RECESSION BAROMETER

March 1, 2019

Spotlight on : 10-2 Yield Curve

COMMENT: *Rates are rising. So, too, are spreads. This means, the recession barometer indicator is rising and a consequent economic recession is lessening.*

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, but the "spread" "blipped" up this past week in both countries. Friday's close has the 10/2 spread for Treasuries at 0.21x, up from 0.17x at the end of the previous week. In Canada, it was 0.16x up from 0.12x.

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. For now, we are holding with our 15-month time-frame.

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

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LATEST READINGS

1. U.S. Treasuries

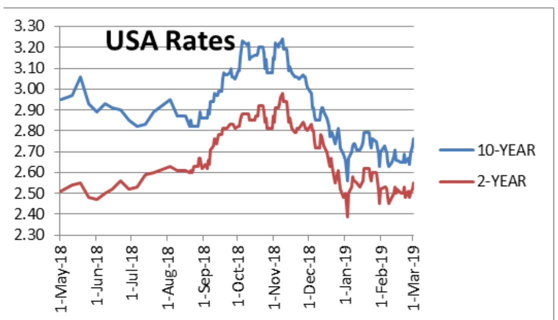
- The 10-year U.S. Treasuries yield jumped this past week, rising steadily since Tuesday. It closed at 2.76% up from 2.65%.

- The 2-year U.S. Treasuries yield followed suit, closing at 2.55%, up from 2.48%.

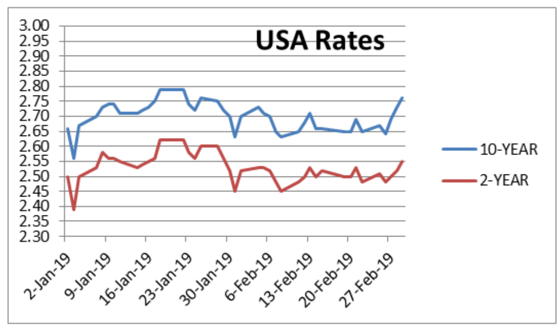
- The 10/2 yield spread rose over the wek and closed at 0.21x, up from 0.17x last week.

- 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, are fairly flat, until last week.

May 1, 2018 – March 1, 2019

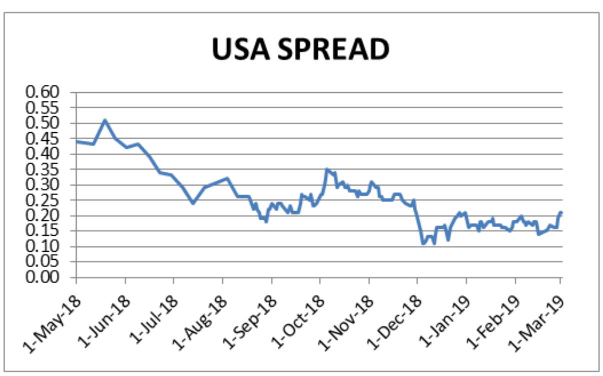


January 2, 2019 – March 1, 2019

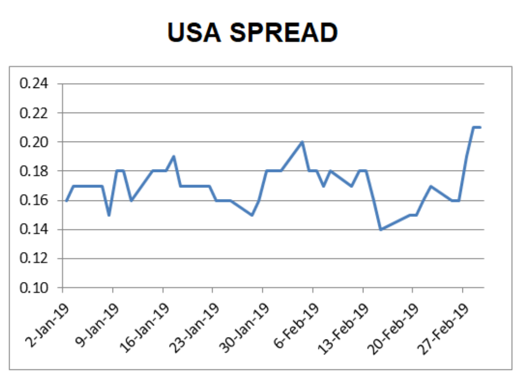


- The next two charts show the "spread" between the 10-year and the 2-year yields. The longer-term chart shows that the spread has declined and reached a low last December. Since then, it has become fairly stable, as borne out on the short-term chart, although it has risen these last two weeks. When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

