# The Unexpected 2026 Economy

## Status to date and the Outlook for 2027

**November 3, 2026**



CALIFORNIA Economic Forecast

**Mark Schniepp**
**Director**

Image: Zack Blanton

# The Big Issues in 2024

- Most of the imbalances caused by the Pandemic have largely corrected
- However, not all . . . .
- Labor Markets are still too tight
- Due to runaway Federal Gov't Spending . . . .
  - Inflation remains persistent
- Due to persistent inflation . . . . .
  - Interest rates remain high
  - Food and energy prices are now 20 percent higher
  - along with car prices, car insurance, car repair, rent, admissions to sports, admissions to anything

From 6-7-24

# The 2024 Forecast

- GDP growth at 1.6 percent in Q1 and about 2.0 percent the rest of the year.
- Consumer spending pullback does not occur
- The imbalances brought by the pandemic have led to these problems which will not be resolved in 2024
  - the office market distress
  - stubborn inflation
  - high interest rates, and
  - global / political uncertainties
- Inflation will decelerate but achieving Fed target of 2.0 percent won't occur this year
- However the first rate cut occurs later this year

From 6-7-24

# The 2024 Forecast

From 6-7-24

- Banking failures are largely contained to date
  - But a CRE vulnerability remains a threat
  - Will banks continue to extend and modify, or will we see a surge in distressed assets and foreclosures
- Job market will soften some with rising unemployment; however qualified labor will remain scarce
- And because population is declining in California, the labor force represents a limiting factor to both job creation and loss

# The Pressing Issues / U.S. Economy

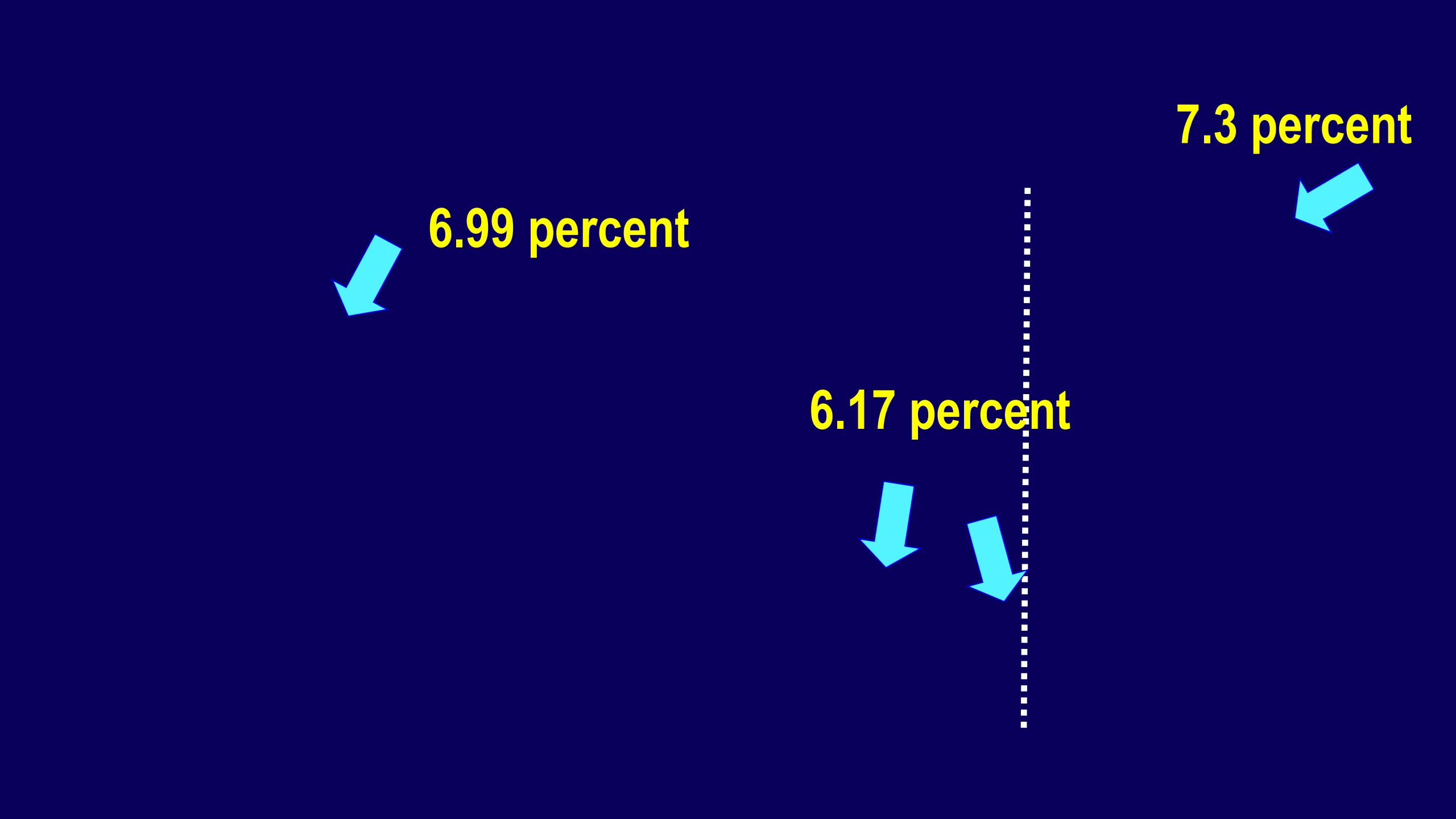
- Higher core and headline inflation than expected especially in energy sensitive sectors
- Rising treasury yields and mortgage rates

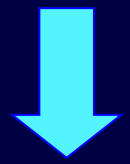
  ~ this pressures housing, CRE, business investment, credit cards, and auto financing
- An unusually cautious hiring environment that has narrowed the breadth of job creation, especially in California
- Fed policy uncertainty

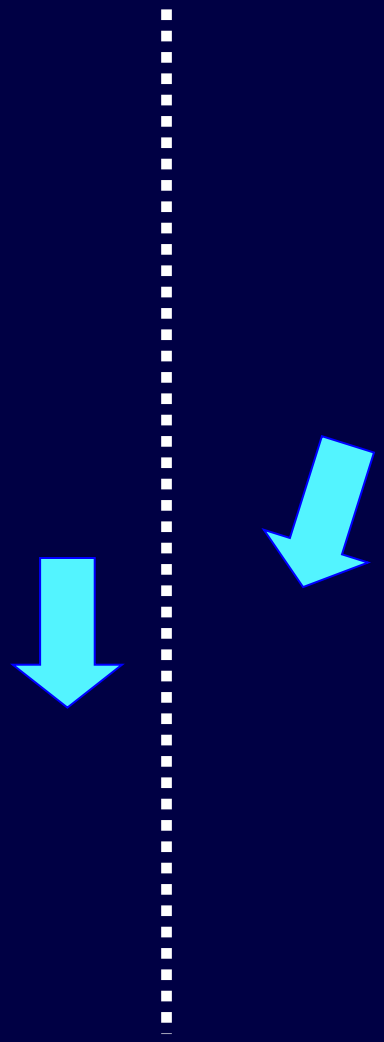
  ***the September hike was generally unexpected***

