US Macroeconomics

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Joseph Lavorgna, Chief US Economist | 212.610.1741 | joseph.lavorgna@smbcnikko-si.com

Echoes of 2008

The current environment is reminiscent of the one leading up to the 2008-09 downturn. It, too, was heavily advertised, as economists debated the extent to which the subprime meltdown would spill over into the broader economy. The soft landing versus recession narrative was commonplace. The Index of Leading Economic Indicators (LEI) was declining like today, yet real GDP and employment kept growing (also like today). In the current cycle, the LEI peaked in December 2021.

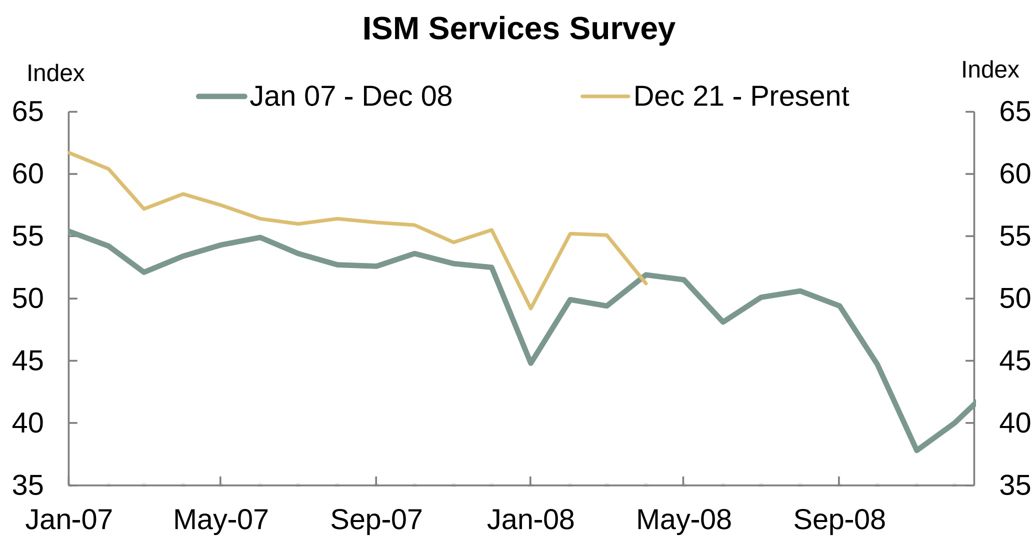
The LEI peaked in March 2006, but the economy did not peak until a long 21 months later in December 2007. But when the economy entered recession, market participants were still debating whether one had been avoided. The economy grew in the first half of 2008, with Q1 and Q2 real GDP growth initially reported at 0.6% and 1.9%, respectively.

While Q1 2008 real GDP has since been revised down to -1.6%, Q2 2008 real GDP growth has been revised up to a solid 2.3%. No wonder it is so hard to know when the economy is contracting. The economic data get substantially revised, and even during a downturn, the statistics can move in confounding ways with inexplicable improvements relative to the underlying fundamentals.

One way investors can get around revisions is to look at data that does not get revised such as financial market prices like the yield curve or credit spreads. Investors can also look at purchasing managers surveys which tend to show minimal revision.

Once again, take the 2008-09 analog. **In the chart below, we show the ISM services survey. Look how similar the trends were heading into 2008 compared to today. Services activity was still expanding albeit at a slower pace**. But in February 2008, the services sector showed a substantial jump. The ISM services survey was back above 50 again and expanding during recession. It was not until the Lehman Bankruptcy that this series and other broader measures of activity turned noticeably downward, ending the soft landing versus recession debate.

While history may not repeat, the cadence of 2023 bears similarity to 2008. Put another way, the trajectory of today is similar to back then. Investors beware. The dispute is not yet settled.



Sources: Institute of Supply Management, Haver, SMBC Nikko

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