Invictus Oil Price Shock and Stagflation Scenario

Version 1.0, as of April 30, 2026

Scenario Purpose and Design

The Invictus Oil Price Shock and Stagflation Scenario is intended to reflect—but not predict—a severe tail-risk outcome for the U.S. economy driven by a sudden and sustained energy supply shock. The scenario is designed for stress testing, capital planning, and risk management purposes, and is calibrated using the same core macroeconomic and financial market variables utilized in the Federal Reserve's CCAR framework, with oil prices included as explicit satellite variables.

Unlike demand-driven recessions or financial crises, this scenario analyzes a supply-driven inflation shock that constrains monetary policy, produces persistent price pressures, and results in weaker economic activity alongside rising unemployment.

Scenario Trigger and Oil Market Assumptions

The scenario assumes that an abrupt geopolitical or supply-side disruption causes oil prices to rise sharply at the jump-off quarter (2026Q2). WTI crude oil reaches approximately $150 per barrel by the end of 2026Q2 and peaks modestly above that level in the low-$150s during 2026Q3, with Brent crude following a slightly higher but similar trajectory.

Oil prices remain elevated through late 2026 before gradually moderating as global demand softens and marginal supply responds. Importantly, the scenario assumes persistence rather than a brief spike, ensuring second-round inflation effects and sustained pressure on households and businesses.

Macroeconomic Transmission Mechanism

Higher energy prices act as a broad-based tax on the economy. Transportation, utilities, and energy-intensive industries experience immediate cost pressures, while households face reduced real disposable income due to higher prices for fuel, goods, and services.

INVICTUS ANALYTICS

Consumer spending slows, corporate margins compress, and capital investment is delayed or canceled. These forces lead to a contraction in real GDP that is meaningful but not as deep as the Global Financial Crisis, reflecting the absence of widespread financial system failure.

GDP, Labor Markets, and Inflation Dynamics

Real GDP contracts in the scenario and recovers only gradually. The downturn is prolonged by persistent inflation pressures and restrictive financial conditions. Unemployment rises with a lag, ultimately peaking in the high-7% range before slowly improving in the outer years as inflation moderates.

Inflation rises sharply due to direct energy pass-through and second-round pricing effects. CPI is already elevated in the jump-off quarter and spikes further in 2026, remaining above target for an extended period before gradually decelerating.

Monetary Policy Response and Interest Rates

In the jump-off quarter (2026Q2), the Federal Reserve is assumed to be flat-footed and holds the effective fed funds rate approximately unchanged versus 2026Q1 despite rising CPI. As inflation accelerates further, the Fed responds with a 75 basis point increase in 2026Q3, followed by another 75 basis point increase in 2026Q4.

Policy tightening is capped thereafter as rising unemployment and weakening economic activity constrain further increases. Long-term Treasury yields remain elevated, reflecting inflation risk premia and term premia, even as growth deteriorates.

Key Sanity-Check Metrics

Real Interest Rate Proxy (EFFR – CPI): Real short-term interest rates remain negative for much of the scenario horizon, consistent with a delayed and constrained policy response to a supply-driven inflation shock. As CPI gradually decelerates later in the scenario, real rates move toward zero or mildly positive levels without requiring aggressive additional tightening.

Yield Curve Slope (10-Year – 3-Month Treasury): The yield curve flattens and inverts as short-term rates rise while inflation remains elevated. Given the stagflationary environment, the curve remains flat or inverted longer than in a deep demand-driven recession and only normalizes gradually once policy easing becomes feasible.

Asset Prices and Financial Conditions

Equity prices decline materially due to weaker earnings expectations and higher discount rates. Financial conditions tighten across credit markets as risk spreads widen and capital availability contracts.

Housing Market Impacts

Residential housing prices decline approximately 25% from pre-stress levels. Rising unemployment, elevated mortgage rates, and affordability shocks contribute to forced selling, particularly in highly leveraged markets and regions with energy-sensitive employment bases.

Commercial Real Estate Impacts

Commercial real estate prices decline approximately 30%. The decline reflects both falling net operating income due to higher vacancy rates and rising capitalization rates driven by higher long-term Treasury yields and risk premia.

Retail and office properties are particularly exposed, while development and transitional assets face additional challenges from higher financing costs and reduced capital availability.

Illustrative NOI and Cap Rate Decomposition

CRE valuation is modeled as NOI divided by the capitalization rate. At the trough, the scenario implies a meaningful decline in NOI alongside an approximately 125 basis point increase in cap rates. The multiplicative interaction of these factors reconciles to the modeled 30% decline in CRE prices. An illustrative decomposition is included in the accompanying spreadsheet.

Sectoral Implications

Energy-intensive industries, transportation, manufacturing, logistics, construction, and discretionary consumer sectors experience disproportionate stress. Regional economies with concentrated exposure to these industries are subject to higher unemployment and secondary spillover effects.

Impact on Financial Institutions

Banks are affected heterogeneously based on balance sheet composition, funding mix, asset duration, geographic footprint, and exposure to real estate and rate-sensitive lending. This scenario differs materially from standard recession templates because inflation remains elevated and long-term rates do not rally meaningfully during the downturn.

As a result, stress test loss dynamics, capital ratios, and net interest income behavior may differ substantially from outcomes observed under demand-driven recession scenarios.