6.99 percent

6.17 percent


7.3 percent
6.99 percent
6.17 percent



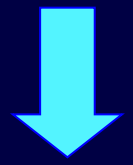



$95 - $110
$97
$63

S&P 500: up 10.5 % year-to-date

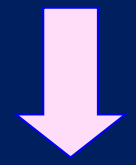
Nasdaq: up 10.8 % year-to-date

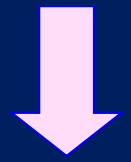
Earnings have been stellar



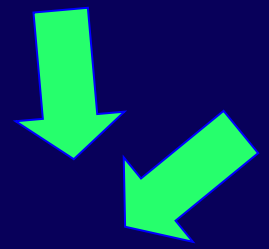


| | |
|---|---|
| GOOG | APPL |
| MSFT | NVDA |
| AMZN | AMD |
| META | TSLA |
| | MU |





moved in October to
the highest level
since 2007



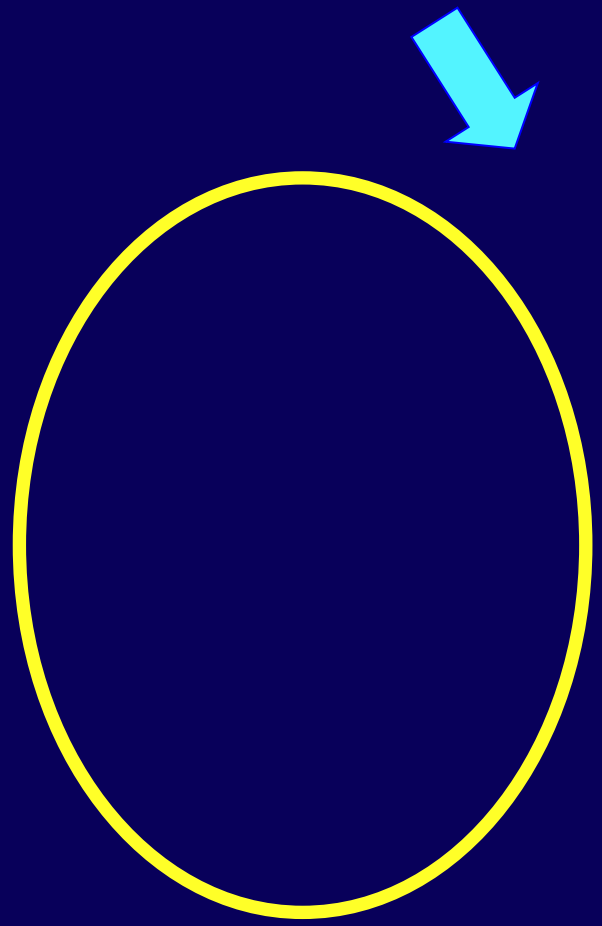
# The Bond Market: What is it telling us ?

- to expect higher and more persistent inflation
- to say arrivederci to FED rate cuts
  - 10 year = expected real short term rate + expected inflation + risk premium
- to demand a larger risk premium for holding long term U.S. gov't debt
- to plan for stronger economic growth
- It's telling us the future is more uncertain and more likely to be more inflationary than previously thought
- And the lateral stock market is nervous about higher rates leading to lower present values for distant expected earnings . . . . .

# Good stuff about the U.S Economy

- ❑ Growth is accelerating
- ❑ Manufacturing is surging
- ❑ Tariffs not negatively impacting consumption or investment
- ❑ Stock market remaining near an all-time-record-high
- ❑ AI investment continues to accelerate
- ❑ Job growth is still positive
  - inflation adjusted salaries are rising
  - still no obvious trauma in the labor market
- ❑ no recession expected





# Quiz 1: What will the FED do next ?

They next meet on December 9. . . .

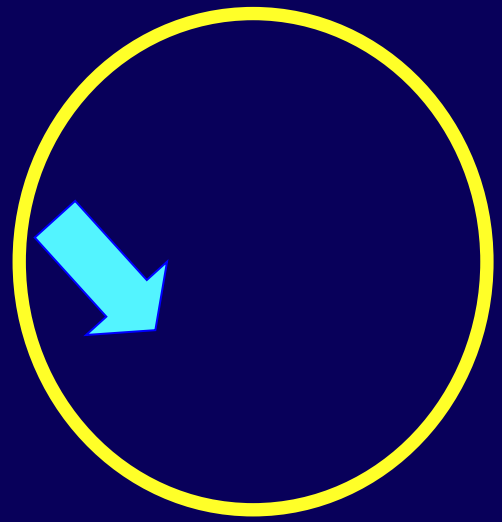
(1) They will raise rates another 25 basis points

(2) They will raise rates another 50 basis points !

