

18th Annual Real Estate Forecast

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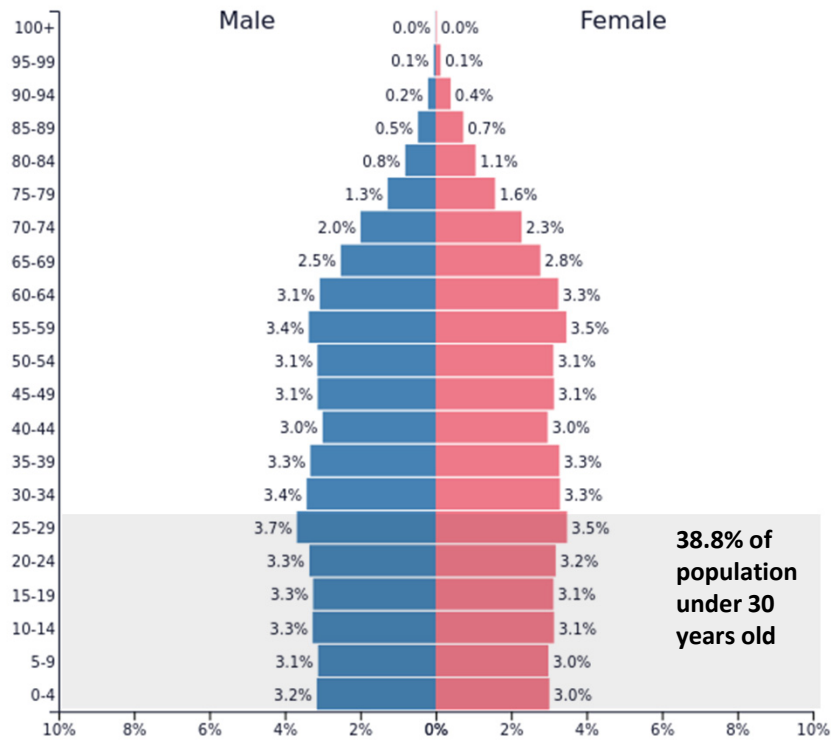
OLD NATIONALSM
Wealth Management

2019 Big Picture Themes

- **We live in a Globally Integrated Economy**

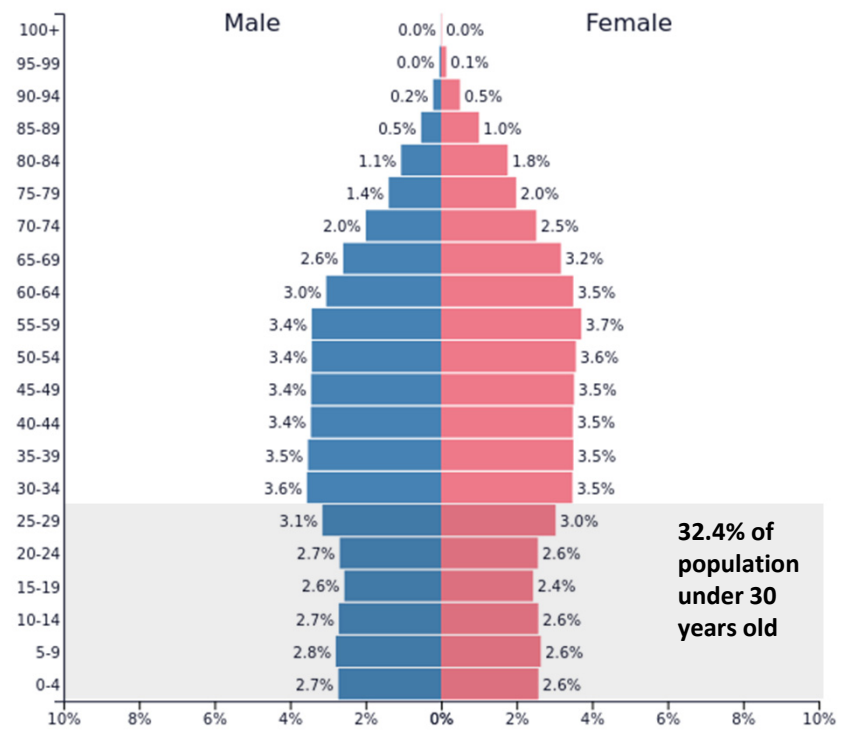


Europe's population is aging rapidly and will begin to decline after 2020



PopulationPyramid.net

United States of America - 2019
Population: 331,195,364



PopulationPyramid.net

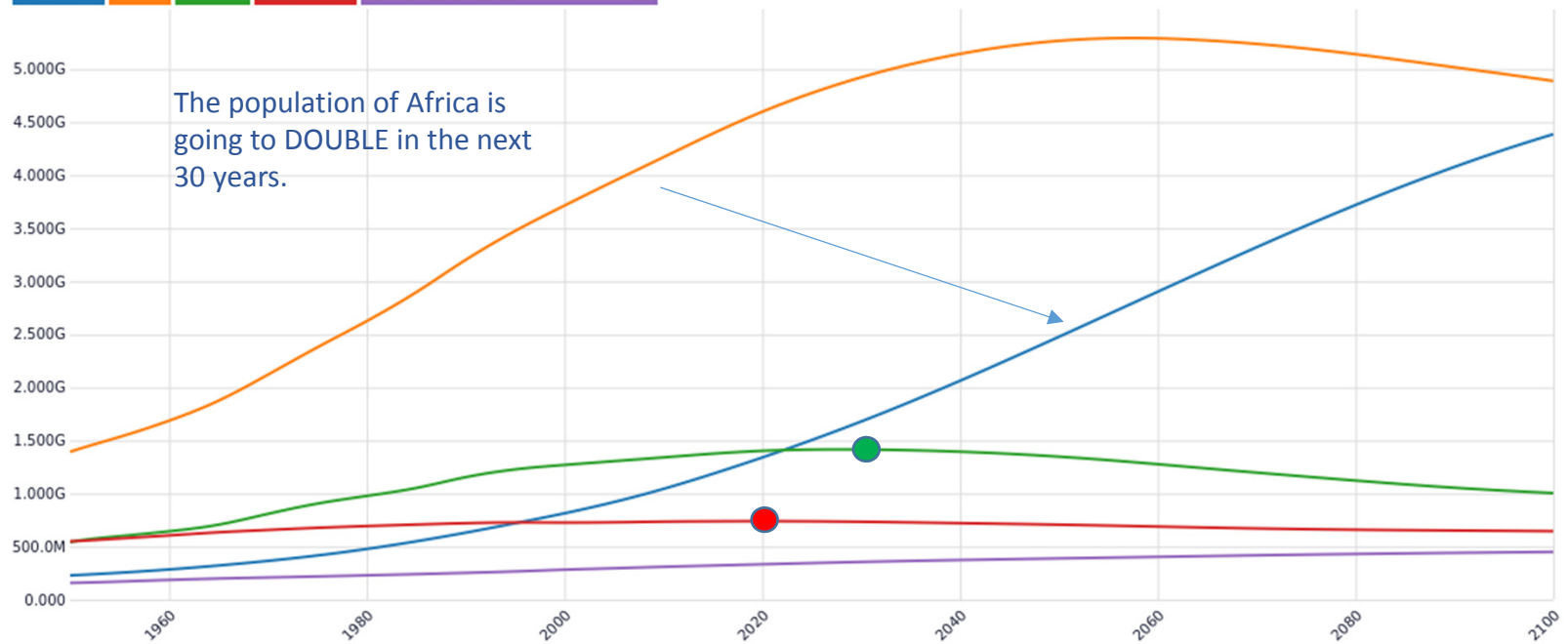
EUROPE - 2019
Population: 739,675,900



2019 Big Picture Themes

Population projections (1950-2100)

