U.S. Recession Scorecard

March 2024

Defying the odds, for now

With some data still to come, there have been no sufficient changes recently necessitating adjustments to the positioning of our seven U.S. recession indicators on the Scorecard.

"The most anticipated recession ever" has been an overused phrase for more than a year now. The implication has been that because a recession is expected by "everybody" it won't arrive, or at the very least it is wildly overdue. Neither view holds much water, in our opinion.

There is no evidence that a "rate of anticipation," if one could be measured, would tell you anything about the likelihood of a recession starting. And we see little to no evidence that one is overdue. The most straightforward recession-start-time clock is the elapsed interval since the first Federal Reserve rate hike. On average, recessions have arrived 25 months following that first increase—which would target this April. Nor would April be a "drop-dead" line in the sand. In half the instances measured, the wait time was longer than 25 months.

Our two most reliable leading indicators of U.S. recession are in the outright negative column. While the "average" experience of both pointed to last summer as a recession kick-off date, both have histories with instances of much longer signal-to-recession intervals. Note that the official start date of any recession may not be announced until many

U.S. Recession Scorecard

Indicator	Status		
	Expansionary	Neutral	Recessionary
Yield curve (10-year to 1-year Treasuries)			✓
Unemployment claims		✓	
Unemployment rate	✓		
Conference Board Leading Economic Index			✓
Free cash flow of non-financial corporate business	✓		
ISM New Orders minus Inventories		✓	
Fed funds rate vs. nominal GDP growth		✓	

Source - RBC Wealth Management

For important and required non-U.S. analyst disclosures, see page 5.

All values in U.S. dollars and priced as of market close, Feb. 29, 2024 unless otherwise stated.
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months or quarters after the fact, so the soft vs. hard landing debate won't be settled for some considerable time yet.

Three indicators are in the "cautionary" yellow column, while the other two, still green, continue to suggest there is further to go in the economic expansion.

Yield curve (10-year to 1-year Treasuries)

The 1-year Treasury yield rose above the 10-year yield decisively in July 2022, with the negative gap growing further over most of the following year, reaching its widest point in June 2023. The average historical experience of this indicator after crossing into negative territory suggests the U.S. economy would have been in recession by late this past summer. However, while the average time interval between "inversion" of the yield curve and the onset of recession is 13 months, in four instances the gap was longer than average, with the longest being 23 months.

Yield curve inversion is an unequivocal indication that credit conditions are tightening, a fact underscored by the message delivered consistently for seven consecutive quarters by the Fed's Senior Loan Officer Survey (most recent issue released on Feb. 5). A majority of U.S. banks continue to raise lending standards on almost every category of business and consumer loan, including commercial and industrial loans for businesses of all sizes, credit card loans, consumer installment loans, mortgage loans, and commercial real estate loans.

The negative spread between the 1-year yield and the 10-year yield reached its widest point this cycle so far last June at 158 basis points (bps). It has since narrowed dramatically to just 75 bps, strongly suggesting the period of "de-inversion" is underway. The crossover from "inverted" to "normal" tends to occur just as the recession is starting or a few months before. There is also a reasonable correlation between how long the total period of inversion runs and how long the ensuing recession lasts. This latest inversion is at 20 months and counting.

ISM New Orders minus Inventories

The difference between the New Orders and Inventories sub-indexes of the ISM Purchasing Managers' Index has turned negative near the start of most U.S. recessions. But it has also registered occasional false positives—signaling a recession was imminent when none subsequently arrived. Moreover, this indicator only relates to activity in the manufacturing sector (some 15% of the U.S. economy) and is derived from a survey rather than hard data. For those reasons, we look at it as a corroborative indicator rather than a decisive one taken on its own.

After setting its most recent low in September 2022, this series has steadily moved higher and August 2023 data (we use a three-month moving average) moved back above zero, shifting the indicator back to yellow from red.

Conference Board Leading Economic Index

Historically, this series has given reliable early warnings of recession. When the index has fallen below where it was a year earlier, a recession has always followed—usually two to three quarters later.

This indicator turned decisively negative in Q3 2022, shifting it to the red column on our Scorecard. As of the February report, the index had fallen for 22 consecutive months moving deeply into negative territory, although the rate of year-over-year decline has slowed over the past six months. The indicator has never fallen this deeply without a recession arriving.

U.S. RECESSION SCORECARD

Unemployment claims

The monthly low for this cycle occurred in September 2022. The cycle low for claims has typically been registered about 12 months before the start of the next recession. So far, no lower reading has been posted in the ensuing months, so the history of this indicator would suggest a recession could get underway as early as this fall.

The fact that temporary employment, job openings, average hours worked, and overtime hours worked have all been falling on a year-over-year basis adds to the likelihood the tide may be turning for unemployment claims. While we wait for that shift to be confirmed or for claims to subside once again, we think this ambiguity warrants leaving the indicator's status at yellow.

Unemployment rate

The unemployment rate jumped to 3.8% in August 2023, its highest posting since January 2022. It stayed there for three months before easing to 3.7% through to January. Any move above 4.0% in the next few months would turn the smoothed trend of this indicator higher and, in our view, signal a recession is on the way. Once that signal is given, on average, it has been eight to nine months from the lowest monthly posting (which was 3.4% in April last year) until a recession gets underway.

Free cash flow of non-financial businesses

This gives an indication of the ability of such businesses, in aggregate, to internally fund any capital spending they want or need to do. Historically, whenever it has posted a year-over-year negative reading, a decline in corporate capital spending has typically followed, either indicating a recession is coming or deepening one that is already underway. This number declined in both Q4 2022 and Q1 2023 before ticking fractionally higher in Q2, and moving up again in Q3. It remains well above a negative crossing point. There is a long lag time before this data is reported with the Q4 release not coming until March.

Fed funds rate vs. nominal GDP growth

The fed funds rate has risen above the six-month annualized run rate of nominal GDP either before or at the start of every recession in the past 70 years. (Nominal GDP is GDP not adjusted for inflation.) That GDP run rate has been declining since its pandemic reopening high of 23% recorded in Q4 2020. By the end of last year, it had slowed to 7.2% but was still well above the fed funds rate, which at the time had risen to 4.50%. Now the fed funds rate is up to 5.50%, and Q4 GDP data shows the six-month run rate of nominal GDP growth remained marginally above that at 6.1%. We expect nominal GDP growth to slow to something below the 5.5% fed funds rate in Q1, meeting a necessary precondition of a recession. But for now, that line in the sand has not been decisively crossed.

Clock still ticking

Weighing up the current positioning of all seven indicators and projecting their likely paths points to a growing probability the U.S. will enter a recession this spring, in our view.

Research resources

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