(3) They will cut rates 25 basis points

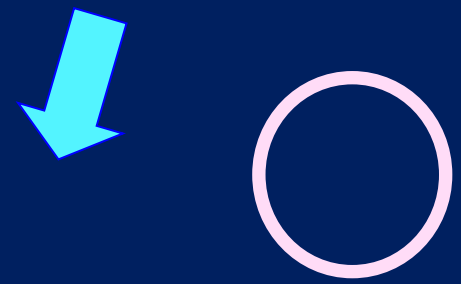
(4) Nothing, they will now wait and see

(5) Whatever they do, they will make matters worse



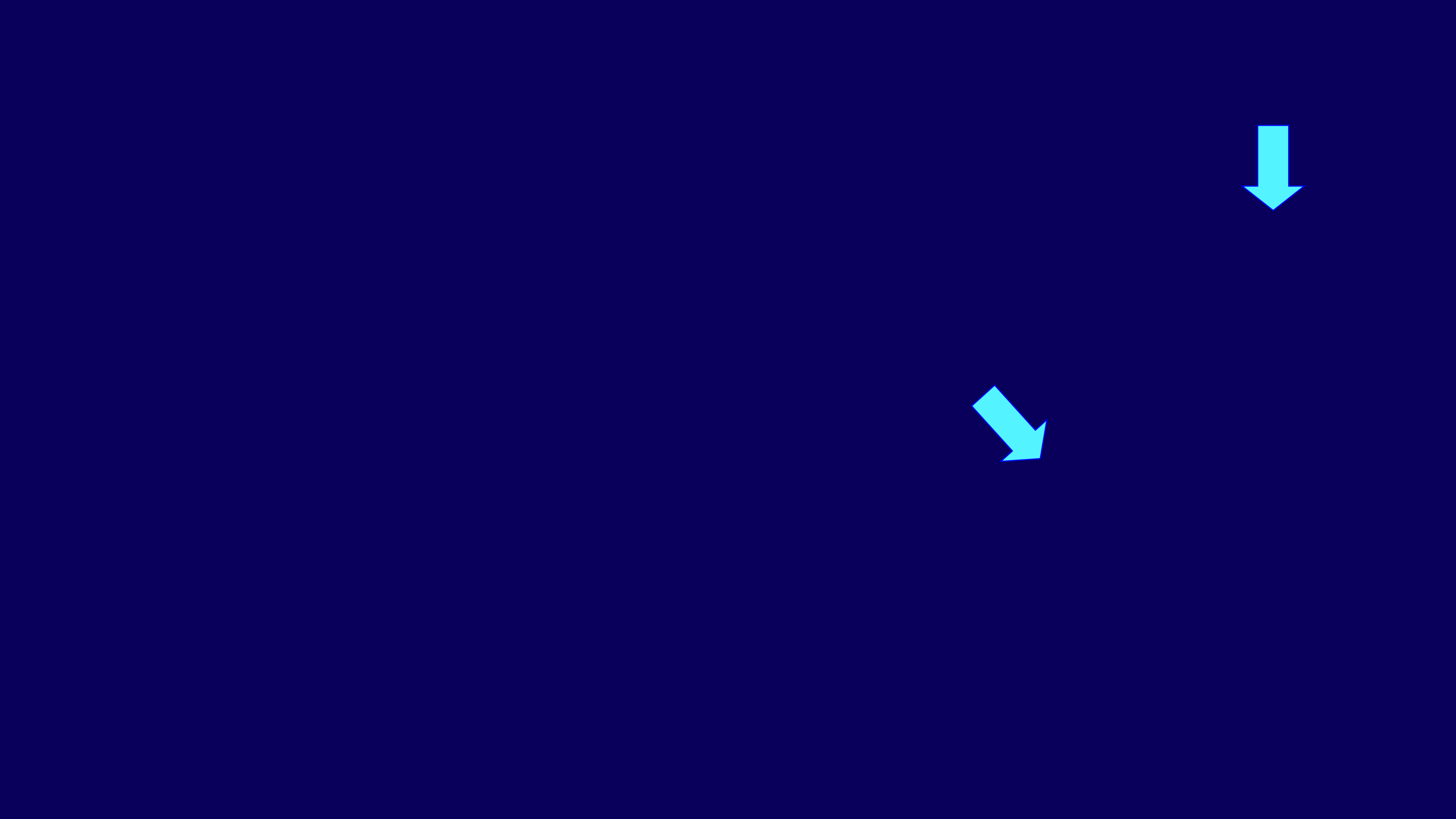
Consumer
price Index

Average Earnings -
All Private Sector Workers



# Consumers have more disposable Income

- Real wages remain positive and labor market at or near full employment
- No Tax on Overtime: 30 million workers claimed
  - Average benefit: $3,100
- No Tax on tips: 8 million workers claimed
  - Average benefit: $7,000
- Senior Deduction: 38 million Americans claimed
  - Average benefit: $7,500
- No Tax on Made-in-USA Car Loan Interest: 1.5 million workers claimed
  - Average benefit: $1,800



Data centers

Data center power generation

Advanced mfg facilities

- ~ semiconductors
- ~ batteries
- ~ EV-related



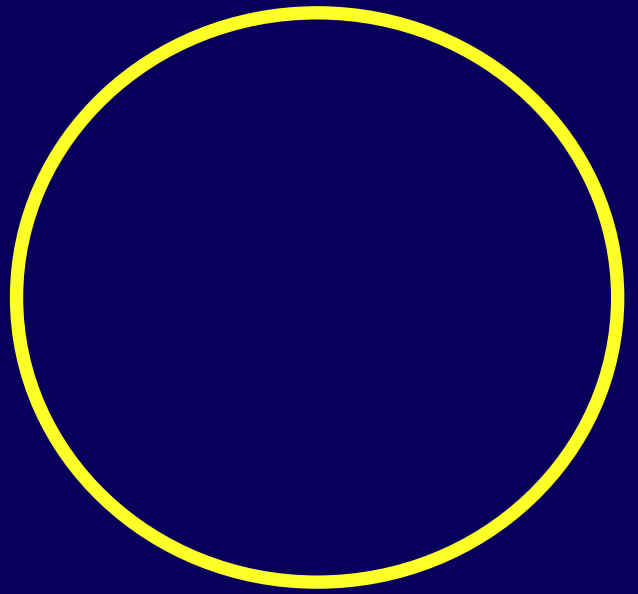
Cost to construct data center buildings each month, including materials and construction labor.

Up 71 percent

Up 39 percent

# Top 15 New Factories built or underway Oct 1

| Company | Location | Value (millions) |
|---|---|---|
| GlobalFoundries - Semiconductors | Malta, NY | 10,000 |
| Anduril - Defense Technology | Sparrows Point, MD | 3,700 |
| U.S. Steel - Steel Manufacturing | Braddock, PA | 3,000 |
| Westinghouse - Nuclear Energy | Hopkins, SC | 1,000 |
| Hyundai Translead - Commercial Trailers | Joliet area, IL | 600 |
| Carrier - HVAC Systems | Fort Worth, TX | 600 |
| Corning - Specialty Glass | Wilmington, NC | 585 |
| Hyundai Transys - Automotive Components | West Point, GA | 560 |
| Blue Origin - Space Technology | Hutto, TX | 555 |
| Mitsubishi Power - Power Generation | Pooler, GA | 490 |
| M.C. Dean - Electrical Infrastructure | Caroline County, VA | 413 |
| Blue Origin - Space Technology | Merritt Island, FL | 330 |
| Blue Bird - School Buses | Fort Valley, GA | 300 |
| Lockheed Martin - Aerospace & Defense | Grand Prairie, TX | 300 |
| Nucor - Steel Manufacturing | Crawfordsville, IN | 105 |







# Other Issues

- **The war**

  Oil prices remain high despite expanded oil flows, due entirely to expectations of supply disruptions

  Credible prospect of the entire strait opening soon still absent

- **Tariffs**

  . . . . have become a nothing burger

  . . . . are a new revenue source for the federal gov't: $167 B in FY26

- **Federal Debt**

  Now at $40 trillion. Some direct economic impact by constraining the ability of the U.S. to reduce spending, keeping longer term rates higher





# U.S. Economy for rest of 2026

- Growth accelerating
- Labor market condition improving
- Inflation slowly improving
- . . . but not yet interest rates
- Stock market likely to maintain higher valuations if treasury yield surge cools
- Midterms
  - possible disruptions from midterm elections
  - midterm miracle

# The Midterm Miracle

- There have been 25 midterm-elections from 1926 to 2022
- The S&P rose in 23 of them (the October-June) period
  - A 92 percent positive rate
  - The average cumulative return was 19.8 percent
- Elections clarify the policy outlook moderating uncertainty
- Since they favor the non-presidential party, they can reduce the likelihood of more policy changes
- Greater gridlock can make business conditions more predictable

Index:
1985 – 2014
avg



# Quiz 2: Are you concerned about 2027 ?

(1) I'm worried that inflation and interest rates will stay high

(2) I'm afraid I'll be replaced by a robot

(3) I'm afraid all my AI stocks will implode

(4) I'm confident my AI stocks will retire me early

(5) I'm betting the bank on SPACE-X (symbol SPCX)

(6) 2027 will be a break out year for growth and income

(7) inflation and interest rates will decline

(8) No, AI transitions into full superintelligence by mid-2027

First Avenue Finance

Private Financial Publication

September 23, 2026

# AI trading system outperforms human experts, achieving record gains in real market conditions. We investigated whether its performance is credible.