AFRICA ASIA China EUROPE United States of America



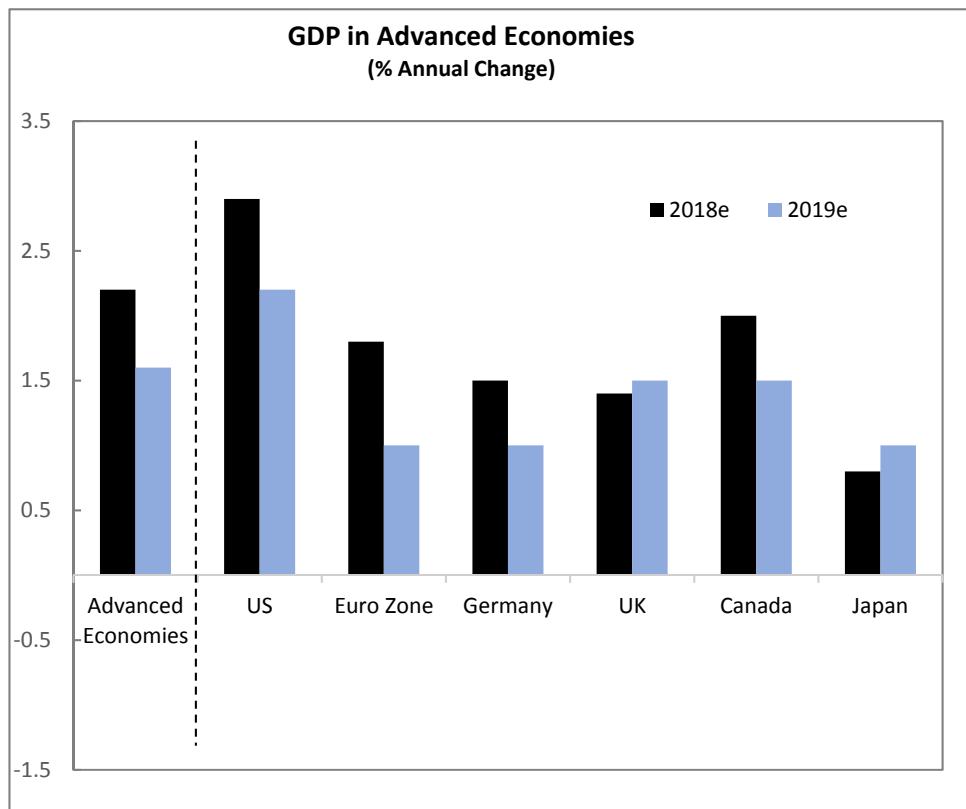
● Europe's population starts declining in 2020

● China's population starts declining in 2030

PopulationPyramid.net



Advanced Economies



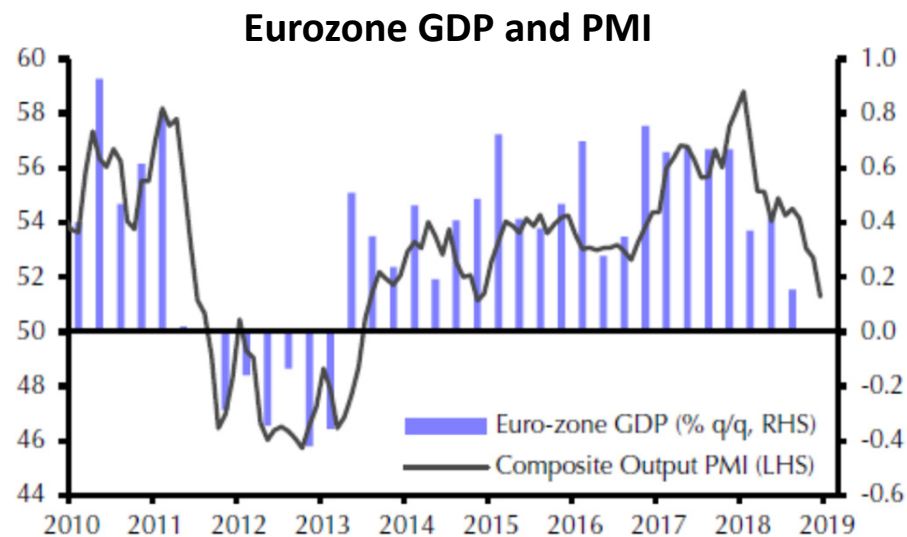
- Global growth is slowing especially in the Euro-zone and China, and the US is about to follow.
- Decent consumption growth should prevent a sharp slowdown in GDP growth.
- Labor markets will remain tight, while wages grow at a steady, unalarming pace.
- With limited upside risk to core inflation, major central banks will not tighten for long, if at all.
- Fiscal policy will become less supportive as last year's stimulus fades.



2019 Big Picture Themes

Europe

- Eurozone GDP growth will slow in 2019 to about 1% from 1.5% in 2018.
- Germany and France will avoid recession, but Italy likely will not.



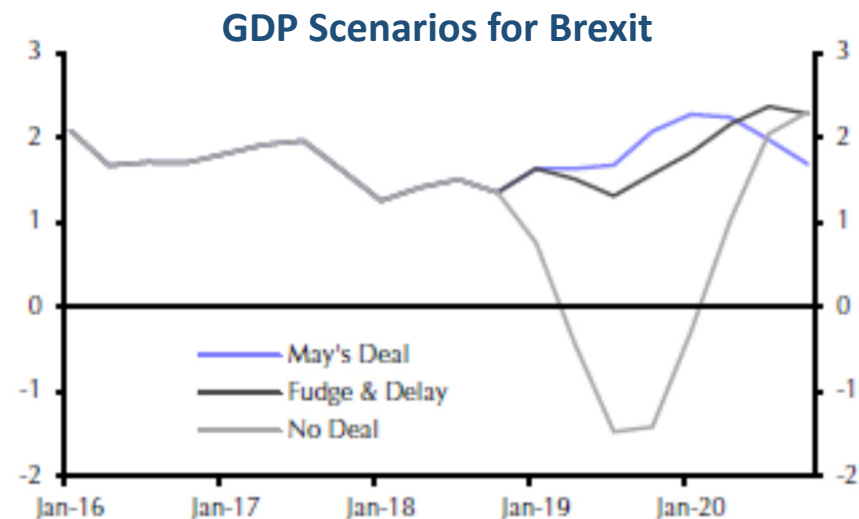
- Inflation will remain low in 2019 allowing the ECB to leave rates unchanged.
- Real incomes should rise in 2019, but much of it will be saved due to lower consumer confidence and a historically low savings rate.



2019 Big Picture Themes

United Kingdom

- To the outside world, it looks as though the UK is descending into chaos over Brexit. But while it is true that the UK political situation is highly uncertain, its economy is holding up reasonably well. And while the UK would suffer some short-term economic disruption if it ended up leaving the EU without a deal, the threat to the rest of the world from this remains small.
- Unemployment will continue to fall and household incomes are set to rise in 2019 thanks to lower inflation.
- Anything but a no deal Brexit should free up investment and accelerate growth in 2020.



