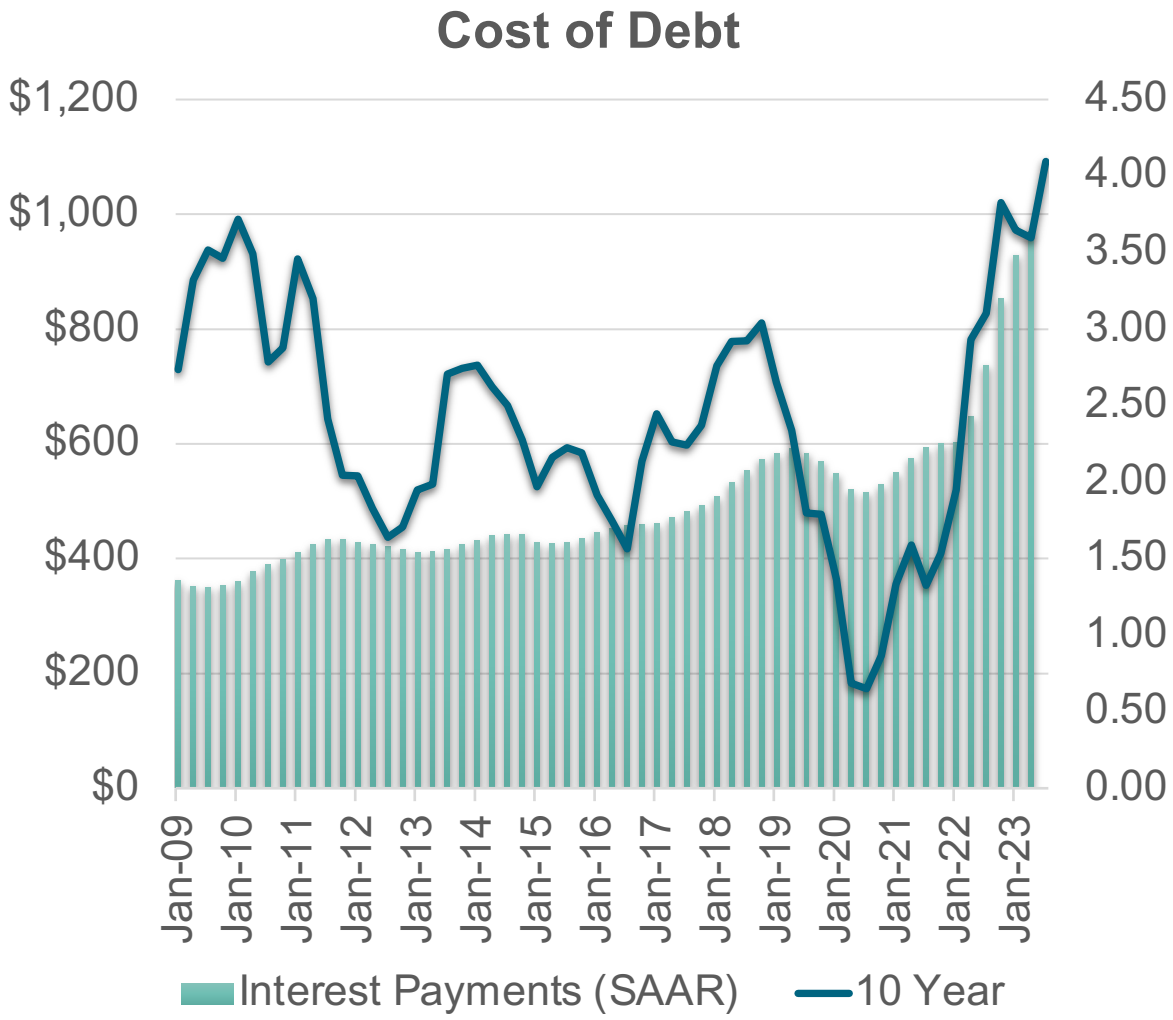
10 Year Treas 2 Year Treas 30 Yr FR Mortgage