By Eileen M. Boehm, MBA • Investigation Report




Forbes

INNOVATION > AI

# AI Bot Wows The Crowds With Unprecedented Stock Earnings

By John Werner, Contributor. ⓘ I am a 5x-founder & VC investing in AI

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Published Jan 03, 2025, 12:34pm EST, Updated Jan 07, 2025, 10:05am EST

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January 2025

# AI → AGI → ASI

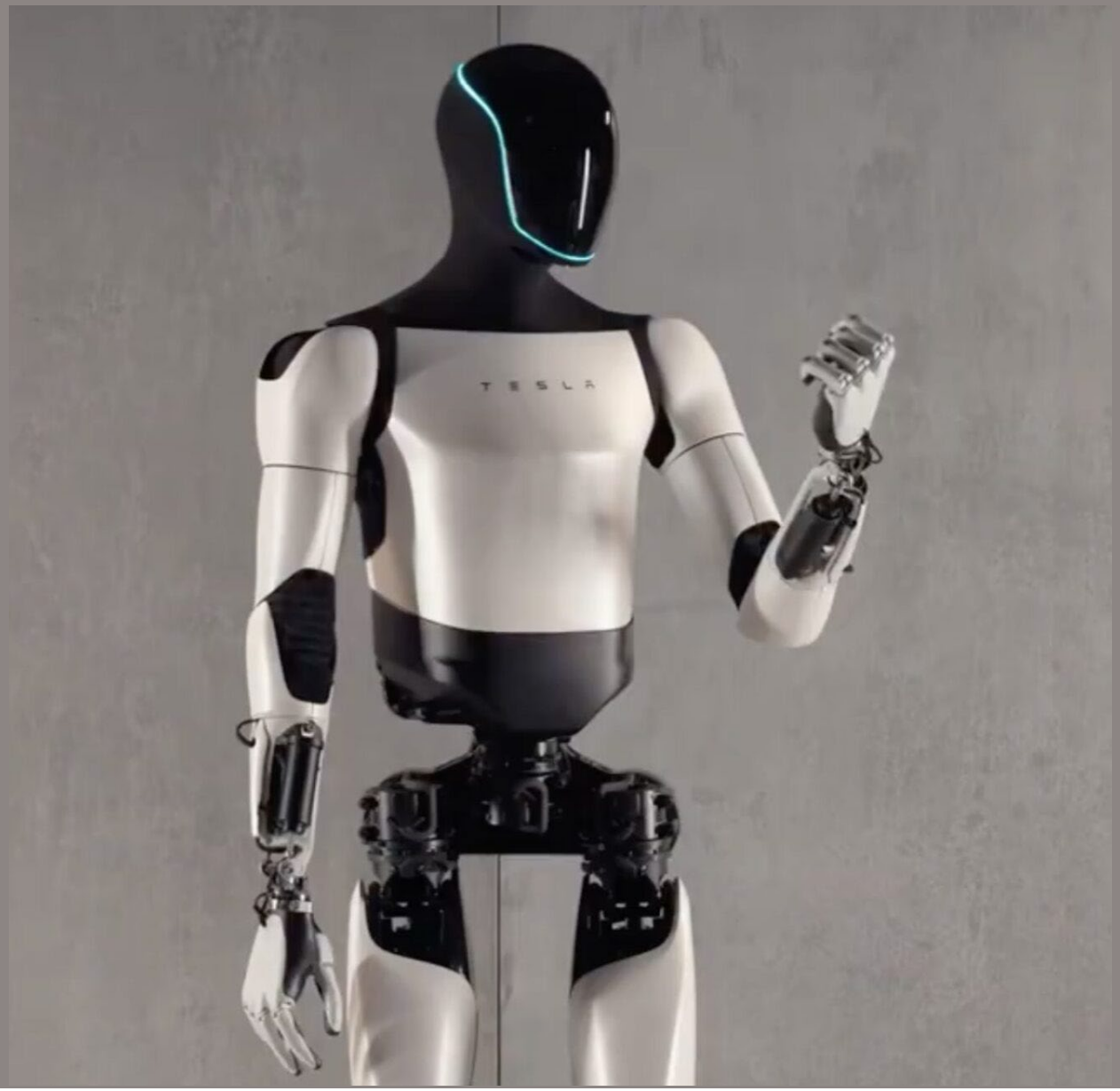
(1) The speculative but possible forecast scenario for AI to become ASI is underway. The scenario's date is actually December 2027 (says EM)

(2) AI models transition from human-level general intelligence (AGI)—where an AI can match a skilled human across digital tasks—to ASI that outperforms the best human minds collectively across all cognitive and scientific domains

(3) Operationally, the AI of today improves the methods and systems used to build AI. This is called "recursive self improvement" (and it is an accelerating and compounding process)

(4) It applies to all digital tasks, not physical activity (yet)

(5) Musk is predicting better-than-human capability across all digital categories

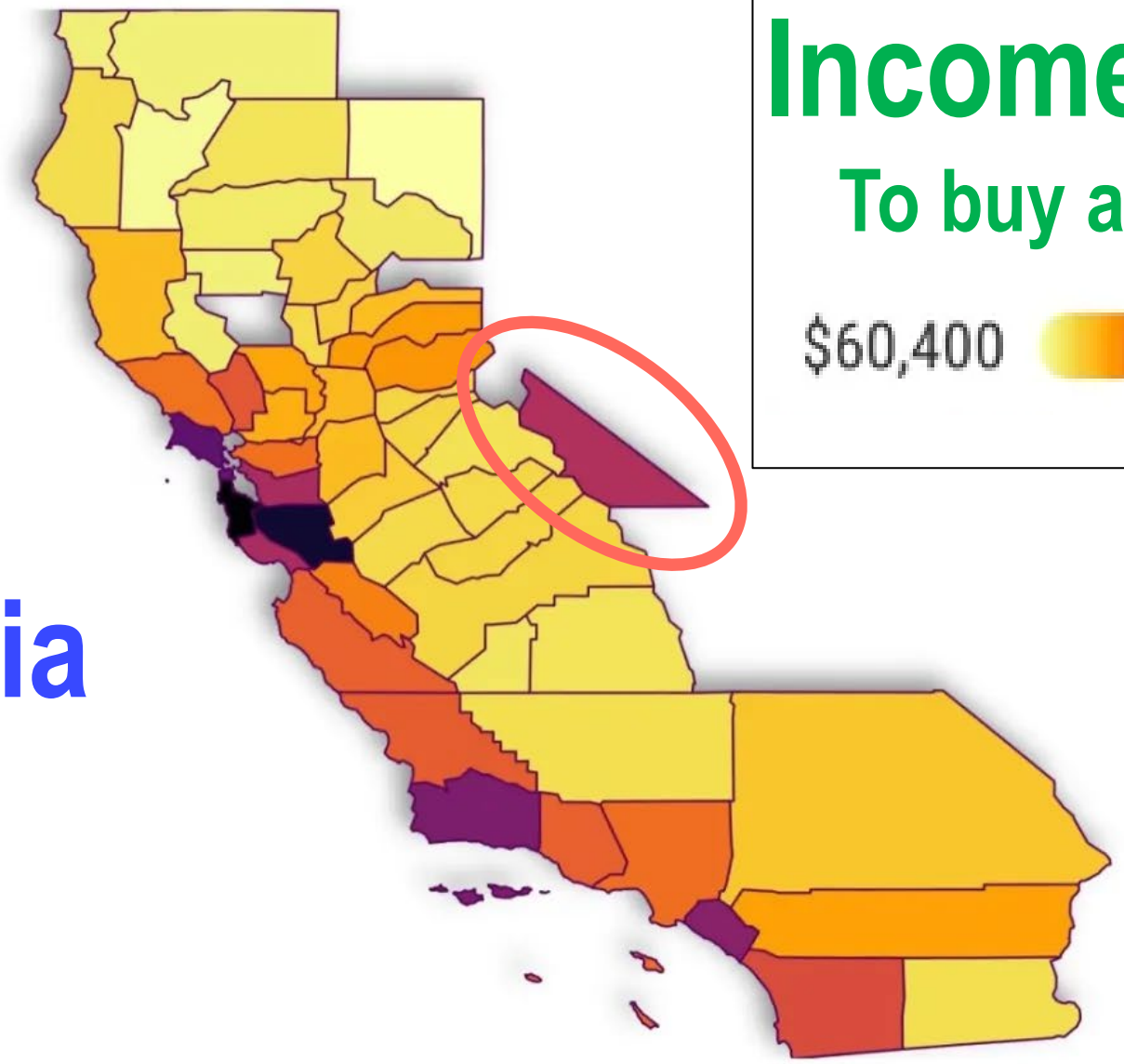



Coming in 2027: Optimus 4

# The Three Principal Criteria

- Human-level manual dexterity
  - Hands capable of manipulating objects with human precision
- AI mind that comprehends the real world
  - Intelligence that can interpret its surroundings and carry out useful and spontaneous tasks, rather than scripted ones
- Production must scale at high volumes
  - The design and mfg system must be capable of producing millions of robots. Marginal production cost would be approximately $20 to $25K at scale of 1,000,000 units annually

