

Thinking Out Loud



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The Waiting Is The Hardest Part

- We continue to wait for the most anticipated recession in modern times to materialize, despite posturing by the [Federal Reserve](#)¹ and several sell-side [Wall Street firms](#)² either pushing back recession timing or entirely capitulating to the “soft-landing” camp. The most recent flip-flop comes from [Bank of America/Merrill Lynch](#)³.
- We remind investors that soft landings have occurred only [three times](#)⁴, dating back over the eight (8) recessions since 1961. But regardless of all this “institutional” pushback, we continue to suggest it may be difficult for the U.S. to entirely avoid a typical hard landing over the next 12 months.
- We reiterate our recession position published in our [2023 Outlook](#)⁵, that any potential recession will be shallow and short, which may mirror the two downturns prior to 2007. Therefore, multiple contraction associated with any possible recession could be less severe than witnessed during the 2007-2009 Great Recession (roughly a 40% contraction to approximately 8.8x).
- Hence, we also reiterate our near-term S&P 500 target of roughly 4,200 (down 8-9%), which implies an 18.3x multiple on 2024 FactSet consensus S&P earnings, compared to the current forward 12-month multiple of 19.1x and the long-term average dating back through 1997 of 16.9x.
- We believe this multiple premium of 18.3x (vs. 16.9x) could hold, given the [National Bureau of Economic Research](#)⁶ (NBER) is typically late to the party in determining shorter recessions. For example, the NBER did not even declare the 8-month 1991 recession until after it ended. Further, the NBER did not announce the U.S. was in the midst of the 2001 recession until four (4) months after it started.
- The most compelling evidence supporting our recession view is the massively inverted yield curve (10yr less Fed Funds), which has portended every recession dating back through the early 1970s. But not just one trend or concept drives our more cautious economic call moving forward.
- [Demand destruction](#)⁷ is beginning to materialize across the economy, with more restrictive expectations moving forward. Student loan forbearance ends in September, while the recent [Senior Loan Officer Opinion Survey](#)⁸ suggests bank lending is becoming more restrictive. Adding to bank headwinds is the recent [Moody's](#)⁹ downgrade in the face of ongoing [commercial real estate concerns](#)¹⁰. Further, credit card default and borrowing rates are surging higher, and the [Index of Leading Economic Indicators](#)¹¹ has been in recession territory for some time now. In addition, the [ISM Manufacturing PMI](#)¹² is signaling a recession, while the ISM Services PMI is also showing weakness.
- But there are sparse green shoots. The most recent of which is the [National Federation of Independent Business Optimism Index](#)¹³, which has increased for three (3) consecutive months. The June print was 91, a 1.6-point increase from May. However, the June reading also marked the 18th consecutive month below the longer-term average of 98. And while the share of business owners reporting that obtaining credit was unchanged, the recent downgrade of regional banks (who small businesses are beholden to) may portend further tightening in credit as we move through the back half of 2024. Finally, the recent rebound in the NFIB Optimism Index coincides with the recent surge in the S&P. And while Investment-Grade and Junk-Bond spreads to the 10yr remain tight, they typically bottom just before a recession starts.

We'd love to hear your thoughts!

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- ¹ <https://www.reuters.com/markets/us/fed-staff-no-longer-forecasting-us-recession-powell-says-2023-07-26/>
- ² <https://www.cnbc.com/2023/07/18/goldman-sachs-cuts-odds-of-a-us-recession-in-the-next-year.html>
- ³ <https://www.cnbc.com/2023/08/04/what-predictions-of-a-soft-landing-no-recession-mean-for-you.html>
- ⁴ <https://www.alger.com/Pages/OnTheMoney.aspx?pageLabel=AOM275>
- ⁵ <https://static.fmgsuite.com/media/documents/a2342421-7e47-427e-b1bf-0f54454025c7.pdf>
- ⁶ <https://www.nber.org/research/data/us-business-cycle-expansions-and-contractions>
- ⁷ <https://www.investopedia.com/demand-destruction-5222107>
- ⁸ <https://www.reuters.com/business/finance/us-banks-report-fighter-credit-weaker-loan-demand-fed-survey-2023-07-31/>
- ⁹ <https://www.reuters.com/markets/us/moodys-downgrades-10-us-banks-warns-possible-cuts-others-2023-08-08/>
- ¹⁰ <https://www.insurancejournal.com/news/east/2023/08/08/734339.htm>
- ¹¹ <https://www.conference-board.org/topics/us-leading-indicators>
- ¹² <https://www.ismworld.org/supply-management-news-and-reports/reports/ism-report-on-business/>
- ¹³ <https://www.nfib.com/surveys/small-business-economic-trends/>

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