Conclusion

The Invictus Oil Price Shock and Stagflation Scenario provides a coherent and structurally distinct stress environment designed to test institutional resilience under persistent inflation, constrained monetary policy, and weakening economic conditions. By explicitly incorporating oil prices and stagflation dynamics, the scenario complements traditional CCAR-style stress tests and enhances risk management insight.

Summary of Scenario

Quarter	Segment	Real GDP Growth Rate (%)	Nominal GDP Growth Rate (%)	US Unemployment Rate (%)	CPI Inflation Rate (%)	Effective Fed Funds Rate (%)	3-Month Treasury Rate (%)	5-Year Treasury Rate (%)	10-Year Treasury Rate (%)	EFFR - CPI (Real Interest Rate Proxy)	Yield Curve Slope (10-Year less 3-Month)	BBB Corporate Yield (%)	30-Year Mortgage Rate (%)	Prime Rate	Cumulative Pct Change in DJIA	Cumulative Pct Change in Housing Prices	Cumulative Pct Change in CRE Price Index	VIX	WTI Spot Price ($per barrel)	Brent Spot Price ($per barrel)
2024Q1	Historical	1.6	4.7	3.8	3.8	5.1	5.2	4.1	4.2	1.3	-1	5.6	6.7	8.5	-10.27	-3.94	-2.52	15.9	82	86
2024Q2	Historical	3	5.6	4	2.8	5.1	5.2	4.5	4.5	2.3	-0.7	5.8	7	8.5	-7.68	-3.64	-3.79	19.2	76	80
2024Q3	Historical	3.1	5	4.2	1.2	4.9	5	3.8	4	3.7	-1	5.3	6.5	8.4	-2.32	-2.73	-2.84	38.6	68	72
2024Q4	Historical	2.3	4.6	4.1	2.7	4.3	4.4	4.1	4.3	1.6	-0.1	5.4	6.6	7.8	0	-2.42	-2.52	27.6	70	74
2025Q1	Historical	2.1	4.5	4.3	2.8	4.2	4.3	4.2	4.4	1.4	0.1	5.6	6.4	7.6	0	-1.82	-1.89	26.7	68	75
2025Q2	Historical	1.9	4.4	4.3	2.7	3.9	4	4.1	4.4	1.2	0.4	5.7	6.2	7.4	0	-1.52	-1.58	26.6	68	67
2025Q3	Historical	1.9	4.4	4.3	2.6	3.8	3.9	4	4.3	1.2	0.4	5.8	6.1	7.2	0	-0.91	-0.95	26.6	64	68
2025Q4	Historical	1.9	4.5	4.3	2.6	3.7	3.8	4	4.3	1.1	0.5	5.8	6	7	0	-0.3	-0.32	26.8	58	61
2026Q1	Prelim	2	4.7	4.3	2.8	3.6	3.7	4	4.2	0.8	0.5	5.8	5.9	6.9	0	0	0	27	91	103
2026Q2	Scenario	0.5	3.5	4.4	3.8	3.6	3.75	4	4.2	-0.2	0.45	5.8	6.1	6.75	0	0	0	22	150	153
2026Q3	Scenario	-0.75	2.25	5	6.5	4.35	4.5	4.35	4.55	-2.15	0.05	6.55	6.6	7.5	-5	-4	-5	40	153	156
2026Q4	Scenario	-2	1	5.6	6.25	5.1	5.25	4.7	4.9	-1.15	-0.35	7.3	7.1	8.25	-10	-8	-10	42.5	151	154
2027Q1	Scenario	-2.5	0.5	6.2	6	5.1	5.24	4.95	5.1	-0.9	-0.14	7.8	7.5	8.24	-15	-12	-14	45	148	151
2027Q2	Scenario	-3	0	6.8	5.5	5.1	5.22	5.2	5.3	-0.4	0.08	8.3	7.9	8.22	-20	-16	-18	41.5	145	148
2027Q3	Scenario	-2	0.75	7.2	5	5.07	5.19	5.25	5.35	0.07	0.16	8.25	7.85	8.19	-25	-19	-22	38	140	143
2027Q4	Scenario	-1	1.5	7.6	4.67	5.05	5.15	5.3	5.4	0.38	0.25	8.2	7.8	8.15	-27.5	-22	-26	36	135	138
2028Q1	Scenario	-0.25	2.25	7.8	4.33	5	5.1	5.25	5.35	0.67	0.25	7.95	7.65	8.1	-30	-25	-30	34	130	133
2028Q2	Scenario	0.5	3	7.6	4	4.95	5.05	5.2	5.3	0.95	0.25	7.7	7.5	8.05	-26	-24	-29	32	125	128
2028Q3	Scenario	0.75	3.2	7.4	3.78	4.89	4.99	5.15	5.25	1.11	0.26	7.58	7.4	7.99	-22	-23	-28	31	120	124
2028Q4	Scenario	1	3.4	7.2	3.55	4.82	4.92	5.1	5.2	1.28	0.27	7.45	7.3	7.92	-19.67	-21.33	-26.67	30	115	119
2029Q1	Scenario	1.25	3.6	7	3.32	4.76	4.86	5.05	5.15	1.44	0.29	7.32	7.2	7.86	-17.33	-19.67	-25.33	29	110	114
2029Q2	Scenario	1.5	3.8	6.8	3.1	4.7	4.8	5	5.1	1.6	0.3	7.2	7.1	7.8	-15	-18	-24	28	105	110

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