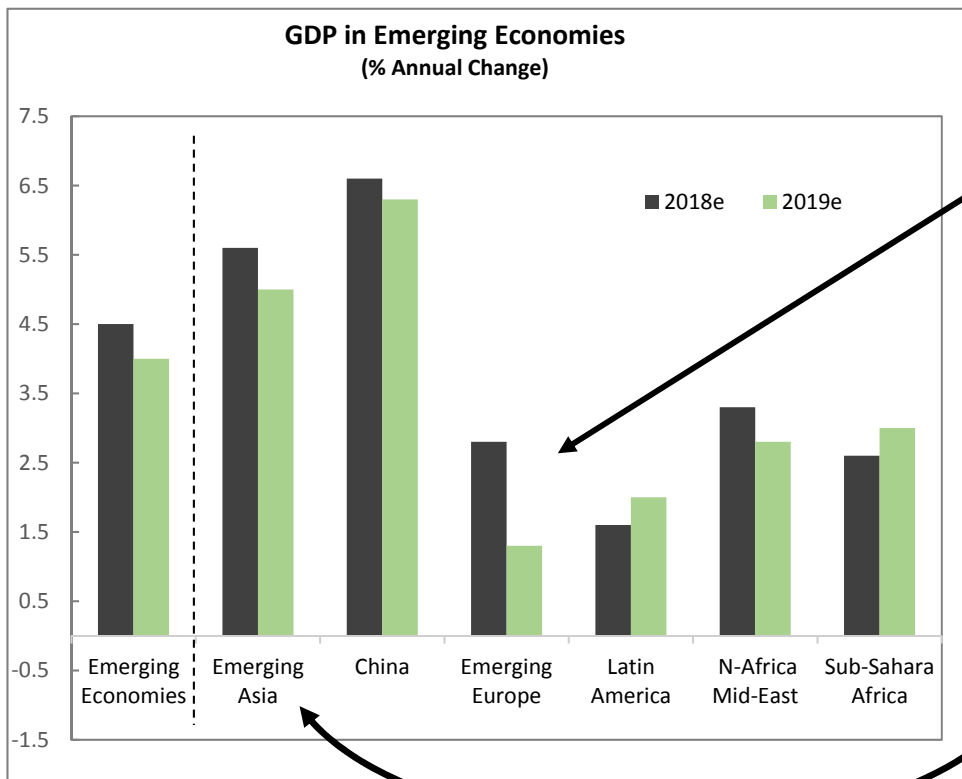
2019 Big Picture Themes

China

- Growth rate of 6.6% in 2018 was the slowest since 1990.
- Estimated economic growth for 2019 could slow further to about 6%.
- Tariffs have exacerbated the long-term structural trend to move manufacturing activity out of China.
- Chinese investment into the US has fallen by 70% in 2018 and will likely slow further.
- Expect China's reengagement with Japan to accelerate in 2019-2020. Chinese tourism to Japan expected to increase 30%.
- An aging Japanese population has led to a proposal to allow 500,000 workers into Japan by 2025. The majority would come from China.



Emerging Economies



Emerging Europe

- Hungary
- Turkey
- Czech Republic
- Poland
- Latvia

- Slowing in Germany will have adverse effects through direct trade links.

Emerging Asia

- India
- S. Korea
- Malaysia
- Philippines
- Taiwan
- Thailand

- Growth will suffer from the slowdown in China and from earlier monetary tightening.

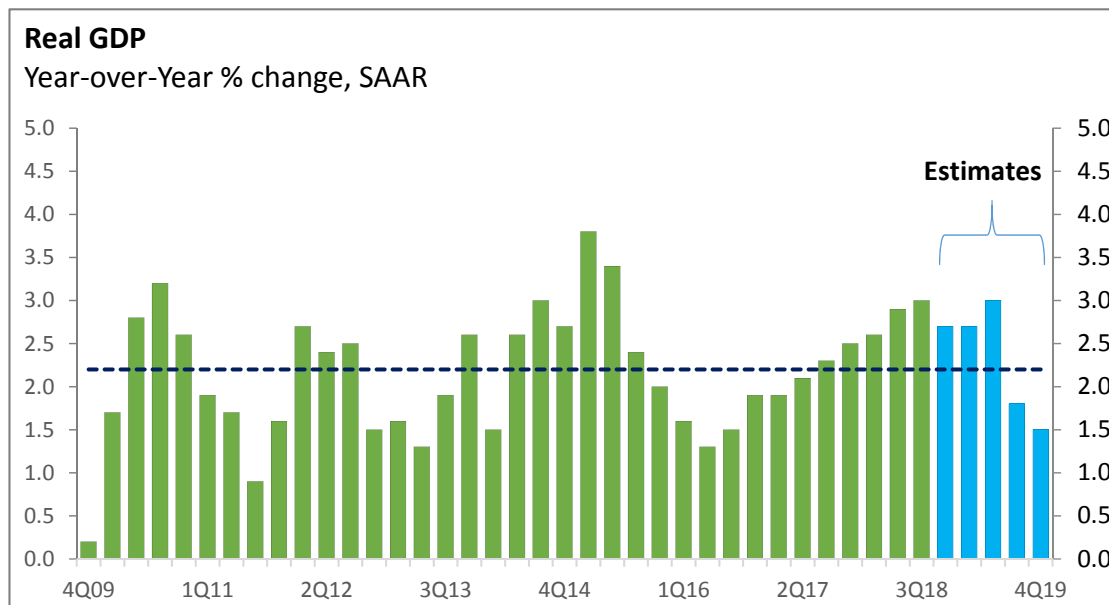


2019 Big Picture Themes

- We live in a Globally Integrated Economy
- **The U.S. Economy will grow near 2.5% in 2019 driven by consumer spending**



