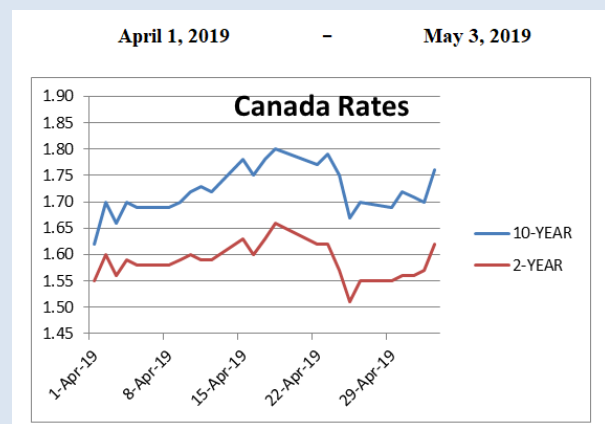
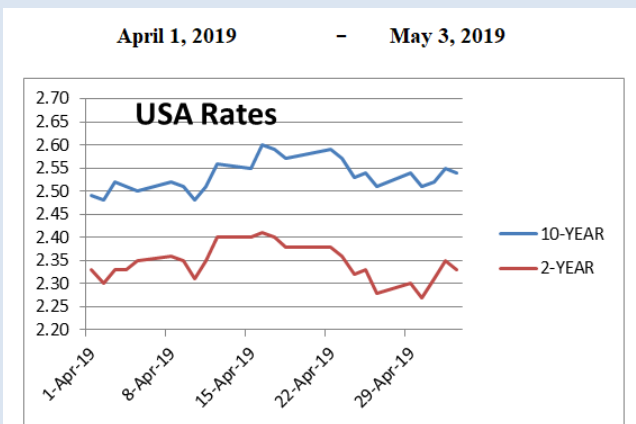


RECESSION BAROMETER

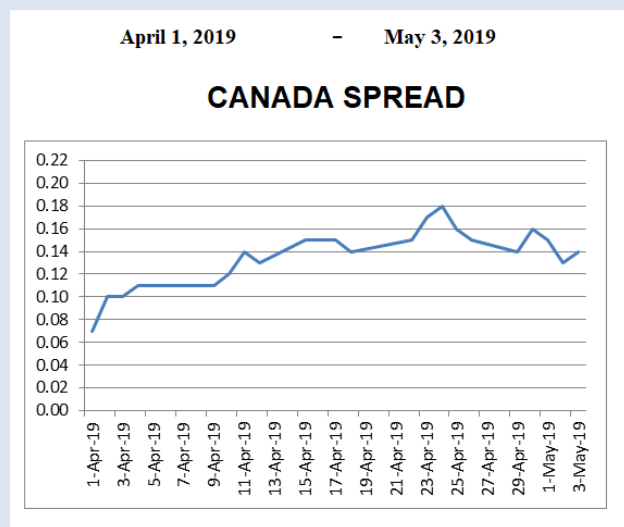
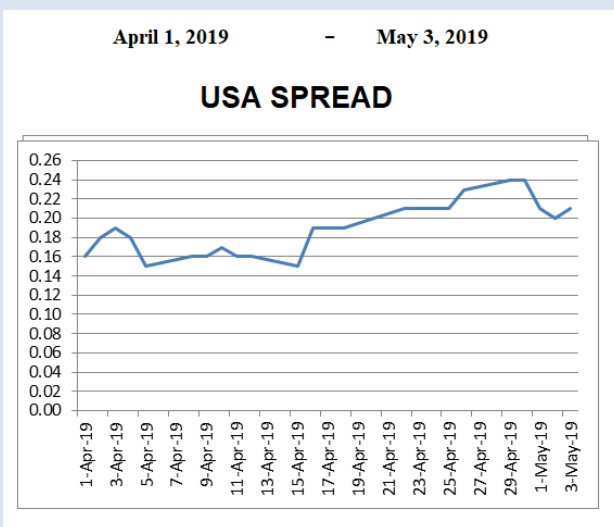
May 3, 2019

Spotlight on : 10-2 Yield Curve

COMMENT: Rates moved up again this past week, more so in Canada than in the USA, as shown in the first two charts below.