# California



## Income Required

### To buy a home in 2025

$60,400 — $561,600

Source: California Association of Realtors

Affordability remains the biggest California issue



# California's Problems

- Faster output growth does not solve all meaningful issues
- Resident well-being still a pressing issue
  - outbound migration
- Affordability
  - housing, insurance, gasoline, healthcare
- Housing supply
- Infrastructure
- Commercial property issues, and the development environment which has slowed down

# The California Economic Summary

| | |
|---|---|
| ❑ New Development | residential has picked up;<br>commercial & industrial have moderated |
| ❑ Labor Markets | more job creation up this year |
| ❑ Tourism | steady |
| ❑ Technology | strong, due to AI investment |
| ❑ Residential Real Estate | stagnant |
| ❑ Hollywood | less production, fewer jobs |
| ❑ International Trade | highest volumes on record |



# Commercial Real Estate

- Generally improving though in distinct areas
- And unevenly, rather than in a synchronized upturn
- Industrial market: mixed bag
  - ~ general evidence of improvement but no return to the extreme scarcity conditions of the logistics boom
  - ~ Some regional markets are diverging
- Office market: improving in Bay Area and San Diego, but substantial excess space remains; not so much in Sacramento or LA metro
  - ~ AI companies are a leading source of demand
- Retail and apartments are retaining high utilization but modest rent growth

# Industrial Vacancy Rates

| | 2025 Q3 | 2026 Q3 | |
|---|---|---|---|
| ➢ San Francisco . . . . . | 8.8 | 8.2 | down |
| ➢ San Jose . . . . | 6.3 | 5.9 | down |
| ➢ Los Angeles County. . . | 4.8 | 5.0 | up |
| ➢ Los Angeles Downtown. . . | 5.1 | 5.3 | up |
| ➢ Orange County . . . . | 4.8 | 5.5 | up |
| ➢ San Fernando Valley . . . . | 3.4 | 5.1 | up |
| ➢ San Diego . . . . | 7.5 | 7.4 | down |

# Commercial Real Estate and California Banks

- Aggregate commercial real estate prices are rising again
- Bank lending on commercial real estate is rising again.
- Banks are better handling CRE exposure by continuing to finance acceptable properties while reserving for losses, resolving problem loans, and disposing of foreclosed collateral
- Losses are being recognized rather than indefinitely postponed through the practice of extend and pretend . . . . .
- 90 percent of banks maintain a Texas Ratio of less than 15 percent
  - The median community bank is at 4.0 percent
- The median community bank NPA ratio is 0.4 to 0.5 percent

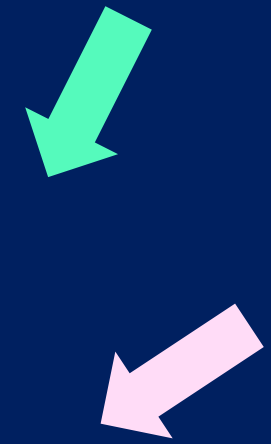
According to The California Bankers Association, California community banks currently hover between 0.10 and 0.16 percent



# Commercial Real Estate and California Banks

- Bank non-performing assets are shrinking, due to
  - Charge-offs and foreclosure sales, mostly, but also
  - financially recovering borrowers
- And of course, the office sector remains the most severe pain point for all commercial banking assets
- However, distress is highly localized in major metro areas with structural occupancy declines, such as Oakland and DTLA
- Delinquency rates rising since 2023 appear to have leveled off; rates are lower for the small domestic bank category





# Office Market Status to Date

- Virtually no new product built over last 4 years
- Valuations of office product are depressed 30 to 50 percent
- Demand gradually improving though unevenly; more business formations
- Possible offsetting demand forces:
  - RTO policies are strengthening office attendance and therefore office utilization (Amazon, Instagram require 5 days/week)
  - A softer labor market reinforces an employers' ability to enforce RTO
  - However, weaker hiring / layoffs is reducing office workers overall
- Absorption in San Francisco and San Jose is significantly net positive
  Asking rents rising sharply in the peninsula and Santa Clara County

