Manulife Investment Management

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Recession risk in 2020

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One of the common questions I've been receiving over the last couple of months is are we headed towards a recession? Now, this is a general question with respect to the Canadian economy, but more specifically to the U.S. economy. And we would suggest that we are not.

We don't believe that there is enough evidence to suggest that we're headed towards a recession. Now, certainly the trade tensions between the United States and China have increased risks from a geopolitical perspective, but the typical signs of recession do not appear to be present. In particular, we never saw the yield curve invert as it has in the past. When we look at the U.S. 10-year Treasury yield relative to the U.S. two-year Treasury yield. That difference didn't invert for more than really just a couple of days, in late August. Historically, in advance of a recession, you see the “10-2 spread” invert for about three months before it is a confirmation that a recession is forthcoming.

Some of the other indicators that we pay attention to always dip negative in advance of a recession. While they have been lower than what we've seen at any other time during this cycle, they are not yet negative. Now, at the same time, we could argue that we are seeing the start of perhaps a manufacturing recession, that the trade tensions between the United States and China have weighed on manufacturers. And we've seen a contraction in manufacturing, not only in the U.S. over the last couple of months, but in other areas around the world. Now, this doesn't always lead to a broad-based economic recession. And in the case of the United States, we would suggest that credit conditions remain very favorable and the consumer remains very healthy. Jobs are plentiful with the unemployment rate hovering around three and a half percent. The household income as a percentage of household debt continues to decline in the United States.

And therefore, we would say those two ingredients that lead to weakness in 2008. Tighter financial conditions and a weaker consumer are not present today. Those, in fact, could be the backbone to the U.S. economy that could provide the U.S. economy with stability while the U.S. economy works through these trade tensions with China. While it's been the number one question on the minds of advisors, are we headed towards a recession? We will put a low probability to that event as we don't have enough evidence to suggest that we are headed in that direction.

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