Solid consumption growth will counter-balance growing risks to the economy

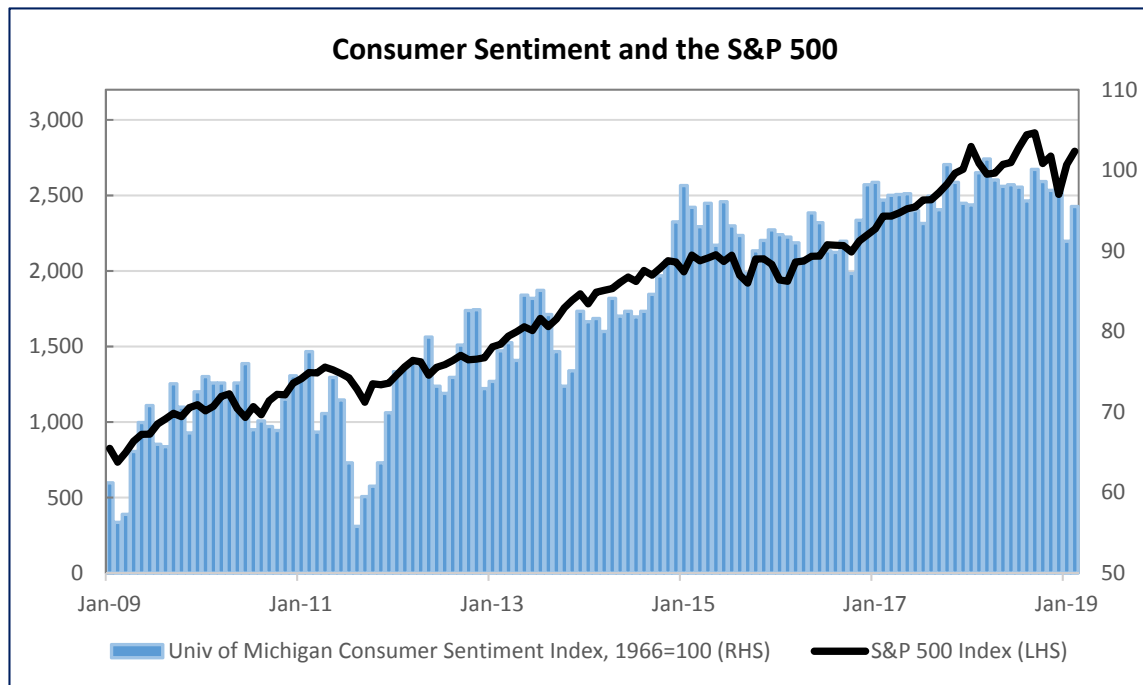


Source: U.S. Bureau of Economic Analysis, fred.stlouisfed.org

- Consumer spending, benefiting from a robust labor market, continues to drive the economy forward.
- The decline in oil prices from \$85/bbl to \$65/bbl will provide a boost to household purchasing power.
- The economy is on track to expand by 2.7% for 2019 as a whole.
- GDP growth will likely slow in the second half of 2019 and throughout 2020, moving below the economy's estimated long-term potential growth rate of 2.0%.



Consumer Sentiment has been affected by the government shutdown and market turmoil



- The University of Michigan consumer confidence index rebounded 4.3 points after the end of the government shutdown.
- Ongoing issues that are effecting confidence include:
 - US-China trade war
 - Rising interest rates
 - Increasing stock market volatility
 - Less certainty of Federal Reserve monetary policy

Source: U.S. Bureau of Labor Statistics, fred.stlouisfed.org



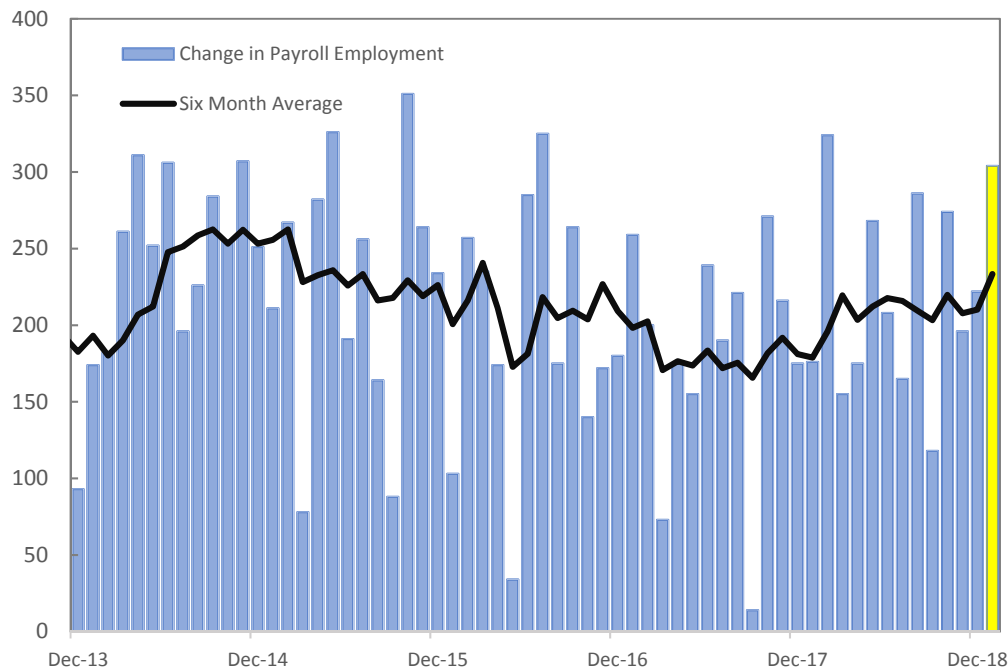
2019 Big Picture Themes

- We live in a Globally Integrated Economy
- The U.S. Economy will grow near 2.5% in 2019 driven by consumer spending
- **The labor market is still very healthy**



Payroll Employment: Average monthly payroll gains of over 200,000 are well above the replacement rate of 150,000

Monthly Change in Payroll Employment (000s)



- The labor market added 304,000 jobs in January, while the unemployment rate remained near a 48-year low of 4.0%.
- Wages crossed the 3% mark for the first time since the end of the Great Recession in mid-2009, increasing 3.1% over the past 12 months.
- The creation of 20 million jobs since 2010 and the steady decline in the unemployment rate has created tight labor market conditions.

Source: U.S. Bureau of Labor Statistics, fred.stlouisfed.org

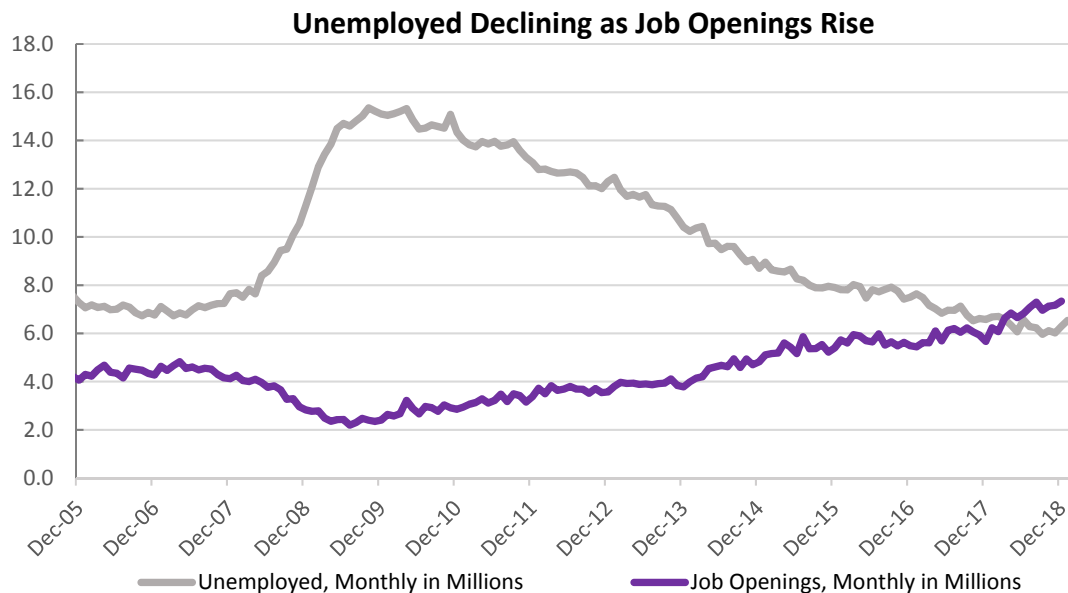


2019 Big Picture Themes

- We live in a Globally Integrated Economy
- The U.S. Economy will grow near 2.5% in 2019 driven by consumer spending
- The labor market is still very healthy
 - **There are over 1 million more job openings than there are people looking for work**



