RECESSION BAROMETER

February 22, 2019

Spotlight on : 10-2 Yield Curve

COMMENT: *Our "recession barometer" kicks in when the "spread" between the 10-year rate and the 2-year rate for Treasuries in the USA and Government of Canada Bonds in Canada reach 0.00x, which means that the yield on the 10s equals the yield on the 2s. If the 10s yield less than the 2s, an "inversion" occurs and then it is likely that a recession will soon follow. Predicting when that will be is the key. Below, we provide various date projections for a possible recession following an inversion.*

Historically, inversions of the yield curve have preceded most U.S. recessions. Thus, the yield curve is considered an important barometer for predicting business cycle turning points. However, it is important to note that, sometimes, a negative yield curve gives a false positive (see the long-term chart on page 4).

The yield curve for the 10s/2s is currently quite "narrow" in both the USA and Canada. Friday's close has the 10/2 for Treasuries at 0.17x and for Canadas at 0.12x. The U.S. spread widened this past week by 3 "beeps", while the Canadian spread rose one "beep".

The following chart shows when a recession could occur for various post-inversion dates. Our current "guess" is 15 months post-inversion (shown in Red). This is a "moving target" and will change with each ensuing quarter. It will also change with changes in global economic conditions.

Forecasting the Commencement of a Recession

If an inversion occurs during the current quarter …	… then a recession will begin at stated date projections.					
Current Quarter	**Inversion +12 Months**	**Inversion +15 Months**	**Inversion +20 Months**	**Inversion +24 Months**	**Inversion +30 Months**	**Inversion +40 Months**
Q1/2019	Q1/2020	Q2/2020	Q3/2020	Q1/2021	Q3/2021	Q2/2022

Source: eResearch

*e*Research Corporation
100 University Avenue, 5th Floor • Toronto, Ontario • M5J 1V6
www.eresearch.ca

LATEST READINGS

1. U.S. Treasuries

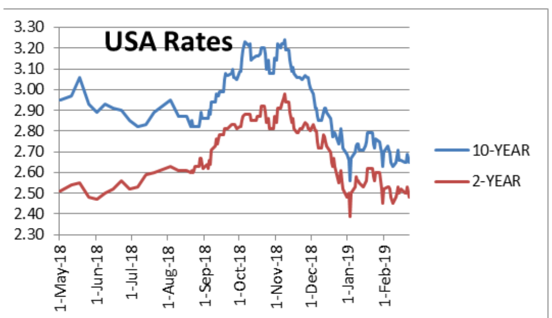
- The 10-year U.S. Treasuries yield blipped up on Thursday, then retraced completely on Friday. Net, it was down slightly, closing at 2.65%, from 2.66%.

- The 2-year U.S. Treasuries yield also rose on Thursday, then dropped on Friday, closing at 2.48%, down from 2.52%.

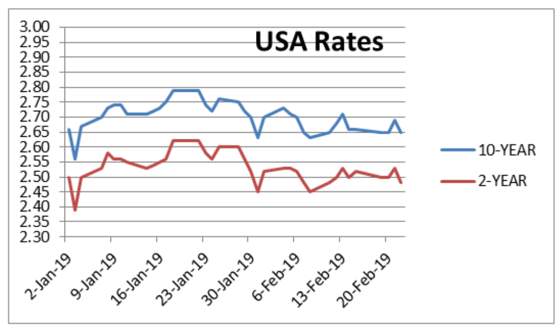
- The 10/2 yield spread rose each day and closed at 0.17x, up from 0.14x last week.

- The first two charts below show the trend in rates since May 1, 2018 and January 2, 2019. The longer-term chart shows that rates rose beginning in September and peaked in November. The subsequent decline reached a low in early January, and then has not moved much. Rates shown on the short-term chart, on the right, is fairly flat.

May 1, 2018 – February 22, 2019

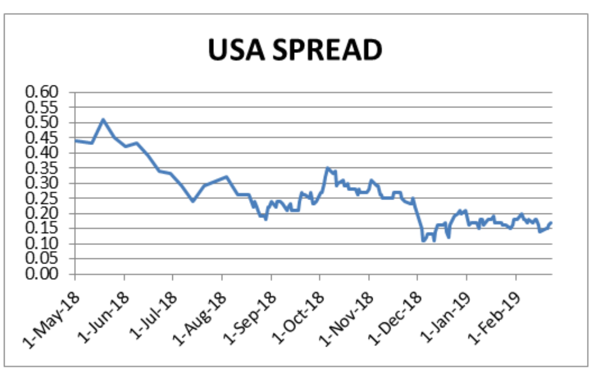


January 2, 2019 – February 22, 2019

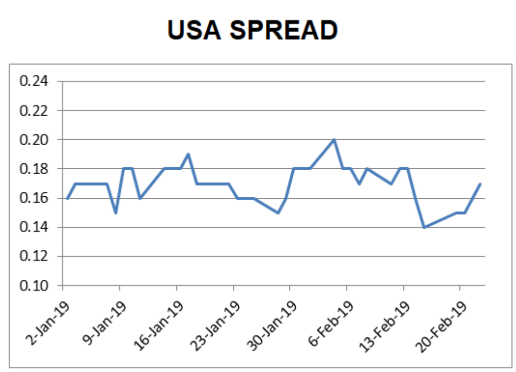


- The next two charts show the "spread" between the 10-year and the 2-year yields. The longer-term chart shows that the spread has declined and reached a low last December. Since then, it has become fairly stable, as borne out on the short-term chart. When the spread gets to "zero", an inversion is imminent.

