Bond iQ
Intra Quarter Update

The Recession Scorecard – An Objective Guide to Recession Forecasting

If there's one question we're asked more often than any other, it has to be "What are the odds we're heading into a recession?" As the current economic recovery continues aging, any whiff of equity or credit market volatility is often met with a healthy dose of recession fear. While predicting turning points in the economic cycle is admittedly difficult, we find that having an objective framework can help guide rational macroeconomic decision making. In this month's "Bond iQ", we introduce our Recession Scorecard – a compilation of 17 key pieces of market and economic data that have proven to be reliable indicators of turning points in the economic cycle.

RECESSION SCORECARD*

INDICATOR	RECESSION RULE	REGENT SIGNAL	RECESSION Y/N	2018	2007	2001	1990
MARKET-BASED:							
YIELD CURVE	10YR Treasury – FF IS NEGATIVE	22	NO	NO	YES	YES	NO
IG CORP SPREADS	ABOVE 150	121	NO	NO	YES	YES	NO
HY CORP SPREADS	ABOVE 500	388	NO	NO	YES	YES	NO
STOCK MARKET	DECLINE 11% FROM PEAK	-3.9%	NO	NO	NO	YES	NO
LABOR MARKET:							
JOBLESS CLAIMS (4 WK AVG)	ABOVE 360K	224	NO	NO	NO	YES	YES
UNEMPLOYMENT RATE	+0.5% FROM BOTTOM	0.1%	NO	NO	YES	NO	NO
TEMP EMPLOYMENT	BELOW -1% YOY	2.4%	NO	NO	YES	YES	NO
AVG WEEKLY HOURS	-0.5% YOY	0.3%	NO	NO	NO	YES	YES
BROAD ECONOMY:							
LEADING INDICATORS	-2% YOY	3.5%	NO	NO	YES	YES	NO
COIN/LAGGING INDEX	96.3 OR BELOW	99.0%	NO	NO	NO	NO	NO
ECRI WEEKLY LEADING INDEX	-10% OR BELOW	-3.7%	NO	NO	NO	NO	NO
MANUFACTURING:							
ISM MANUFACTURING	BELOW 47	54.2	NO	NO	NO	YES	YES
CAPACITY UTILIZATION	4 PTS BELOW PEAK	-1.4	NO	NO	NO	YES	NO
NONDEFENCE CAP GOODS EX. AIRCRAFT	3-MTH AR -10% OR BELOW	-5.3%	NO	NO	NO	YES	NO
CONSUMER:							
HOUSING STARTS	-35% YOY	-7.8%	NO	NO	YES	NO	NO
RETAIL SALES EX. GAS	3-MTH RATE BELOW 0%	0.5%	NO	NO	YES	YES	NO
CONSUMER SENTIMENT	15 PTS BELOW PEAK	-7.6	NO	NO	YES	NO	NO

*Data as of March 2019

While there is no magic number of declining data points to formally affirm a recession, the scorecard framework has been an invaluable tool to help us identify elevated risks of economic turning points. On average, the Recession Scorecard has generated eight warning signals prior to the onset of the past three economic recessions. Once the scorecard begins to identify advanced warning signals, it triggers a deeper dive into the economic data to make a more formal recession forecast.

In addition to helping us accurately identify past downturns, the Scorecard has also helped us avoid falsely calling recessions that were just cyclical slowdowns. The fourth quarter of last year was a perfect example. The stock market fell almost 20% in the final few months of the year, causing many to call the end of this recovery. But as the Scorecard above indicates, none of the economic data that we follow had yet moved into recessionary territory. Using the objective Scorecard framework helped us to swim against the tide of market sentiment and accurately avoid calling for a recession. Like good fixed income management, it's imperative to have an objective discipline when performing macroeconomic analysis. For more information on how we apply our Scorecard framework to recession forecasting, please feel free to reach out to us.

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