Job Openings versus Unemployed: Hard evidence that labor is scarce

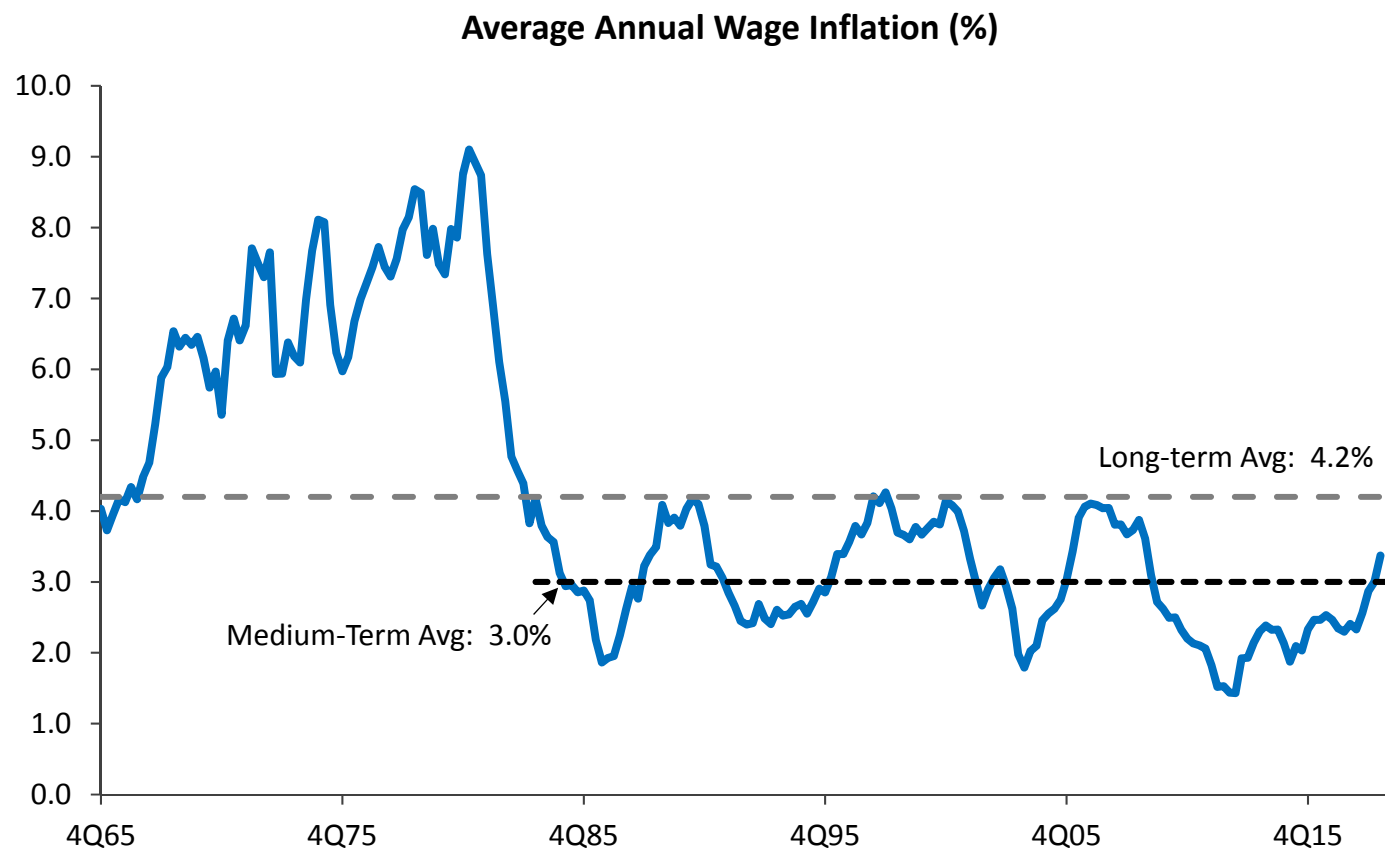


- Job openings are still robust at 7.33 million, a 29.4% increase over a year ago.
- The number of unemployed actively looking for work, stood at 6.29 million in December, down 4.4% from the prior year.
- While noting the one-month gap in the two data series, there are now 1 million more job openings than people looking for work.

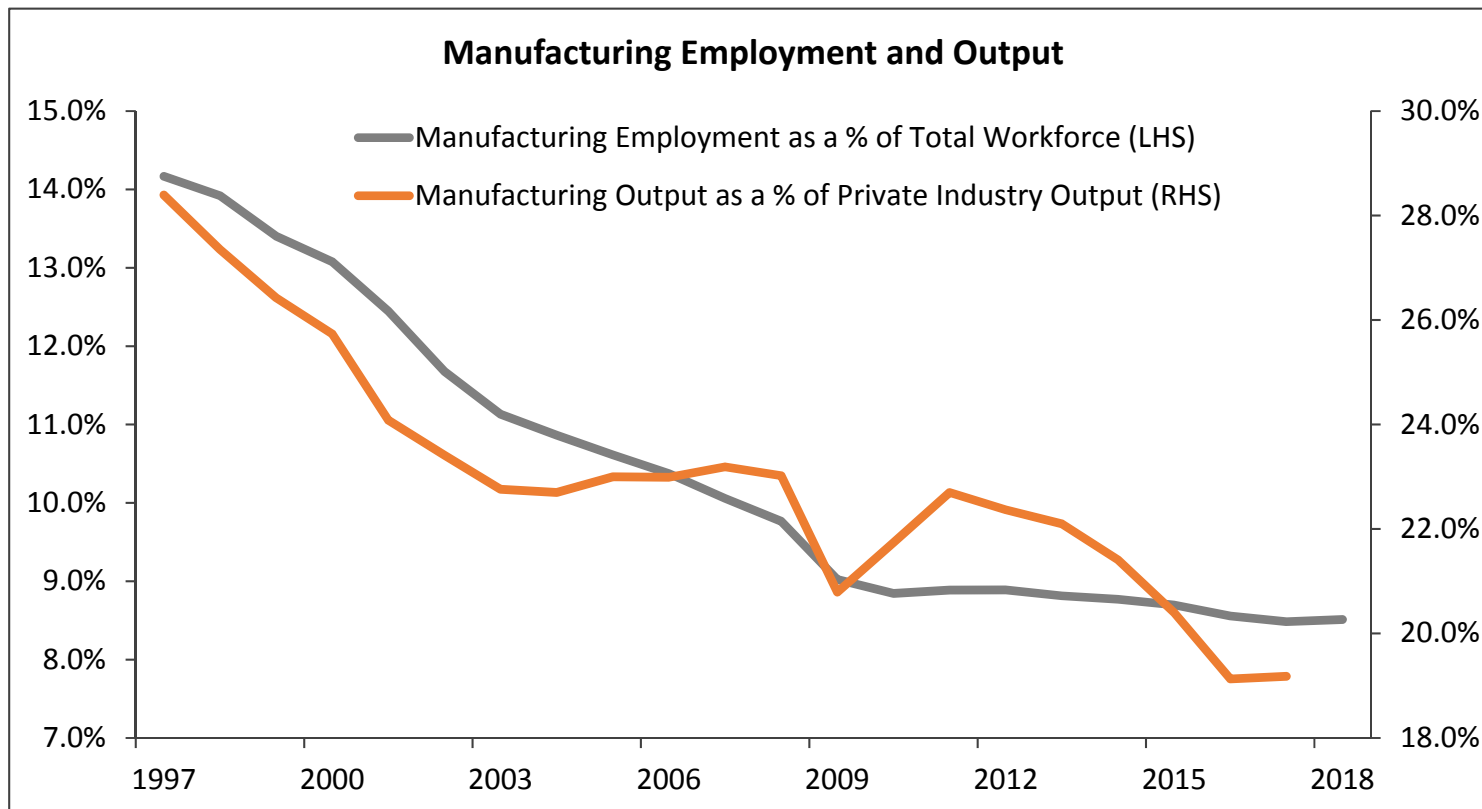
Source: U.S. Bureau of Labor Statistics, fred.stlouisfed.org



Wage Inflation has been largely absent during this cycle



Manufacturing Employment and Output has been declining in the U.S.