The “spread” fell slightly in both countries, but a bit more in the USA (now 0.21x) than in Canada (now 0.14x). Both of these metrics are well above recessionary fears at 0.00x.



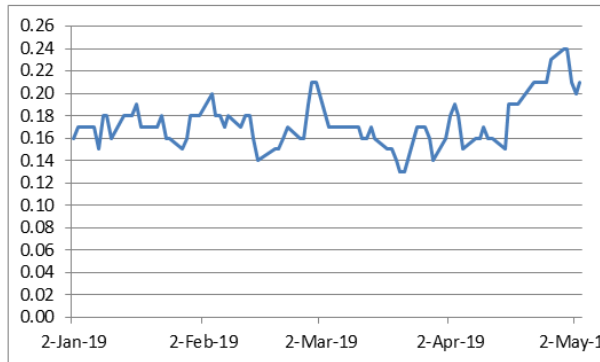
See our new Recession Barometer Reading scale on Page 7.

THE SPREAD

The charts provided below show the “spread” between the yields on 10-year versus 2-year Treasuries/Canadas. Since the beginning of 2019, the U.S. Spread has ranged between 0.24x (happened this past week) and 0.13x. The range for the Canadian Spread is 0.18x (also recently) and 0.06x. The respective Spreads right now are 0.21x and 0.14x. In both instances, there is no discernible move towards 0.00x, an inversion, and a possible subsequent recession.

January 2, 2019 - May 3, 2019

USA SPREAD



January 2, 2019 - May 3, 2019

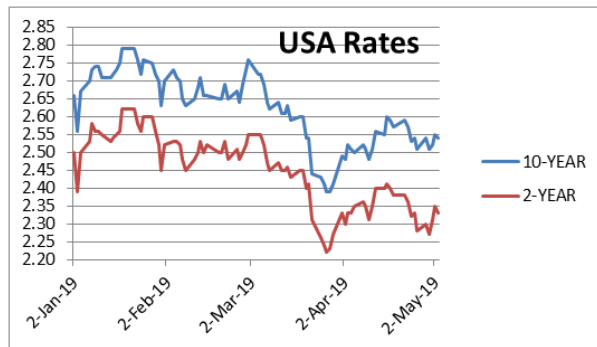
CANADA SPREAD



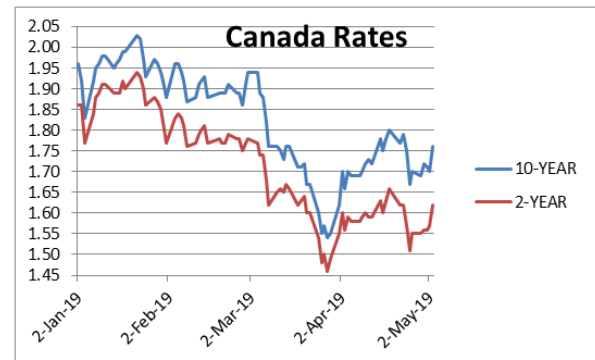
YIELD RATES

The next two charts show the actual rates for 10-year and 2-year Treasuries/Canadas since the beginning of the year. Rates bottomed in the last week of March and then rebounded, taking pressure off of recession fears. In line with the “no change” announcement this week from the Fed, 2-year rates moved upwards more so than 10-year rates, in both countries, but especially in Canada. With its significantly stronger overall economy, U.S. rates are well above corresponding Canadian rates. This should continue.