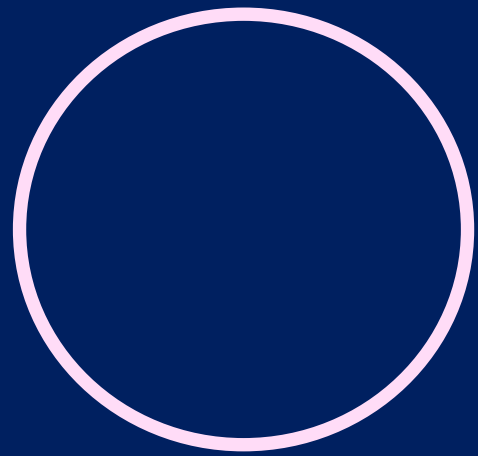


# Office Vacancy Rates

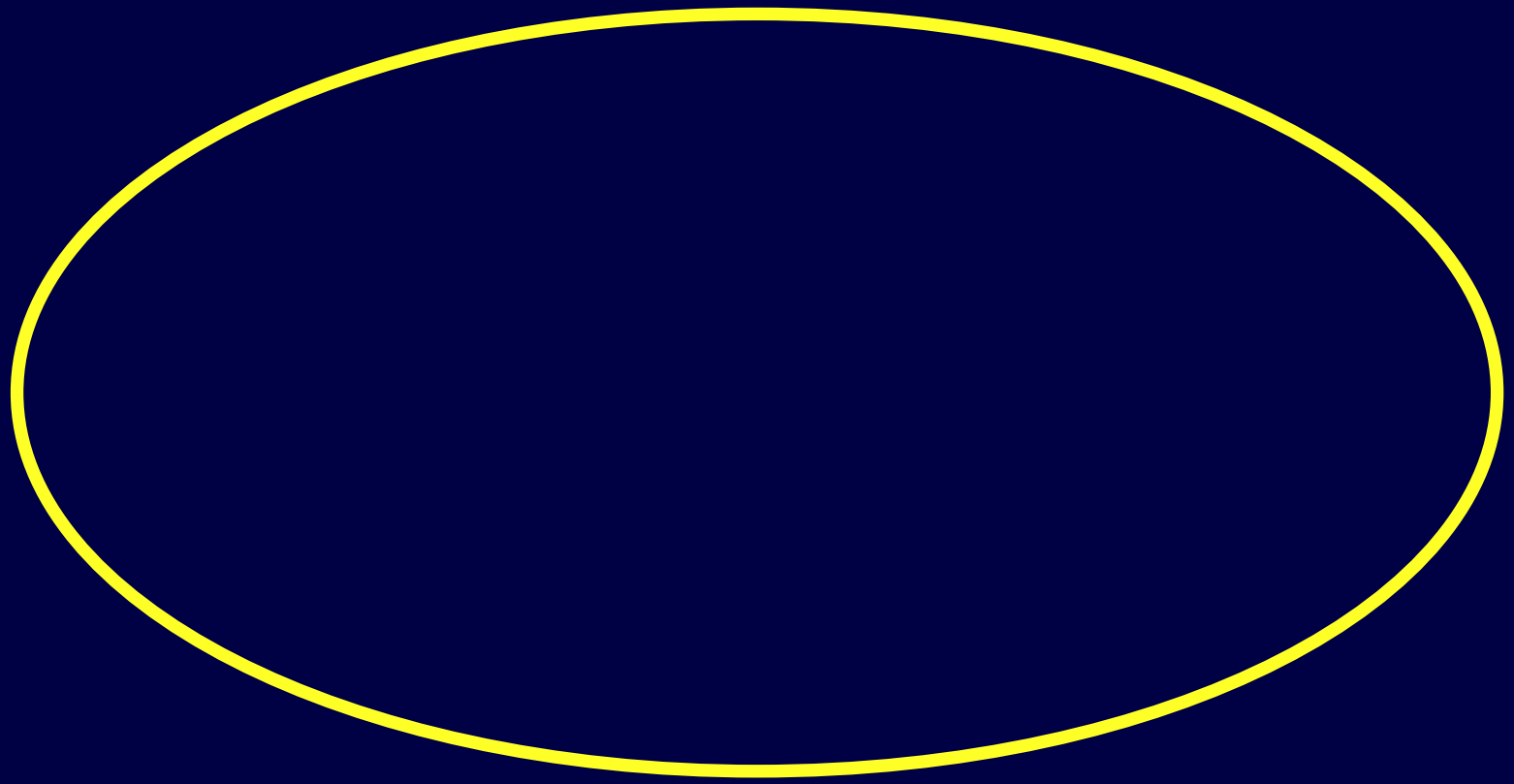
| | 2025 Q3 | 2026 Q3 | |
|---|---|---|---|
| ➢ San Francisco . . . . . | 31.1 | 27.7 | down |
| ➢ San Jose . . . . | 19.1 | 17.8 | down |
| ➢ Los Angeles County. . . | 24.8 | 25.3 | up |
| ➢ Los Angeles Downtown. . . | 33.3 | 34.0 | up |
| ➢ Orange County . . . . | 13.2 | 12.1 | down |
| ➢ San Fernando Valley . . . . | 20.4 | 19.8 | down |
| ➢ San Diego County. . . . | 14.2 | 13.6 | down |
| ➢ San Mateo County . . . | 22.1 | 21.4 | down |

# Further Office Market details

- Class A office vacancy remains clearly higher than classes B and C
- Net Office Absorption in 2026 Q3
  - Orange County: + 100,000 SF
  - San Diego County: + 64,000 SF
  - Los Angeles County: + 235,000 SF
  - San Francisco: +1,068,000 SF and + 3 million Y-T-D
  - San Mateo County: + 133,200 SF and + 600,000 SF Y-T-D
  - Silicon Valley: + 491,000 SF and +1.2 million Y-T-D
  - East Bay: - 84,429 SF
- Inland Empire office market appears stable with office availability at 6.5 percent, a big improvement over year ago







Intellectia Product Resources Markets News Partner Program

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# Microsoft Announces 9,000 Layoffs Amid AI Investments

Written by John R. Smitmithson, Senior Financial Analyst & Columnist




July 2, 2025

Microsoft
6,000 in May
9,000 in July

Meta: 3,600
February 2025

Intel: 24,000
July 2025

Google:
Series of cuts over
April, May, June, August

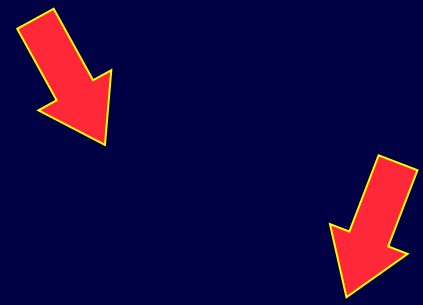



**August 5, 2025**

**Challenger report: 10,000 + job layoffs in first 6 months of 2025**

**January 2025 – August 2026**
**160,000 layoffs**





# ChatGPT



Technical consulting
Scientific consulting
Computer systems design
Data Processing
Web development, hosting

falling
like a rock



# Quiz 3: What do think about AI ?

(1) I've never been more ready . . . . It's a powerful tool that can augment human abilities

(2) It can handle the boring tasks so that I can focus on creative and relational work

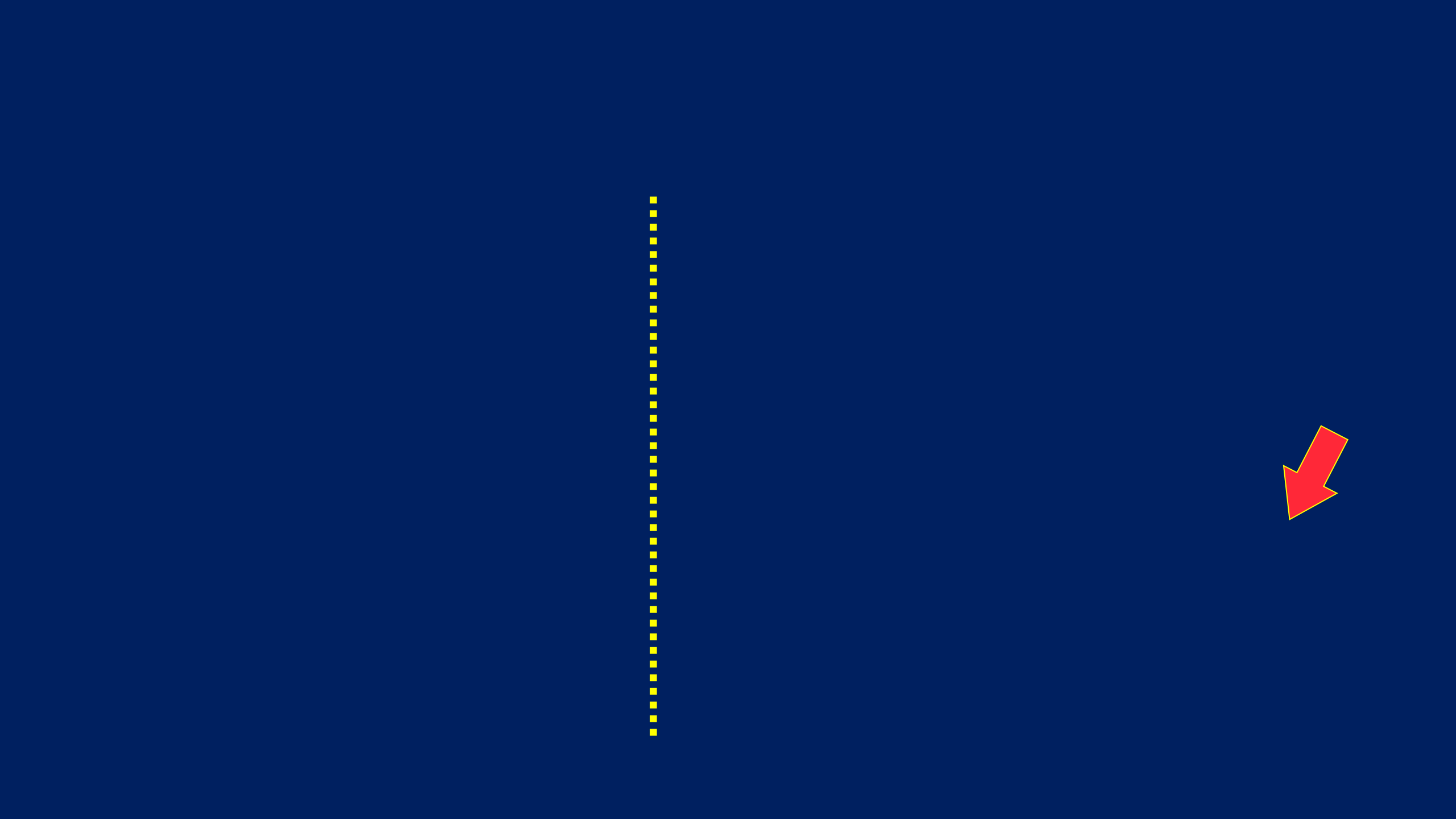
(3) It will disrupt my job, other jobs and my privacy !