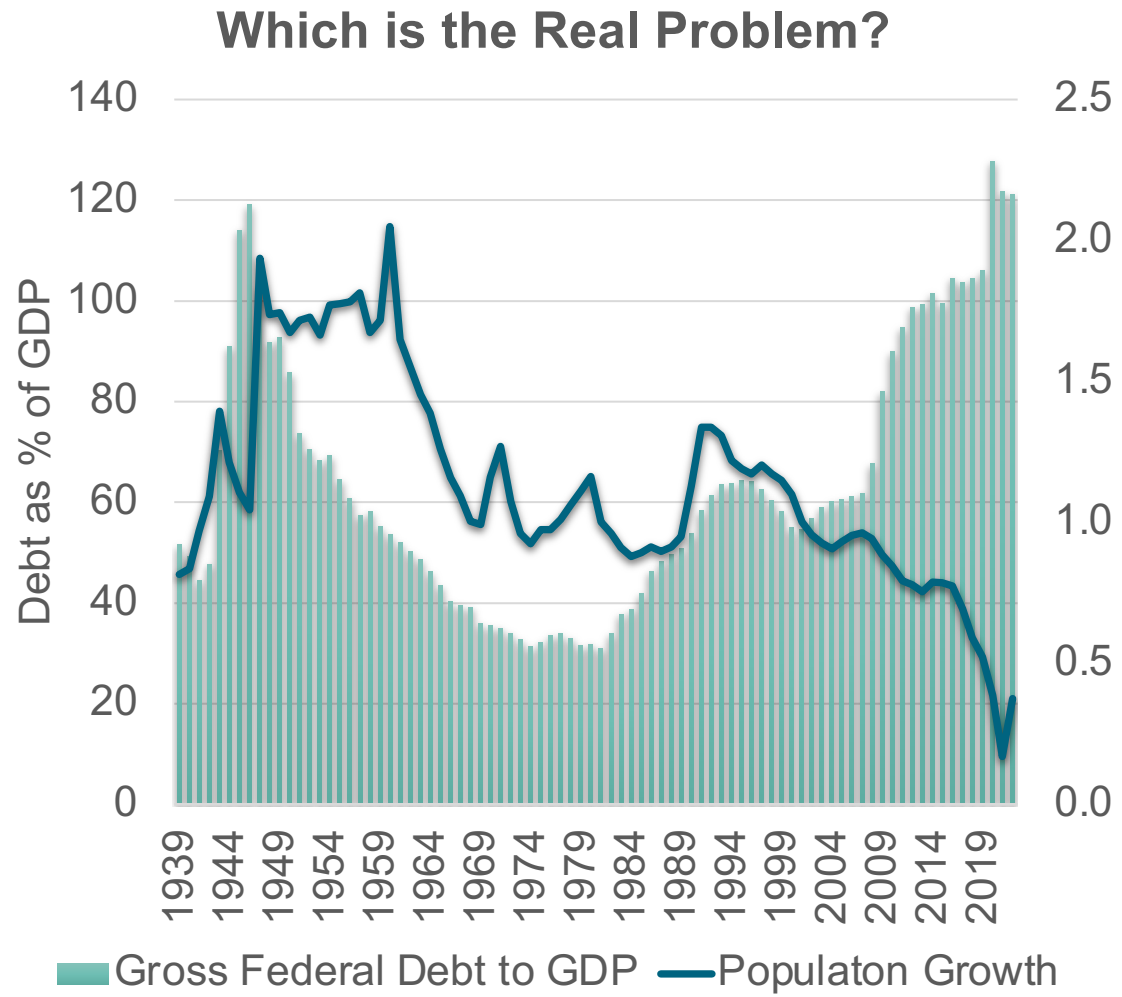
The Fed on the Brake, Congress on the Gas