January 2, 2019 - May 3, 2019



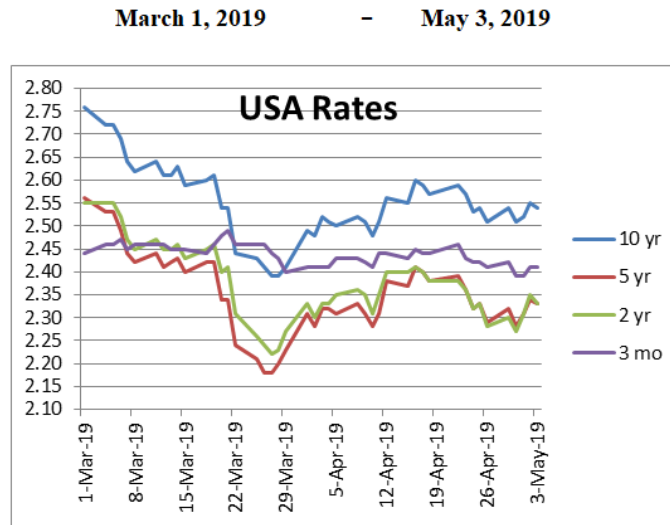
January 2, 2019 - May 3, 2019



<continued>

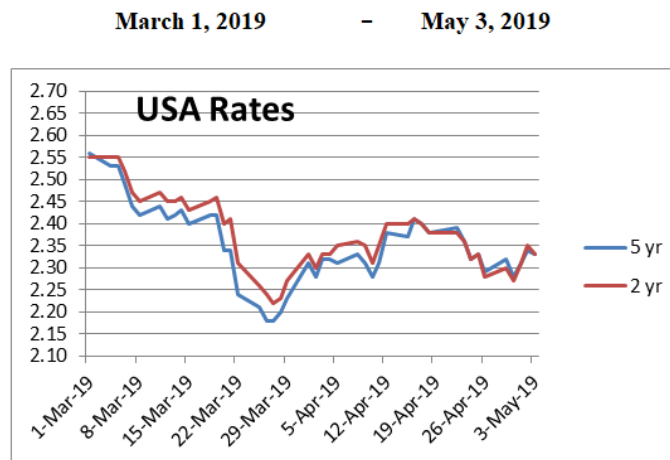
VARIOUS YIELD RATES

The next chart shows the trend in rates since the beginning of 2019 for 10-year, 5-year, 2-year, and 3-month Treasuries. In addition, for a brief period in the last week of March, the 10-year was yielding less than the 3-month. This has since reverted to the “norm”.



Since the beginning of March, the 5-year (**red**) was yielding less than the 2-year (**green**), a distinct inversion.

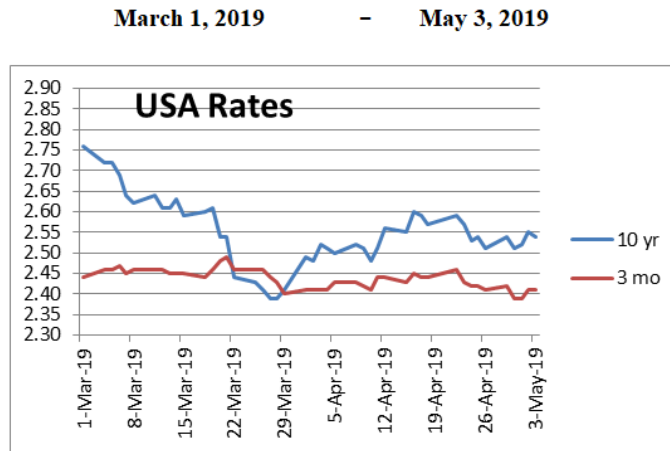
However, since April 16, the two yields have been exactly the same, or just one basis point apart, for both durations. In the following chart, the 5-year is shown in **blue** and the 2-year in **red**.



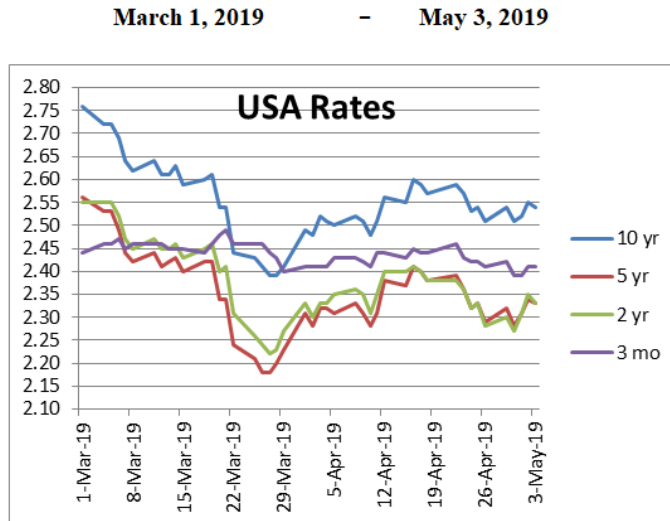
<continued>

In the last week of March, you will remember ... “the sky was falling”. ... “Inversion! Inversion! We are heading for a recession!” Well, the Inversion was short-lived.