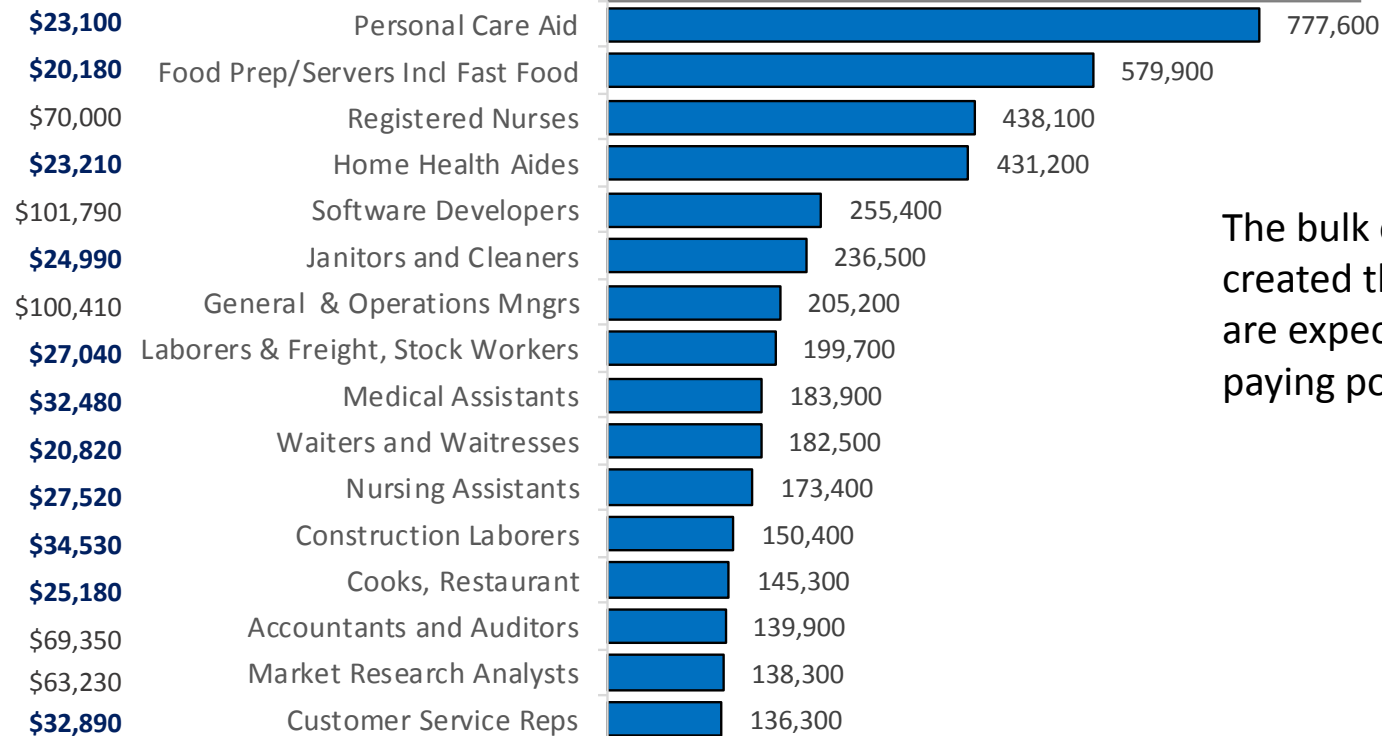
Sectors Forecasted to Create the Most New Jobs, U.S. 2016-2026

New Jobs by Major Occupational Group

Numeric change in employment projected 2016-26

2017 Median Pay

Number of New Jobs (Projected), 2016-26



The bulk of new jobs created through 2026 are expected to be low paying positions.

Source: Bureau of Labor Statistics



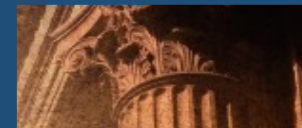
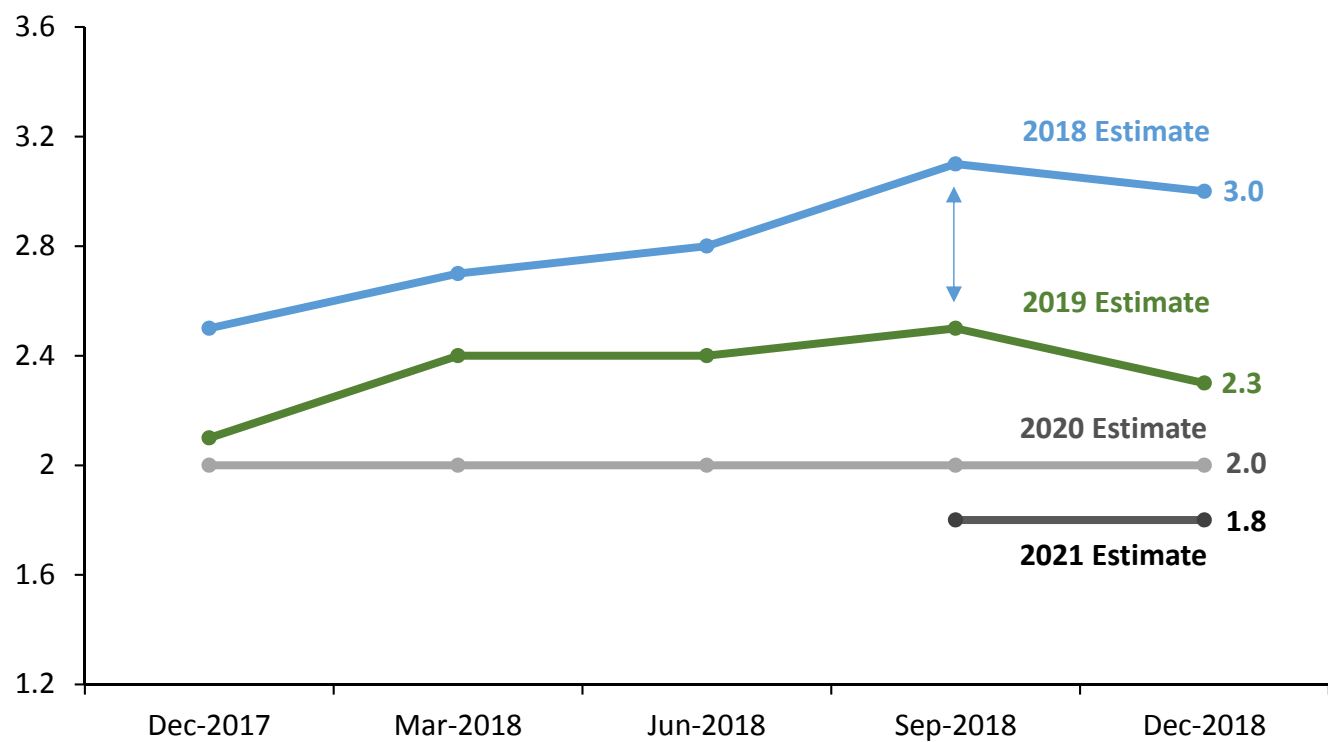
2019 Big Picture Themes