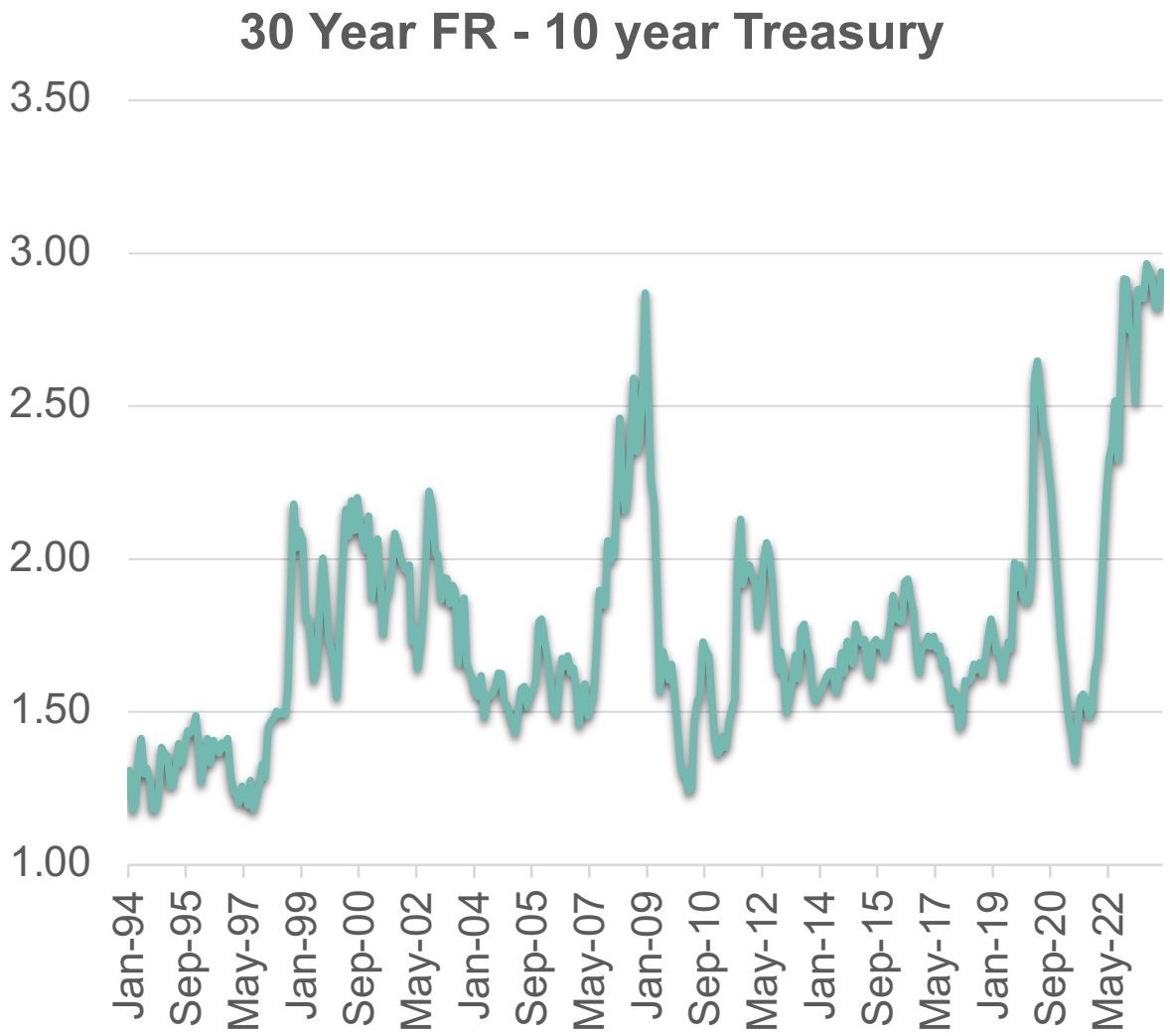


Feedback Effects





Mortgage rates: higher longer



1. Interest rates on Treasury bonds with maturities of less than 10 years are higher than rates on 10-year Treasury bonds

2.Mortgage prepayment risk has increased

3.Reduced demand for financial instruments backed by mortgages

Out of the Woods?

We were never actually in the woods

- Household finances, consumer demand driving the economy
- Economic indicators remain solid, growth to continue
- Fed will likely back off some

Headwinds will intensify

- Inflation will stay above target
- LR Rates will stay higher longer
- Public deficits are unsustainable
- Asset prices too high
- Economic growth to slow—but no recession

The big issue: Narratives

- Labor supply not consumer demand
- Inflation is not a problem, the Fed is
- Government deficits are going to have to be dealt with

2024 Forecast Highlights

- GDP Growth 1.7%
- Unemployment Rate: 3.9%

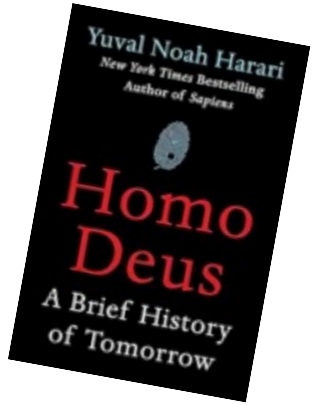
- 10 Year Treasury: 4.9%
- 30 Year FR Mortgage: 8.1%

- HPI Forecast: 1.7%
- Housing Starts: 1.42m

Sticky Narratives

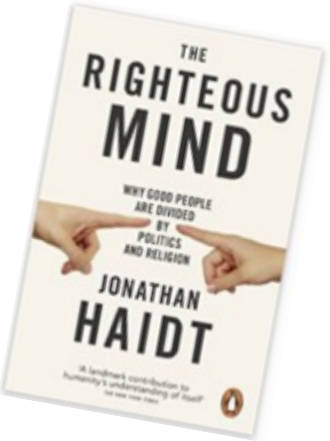
“Sapiens rule the world because only they can weave an intersubjective web of meaning: a web of laws, forces, entities and places that exist purely in their common imagination.

— Yuval Noah Harari, *Homo Deus: A Brief History of Tomorrow*



“People can believe pretty much whatever they want to believe about moral and political issues, as long as some other people near them believe it, so you have to focus on indirect methods to change what people want to believe.

— Jonathan Haidt, *The Righteous Mind: Why Good People are Divided by Politics and Religion*



Thank You!

BEACON ECONOMICS

Sources

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U.S. Bureau of Economic Analysis
U.S. Census Bureau

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