Citizens Market Update

December 14, 2021

Economic and Financial Markets

- The unemployment rate declined by 0.4% to 4.2% in November with 6.9 million unemployed persons, while nonfarm payroll employment rose by 210,000.
    - These unemployment measures are down considerably from their recent highs in April 2020 but remain above their levels prior to the coronavirus (COVID-19) pandemic (3.5% and 5.7 million, respectively, in February 2020)
- The labor force participation rate increased marginally to 61.8%; however, this is 1.5% below its February 2020 level and the U6 unemployment rate, which reflects real unemployment rate is close to 7.8%.
- Total persons claiming UI benefits (all programs) at the beginning of December were 1.9 million (not seasonally adjusted) as compared to 4.8 million at the end of January 2021, 3.6 million at the end of May 2021, and 1.7 million at the onset of COVID-19 in March 2020.
- The U.S. Federal Reserve Fed Funds target is still at 0.00%-0.25% and while the official forecast is for two to three rate increase in 2022, we expect one to two rate increases in 2022. However, we will get more color from Fed tomorrow.
- The FOMC Chair recently talked about at the recent Senate hearing that they will accelerate the tapering or monthly bond-buying program in the amount of $120 billion of Treasury and mortgage-backed securities; currently the Fed balance sheet is at $8.7 trillion as compared to $4.2 trillion on December 31, 2019.
- Real GDP decreased 3.5% in 2020 compared with an increase of 2.2% in 2019. We expect 2021 annual GDP growth to be around 5.5%, decreasing to 3.5% in 2022 before reverting back to historical average of approximately 2.5% in 2023. The robust growth in 2021 is primarily because of negative growth in 2020 and from the addition of significant fiscal and monetary stimulus in 2021.
- Even with high inflation numbers this year, we still believe inflation is transient and not permanent or spiraling, however it is sticking around for little longer than initially expected (partly due to 2021 American Rescue Plan Act which provided $1.9 T in additional funds). We expect Fiscal stimulus to run out and cash savings to deplete by middle of 2022 and that should lead to peak price gains by the middle of next year and at that time prices will start to decrease towards the beginning of third quarter of 2022 as demand stabilizes, people return to labor force and supply bottlenecks fade.

- By third quarter of 2022, we expect our inflation rate to be closer to 2.5% as compared to 1.75% in March 2020 – unless there is more fiscal stimulus.

Equity Market

- The equity market is at record high primarily due to robust growth and fiscal and monetary stimulus, including all time low historical interest rates. YTD, the S&P 500 and DJIA are higher by 24.9% and 17.0%, respectively.

Interest Rates

- Fixed income markets have seen interest rates recover significantly in 2021 as the economy continues to recover. However, due to structural and demographic constrains, we expect interest rates to remain low and range bound from here until the end of 2022 with 5-year Treasury at 1.00%-1.50% and 10-year Treasury at 1.25%-1.75%
- Corporate credit market spreads are back to normal pre-COVID levels due to expected significant economic growth with the Bloomberg Barclays U.S Corporate Investment Grade spread currently at 99 bps.

Fixed Income Market

- Through October 31, 2021, corporate bond issuance is at $1.7 trillion, or 18% lower than the record-breaking $2.1 trillion issued over the same time period in 2020
- The corporate bond market has topped $1 trillion each year since 2011 as interest rates have been consistently historically low.
- For year-to-date 2021, municipal long-term negotiated issuance is $397 billion and is marginally lower compared to the $428 billion issued over the same time period in 2020.
- Overall there has been strong investor demand in both the tax-exempt and taxable markets as evidenced by the record issuance in 2020 and strong issuance so far in 2021

Risk Transfer Market

- In 2020, there were $97 billion of insured losses globally, which were mostly driven by smaller events as no single event incurred more than $3 billion of insured losses.
- As of early fourth quarter 2021, insured losses are approximately $107 billion globally, which is 13% above the 10-year average of $95 billion. The largest event thus far in 2021 is Hurricane Ida, which is estimated to be approximately $35 billion, followed by European flooding in the amount of approximately $12 billion, and $15 billion for U.S. winter weather and storm Uri.

- There is $660 billion of global reinsurer capital available after the first half of 2021. Although global risk has exponentially increased over the last decade, risk transfer capital has only increased by approximately 17%, or $95 billion, and therefore we expect reinsurance rates to continue their upward trajectory to account for additional risk. In 2022, we expect global reinsurance capital to remain unchanged based on the insured losses thus far in 2021.
- While the global markets are improving, the Florida market is still experiencing dislocation due to litigation and social inflation as well as continued adverse loss development.
- For 2022, we expect rate increase of up to 10% with most carriers in the 5%-10% range.