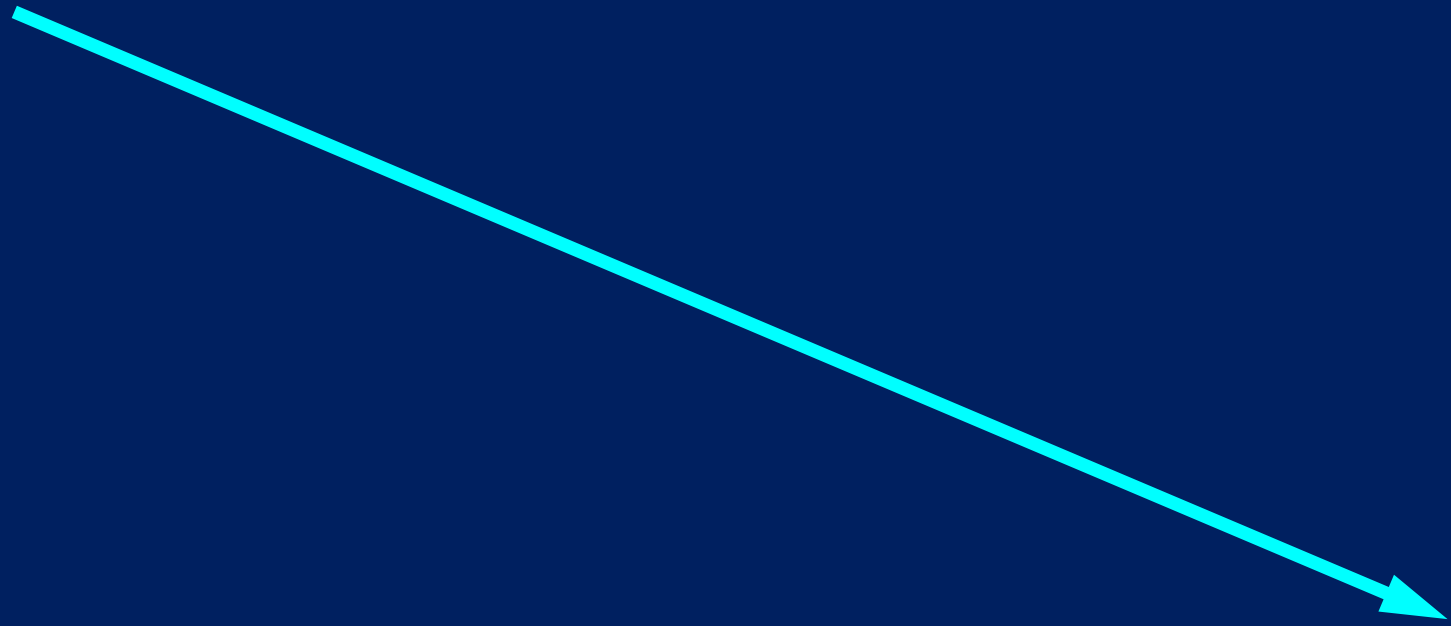
(4) Super strong guardrails are needed as it is prone to annihilate the human race