- We live in a Globally Integrated Economy
- The U.S. Economy will grow near 2.5% in 2019 driven by consumer spending
- The labor market is still very healthy
 - There are nearly 600,000 more job openings than there are people looking for work
- **Fed is “on hold” for most of 2019**
 - **The FOMC’s own estimates for future growth have been trending downward. Why would they move aggressively to raise rates?**

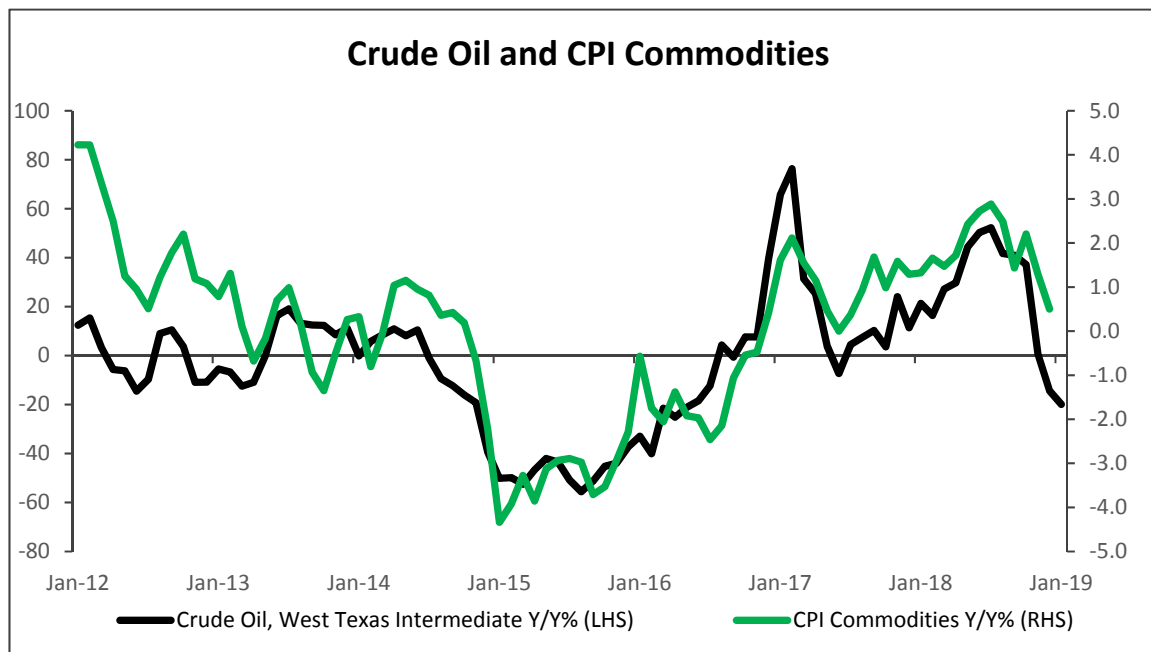


2019 Big Picture Themes

FOMC GDP Estimates (%)



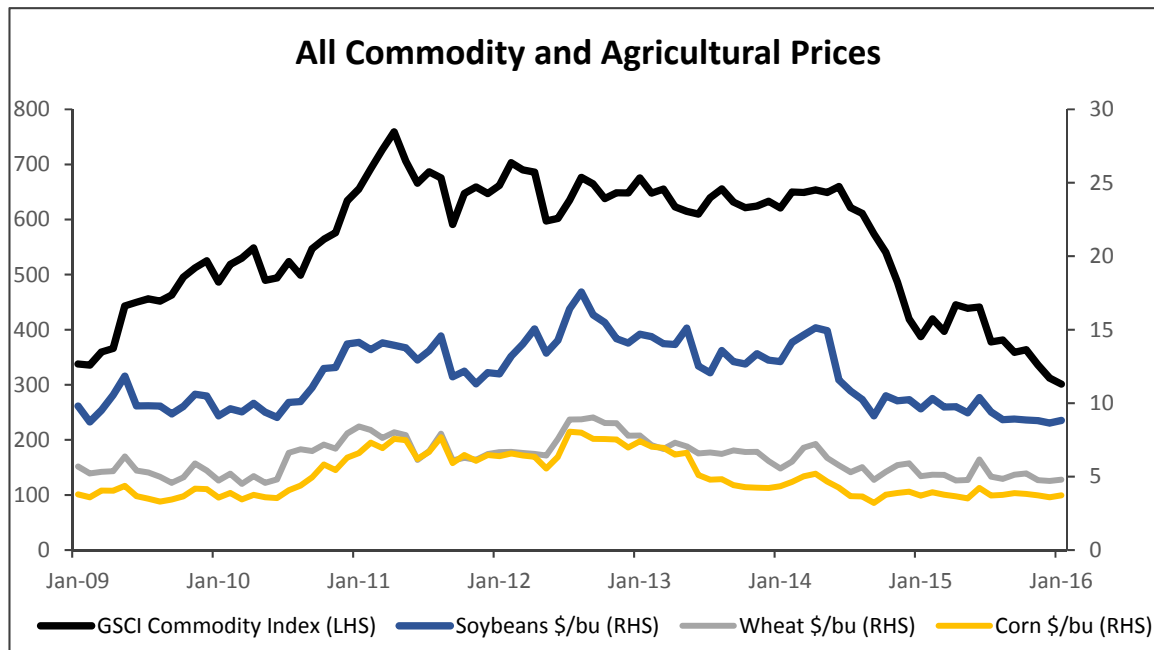
Crude Oil and Commodities



- The recent slump in oil prices will act as a significant drag on inflation.
- A slowdown in GDP growth in the US and China, the world's largest oil consumers, is likely to slow growth in oil demand.
- Energy's contribution to inflation is likely to be negative during the next two years.