May 1, 2018 – February 22, 2019



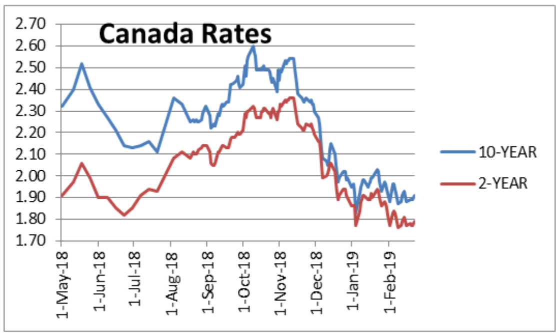
January 2, 2019 – February 22, 2019

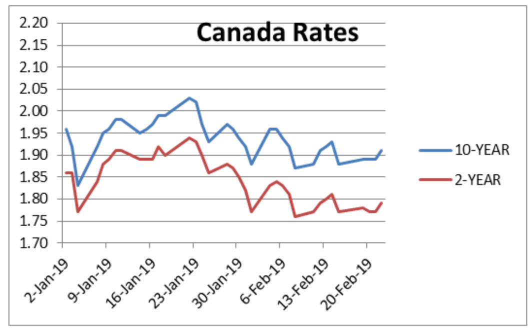


2. Government of Canadas

- The first two charts for Canadas mirror the U.S. Treasuries experience. Rates have declined consistently since last October.

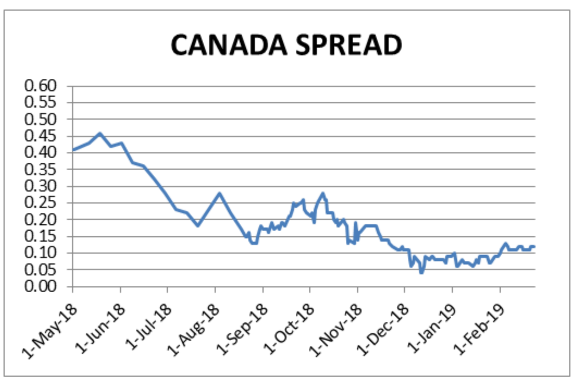
May 1, 2018 – February 22, 2019 | **January 2, 2019 – February 22, 2019**

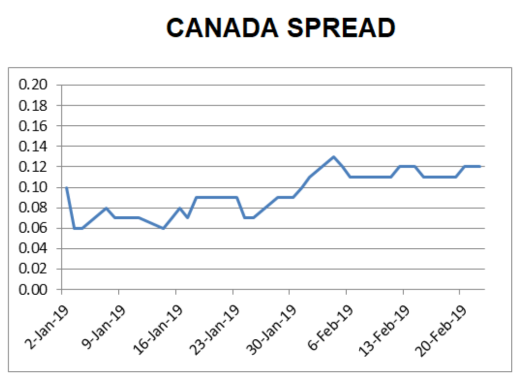




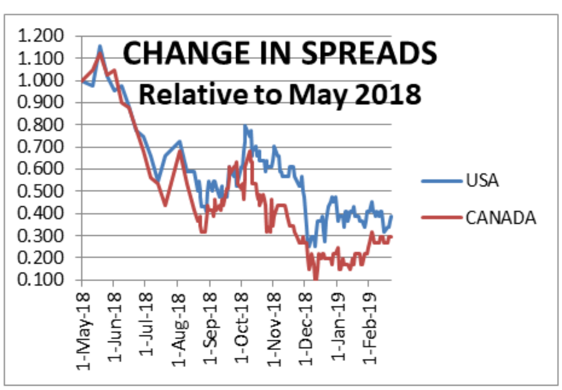
- As shown on the second set of charts the "spread" on Canadas is less than for Treasuries. The Canadas' spread has been very stable since year-end, although it has been rising but become stable at a higher level. It is now at 0.12x, and still well above recession levels of 0.00x.

May 1, 2018 – February 22, 2019 | **January 2, 2019 – February 22, 2019**





The following chart shows the trend in U.S. and Canadian spreads since May 1, 2018:



U.S. Treasuries 10-2 Yield Ratio Since February 1, 1999 (20 Years)

Here is a look at the 10-2 yield curve going back 20 years to February 1999. It shows the negative occurrences (below 0.0x) and the corresponding recessions (shaded areas) that soon followed. Currently, despite the falling trend-line, there is still further to go to reach the inversion level and the possibility of a resulting recession. The current ratio is 0.17x, up from 0.14x one week ago, but comfortably above the 0.00x inversion level.

CONCLUSION

- Despite the lower trending spread that is currently occurring, U.S. economic growth still continues positively, although signs of global slowing could start to impact the USA as well as slower growth from its own making. However, the possibility of a near-term recession in the United States seems remote at this point. Still, our concerns for global economic growth, North American economic growth, the possibility of dysfunctional government in the USA from time to time, and the negative effects of trade wars and ignoble tariffs, cause us to consider the possibility of a recession hitting U.S. shores in 12-15 months after a 10/2 yield curve inversion occurs. We are not there yet, and the trend towards inversion has stalled since the beginning of this year.

Bob Weir, CFA: Contributing Analyst

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