May 1, 2018 – March 1, 2019



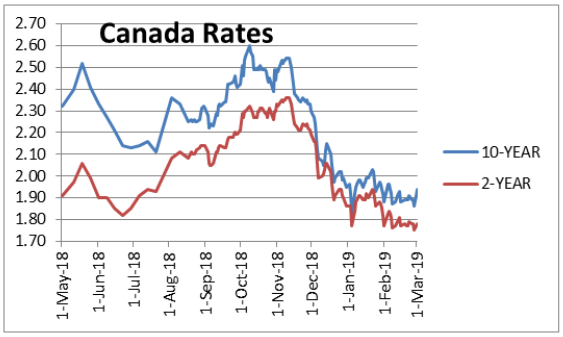
January 2, 2019 – March 1, 2019

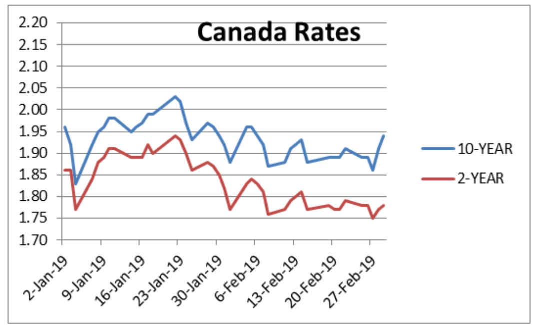


2. Government of Canadas

- The first two charts for Canadas mirror the U.S. Treasuries experience. Rates have declined consistently since last October, but they are trending up again.

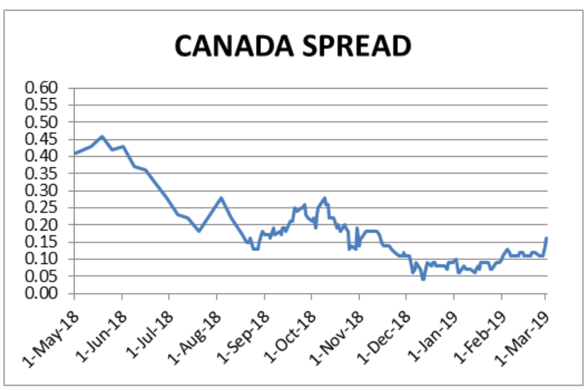
May 1, 2018 – March 1, 2019 **January 2, 2019 – March 1, 2019**

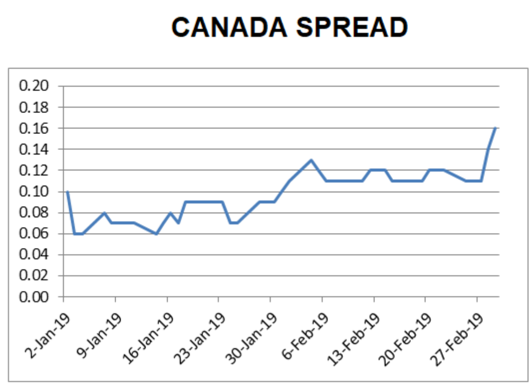




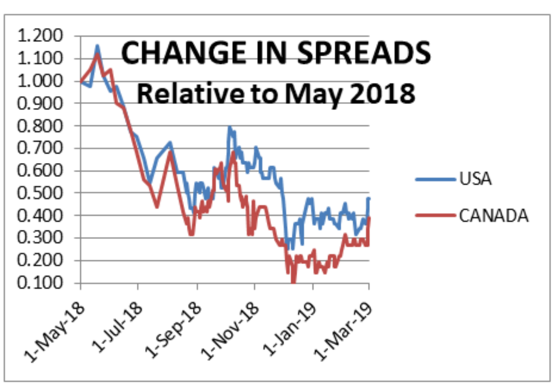
- As shown on the second set of charts the “spread” on Canadas is less than for Treasuries. The Canadas’ spread has been very stable since year-end,. It rose a little at the end of January and become stable at a higher level, until this past week’s increase. It is now at 0.16x, and well above recession levels of 0.00x.

May 1, 2018 – March 1, 2019 **January 2, 2019 – March 1, 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 March 1, 1999 (20 Years)

Here is a look at the 10-2 yield curve going back 20 years to March 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 0.21x, up from 0.17e week ago, andut comfortably above the 0.00x inversion level.

CONCLUSION

- The lower trending spread curved up last week. 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 at inversion yet, and the trend has moved against inversion in the last few weeks.

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