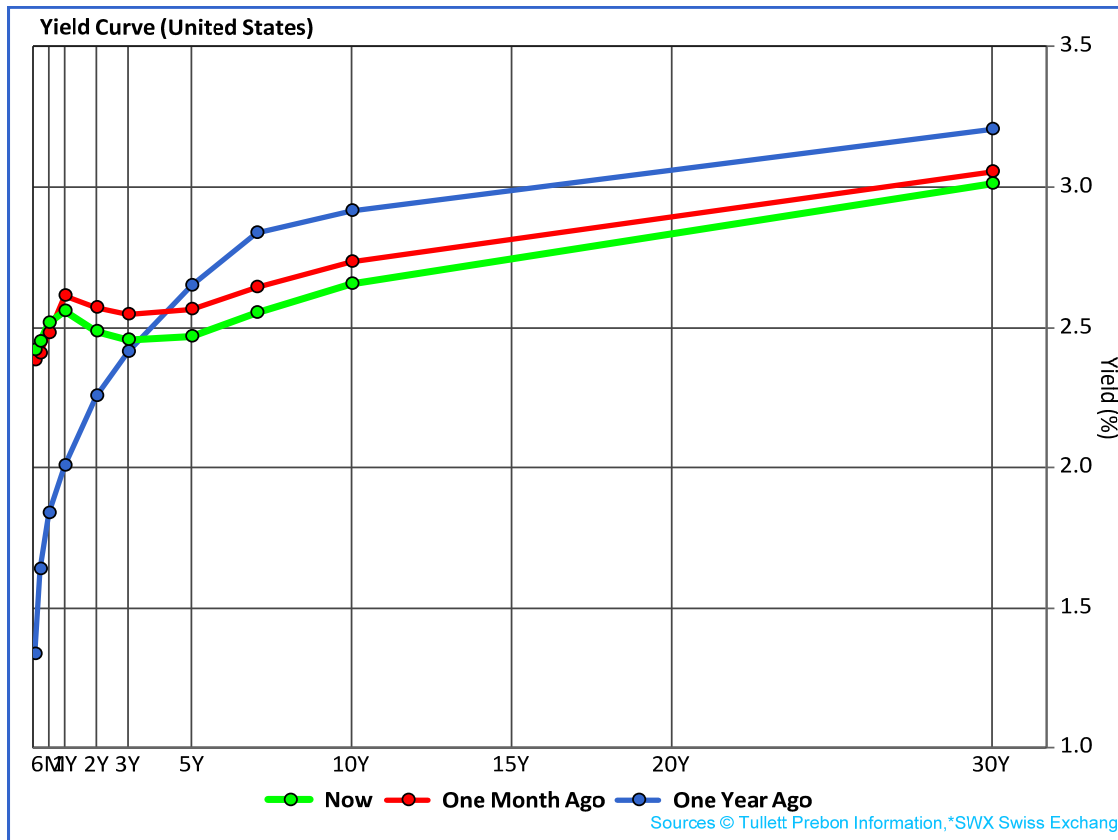
All Commodity and Agricultural Prices



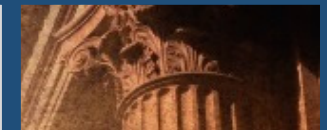
- Movements in agricultural prices are unlikely to have a significant impact on inflation.
- Agricultural commodity markets are depressed due to global supply abundance and ongoing trade disputes.
- The outcome of the 90-day 'cease-fire' with China on trade will be the most pivotal event for US agriculture in 2019.



Interest Rates: Yields across the curve have eased since the Fed adopted its “patient” stance in response to sharper than anticipated slowing of global GDP

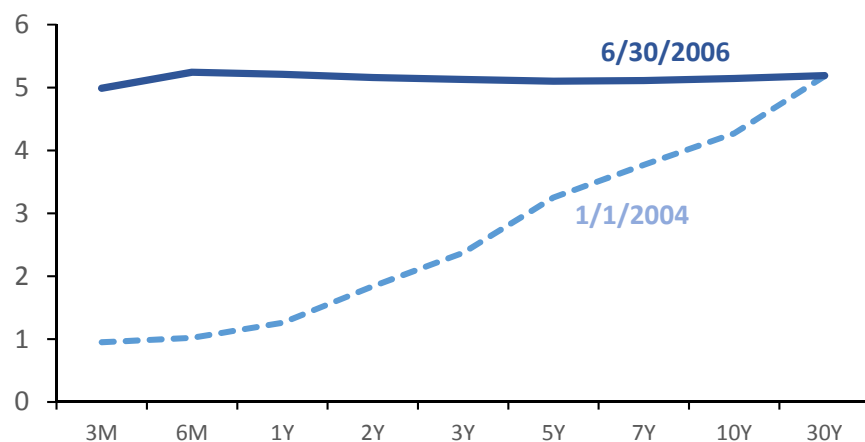


- The Fed raised rates four times in 2018 to the Fed funds target range of 2.25 – 2.50%.
- With inflation under control, the consensus of the Fed is maintain rates at current levels.
- Policymakers are focused on heading-off concerns about excesses in financial markets.
- The Fed is acutely aware that both equity and property prices have risen a long way since 2009, as they did prior to the dotcom and subprime crashes.

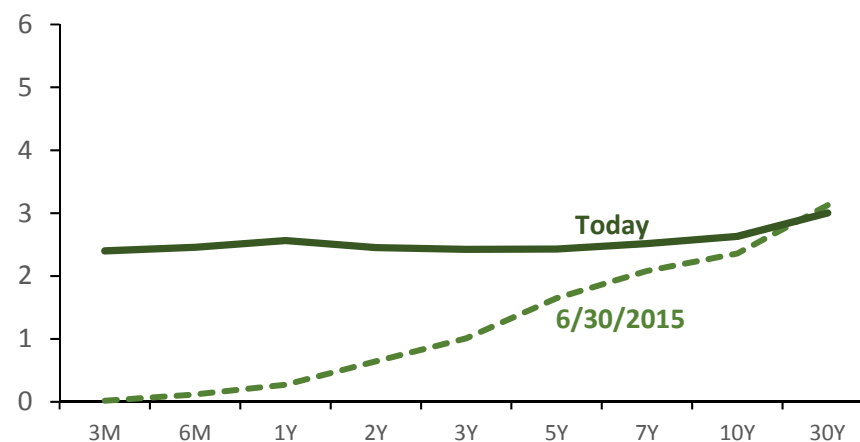


The curve in this tightening cycle has behaved in-line with past experience

The US Yield Curve: The Previous Tightening Cycle



The US Yield Curve: Today's Tightening Cycle



The only difference between the behavior of the yield curve in today's tightening cycle versus the previous cycle is that it flattened at a lower level. That is the result of a lower neutral rate.

The neutral rate is a level that keeps the economy at its production potential over time, i.e., monetary policy is neither accommodative nor restrictive.



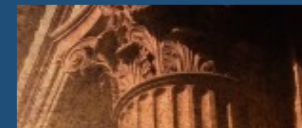
Market Outlook: Is the stock market positioned to resume its uptrend?

Positives

1. **US economic outperformance theme remains intact**; economists continue to highlight very low recession probabilities.
2. **Consumer confidence rebounded** after government shutdown.
3. **The labor market is very strong**; 3- month average of new jobs creation is 240,000 up from 222,000 the prior three months.
4. **Fed policy is back on track.** Fed Chairman Powell is now emphasizing patience, risk management and flexibility.
5. **Inflation is low** and forecasted to remain at moderate levels; upward pressure on interest rates is easing.

Negatives

1. **Global growth has desynchronized** with particular concerns about the slowdown in China.
2. **2019 EPS estimates at risk** from trade conflict and margin pressure.
3. **Interest rate sensitive sectors are weak.** Home sales are trending downward and vehicle sales have softened.
4. **Demand for borrowing is waning** for all types of loans; lending standards for C&I loans and commercial RE are tightening.
5. **Manufacturing activity is vulnerable** due to weakness in export order growth caused by trade and tariff constraints.



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