(5) I can't wait to replace my board of directors with Optimus 4

# Your new board of directors



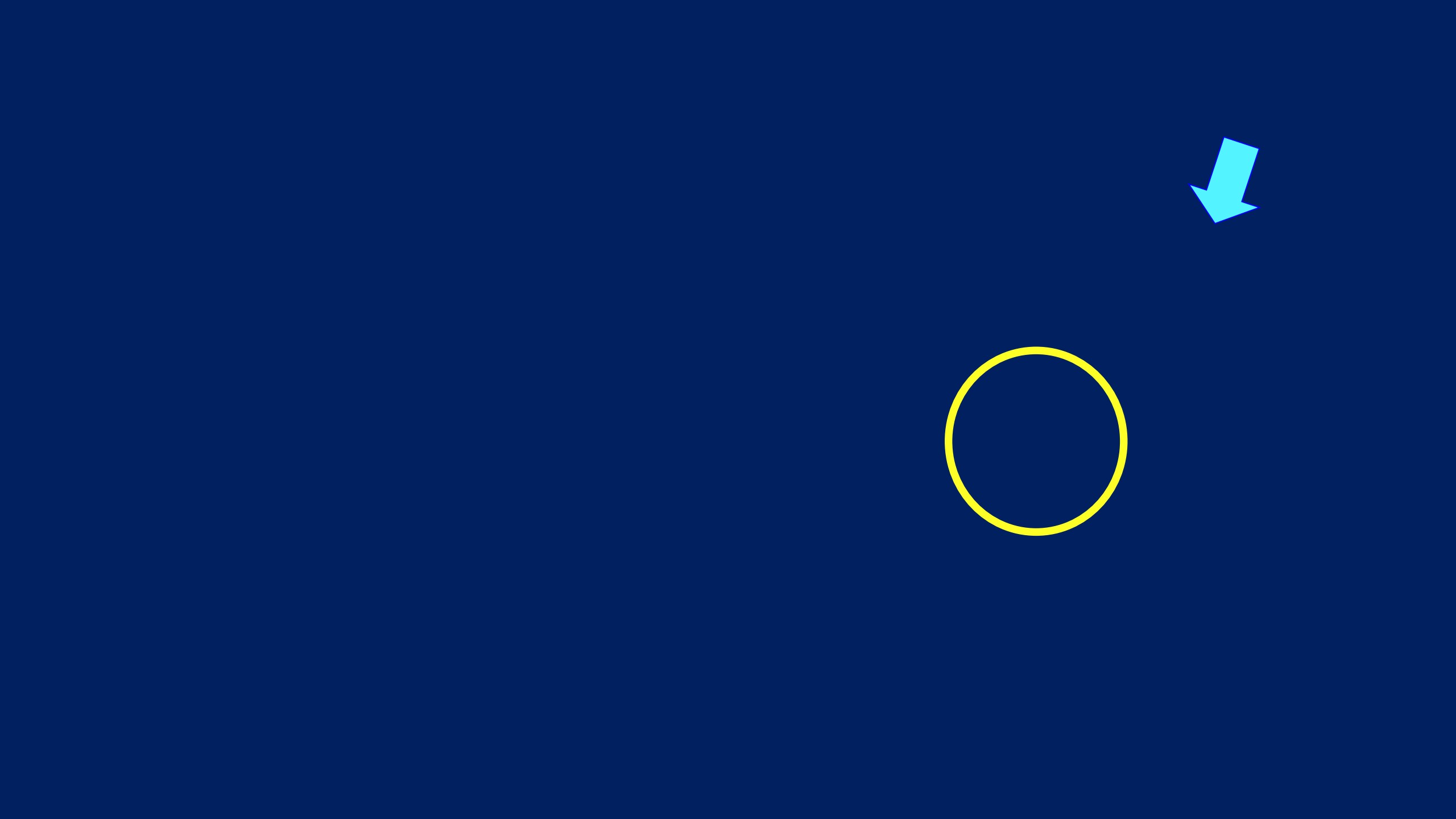






# AI Adoption Levels • 2026

- Technology and Telecom
  - Software, IT automation, content customization — 87%
- Financial Services
  - Fraud detection, credit scoring, trading — 85 %
- Healthcare and Pharma
  - Physicians — 66 %
  - Documentation, Radiology, Imaging — 75 %
- Retail
  - demand forecasting, marketing, inventory — 59%
- Agriculture & Construction
  - precision farming, logistics, site safety — 1 %



El Segundo
Hawthorne
Long Beach
Irvine
Huntington Beach
Antelope Valley
Santa Clarita Valley



# The 2027 Forecast

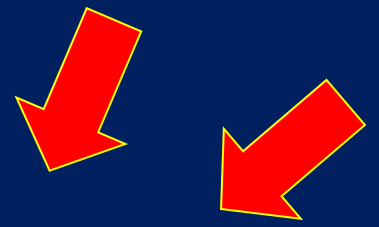


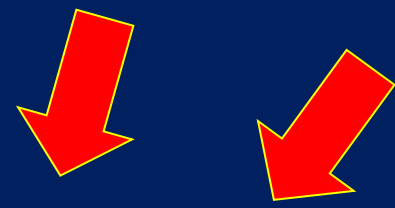
# The 2027 Forecast

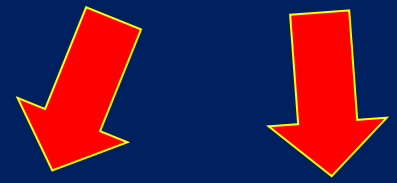
- Growth of the general economy reported at 3.5 percent in Q3. Expectations are for 2.2 (FED) to 3.3 percent growth in Q4
- Growth of employment and output in 2027 to eclipse 2026 rates
  - Less caution in hiring though AI disruption remains a threat
- Consumer spending and business investment not likely to contract much next year; AI adoption to broaden
  - Faster growth is dependent on longer term interest rates
- Industrial demand to absorb most available industrial space
  - Office market continues steady but slow improvement

# The 2027 Forecast

- Creation of jobs to remain positive but numbers are modest
  - Downsizing in white collar jobs to continue
  - Upsizing in manufacturing sectors, and the extent may surprise to upside
- California labor market to improve modestly with job creation in advanced mfg including aerospace, and technology
- Gradual improvement in the new and existing home markets
  - Uncertainty heightened by the war, inflation and interest rates will remain until more evident improvement emerges





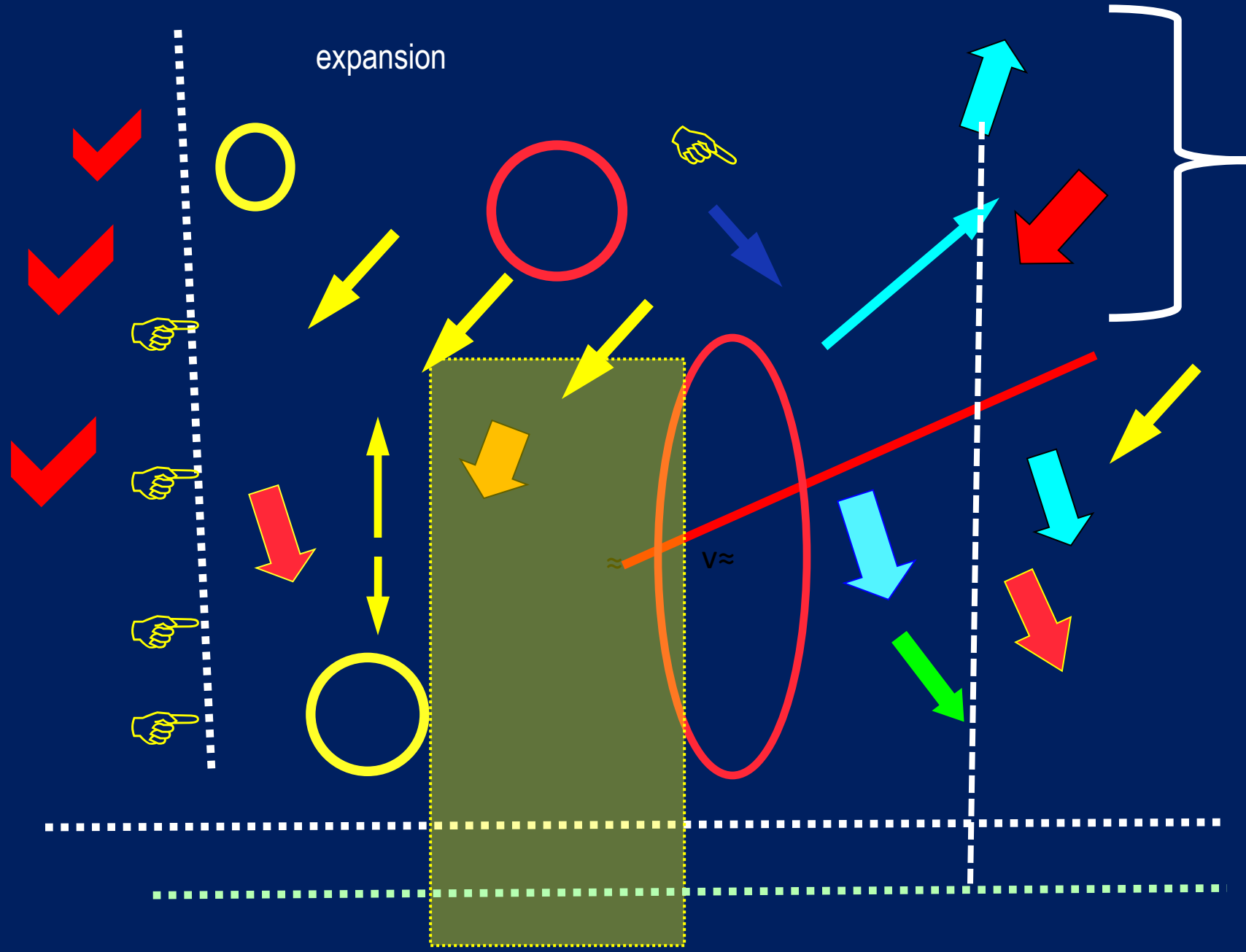


# The end:
# thank you

**November 3, 2026**

**Mark Schniepp**
**Director**




expansion
V≈