Briefly, the yield on 10-year Treasuries fell below the yield on 3-month Treasuries. This was a pure and simple aberration. The yield inversion ended quickly, although it is fair to say that the difference between the two rates should certainly be more than what it is. See the chart below.



Normally, the 3-month yield would be below the 5-year and 2-year, but that is not the case. Here, again, to reinforce our point, is the 4-duration yield chart presented on the previous page. Anomaly!



<continued>

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

Here is a look at the 10-2 yield curve going back 20 years to May 1999. It shows the negative occurrences (below 0.0x) and the corresponding recessions (shaded areas) that soon followed. There was a false occurrence in 2006, but which became a distinct reality in 2007.

Currently, despite the falling trend-line that began at the beginning of 2014, there is still further to go to reach the inversion level and the possibility of a resulting recession. In fact, the current ratio is 0.21x, and is at the high end of its recent range.



In the above chart, the yield spread looks to have bottomed, at least temporarily, and could continue moving up to attempt a test of the downward trend-line. The next chart shows this more clearly.

U.S. Treasuries 10-2 Yield Ratio Since May 1, 2013 (6 Years)

The following chart provides a clearer assessment of just how close the 10-2 spread is to testing the down-trend line. As shown by the arrow, after a period of almost flat-lining, there is a discernible up-tick in the spread. However, there is still quite a ways to go before it breaks through the down-trend line.



How about a shorter-term chart? What does it say?

U.S. Treasuries 10-2 Yield Ratio Since May 1, 2016 (3 Years)



The same down-trend line is drawn. Clearly, yields have to move up quite a bit to breach the line.

Recession Forecast

The following chart shows when a recession could occur for various post-inversion dates. For inversion, we are using the 10-year/2-year metric. Our current “guess” is 15 months post-inversion (shown in Red). This is a “moving target” and will change with each ensuing month. It will also change with changes in global economic conditions.

Right now, the global economy is showing some signs of slowing while the U.S. economy keeps “chuggin’ along”. But how much better can the U.S. figures get? Longer term, this is not sustainable.

Forecasting the Commencement of a Recession

If an inversion occurs during the current month ... then a recession will begin at stated date projections.

Current Month	Inversion +12 Months	Inversion +15 Months	Inversion +18 Months	Inversion +24 Months	Inversion +30 Months	Inversion +36 Months
May/2019	May/2020	August/2020	Nov/2020	May/2021	Nov/2021	April/2022

Source: eResearch

See the Recession Barometer Reading on the following page.

RECESSION BAROMETER READING

We have devised a barometer to depict the status of where we believe the economy is in forecasting an economic recession. The barometer runs from 0 to 10, with 0 being the least worrisome level for recession expectations, and 10 reflecting that an inversion has occurred. Each barometer numeric is associated with a range of yield spreads.

Currently, for 10-year/2-year Treasuries/Canadas, the Canadian barometer reads “7”, while the U.S. barometer reads “6”. This better U.S. reading reflects the stronger economy currently in place in the USA than in Canada.

We extended the concept to the 10-year/3-month and the 5-year/2-year yield spreads, for which we have only U.S. readings. The current 10-year/3-month reading is “7”, and the 5-year/2-year reading is “9”. We then weighted the three yield spreads, being 80% for the 10Y/2Y, 10% for the 10Y/3M, and 10% for the 5Y/2Y. The weighted barometer reading was “6.4”.

RECESSION BAROMETER

Interest Rate Yield Spread	Barometer Reading	
>1.00x	0	
0.85x - 1.00x	1	
0.70x - 0.84x	2	
0.55x - 0.69x	3	
0.40x - 0.54x	4	
0.30x - 0.39x	5	
0.20x - 0.29x	6	
0.10x - 0.19x	7	
0.05x - 0.09x	8	
0.00x - 0.04x	9	
<0.00x	10	Inversion!

Source: eResearch

Weighted U.S. Reading (0.8/0.1/0.1)
6.4

10-Year/2-Year

CURRENT READING

USA = 0.21 x 6

Canada = 0.14 x 7

10-Year/3-Month

CURRENT READING

USA = 0.13 x 7

5-Year/2-Year

CURRENT READING

USA = 0.00 x 9

Bob Weir, CFA: Contributing Analyst

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