February 2022

NCUA's supervisory stress test (SST) consists of baseline and severely adverse scenarios, which regulation requires the NCUA to provide by 28 February each year. As in past SST exercises, the NCUA's 2022 SST scenarios follow the domestic scenarios published by the Federal Reserve Board of Governors (FRB) for the CCAR and DFAST exercises.

The near-term portion of the baseline scenario is similar to the January 2022 consensus projections from *Blue Chip Economic Indicators* and *Blue Chip Financial Forecasts*. The scenario's long-range forecast is comparable to the October 2021 *Blue Chip* releases. The severely adverse scenario depicts a hypothetical prolonged remote work environment which increases commercial real estate losses and negatively affects companies and investor sentiment. These scenarios follow the FRB's Policy Statement on the Scenario Design Framework for Stress Testing and do not represent forecasts of the NCUA or the FRB.[1]

A summary of each scenario follows:

<u>Baseline Scenario</u> - The baseline scenario is an economic expansion over the 13-quarter scenario.

- Real GDP decreases from 5.9 percent at the end of 2021 to 2.0 percent for the last three quarters of the scenario.
- Unemployment starts at 4.0 percent and gradually decreases to 3.6 percent at the end of the scenario.
- CPI inflation drastically falls from 8.2 percent at the end of 2021 to 2.2 percent for most of the last four quarters of the scenario.
- Short-term Treasury rates start at 0.1 percent and increase to 1.5 percent in 2024 Q1 and remain there through the rest of the scenario.
- 10-year Treasury securities rise from 1.7 percent to 2.6 percent over the 13-quarter scenario.
- Prime rates move in line with short-term Treasury rates. Mortgage rates and corporate bond yields rise in line with long-term Treasury rates.
- Equity prices remain constant through the scenario, and equity volatility varies little over the scenario.
- Housing prices rise 11.4 percent at the beginning of the scenario. The rate of increase drops to 3 percent by 2022 Q3 and stays there for the rest of the scenario. Commercial real estate prices follow a similar trend, starting at 8.6 percent and plateau at 3 percent in 2022 Q4.

[1] 12 CFR 252 Appendix A

Severely Adverse Scenario – The severely adverse scenario characterizes a severe global recession with considerable stress on commercial real estate and corporate debt.

- Real GDP falls in 2021 Q1 to -1.4 percent and stays negative until 2023 Q2. Real GDP rapidly grows in three quarters to 6.6 percent and gradually declines to 4.9 percent by 2025 Q1.
- Unemployment increases in the scenario's first quarter and peaks at 10 percent in 2023 Q3. Unemployment slow decreases through the rest of the scenario.
- Inflation drops by over 70 percent in 2022 Q1 to 2.3 percent and remains between 1.3 percent and 1.6 percent through 2025 Q1.
- Short-term Treasury remain at 0.01 percent for the entire scenario.
- The 10-year Treasury rate immediately falls to 0.7 percent and increases to 1.5 percent at the end of the scenario.
- Investment-grade yields immediately increase to 5.4 percent and increase through 2022 Q4 to 6.6 percent. Corporate rates gradually decrease to 3.8 percent by scenario end. Mortgage rates increase to 3.8 percent in 2022 Q4, remain there for one quarter and decrease to 3.2 percent in 2025 Q1.
- The House Price and Commercial Real Estate Price indices fall sharply through 2023 Q4 and modestly increase from the low by the end of the scenario.
- Equity prices fall by 45 percent in the scenario's first quarter and continue to decline through 2022 Q4. Equity prices rally back up to 2021 Q4 levels in 2025 Q1.