PMIs—Time to Get Concerned?

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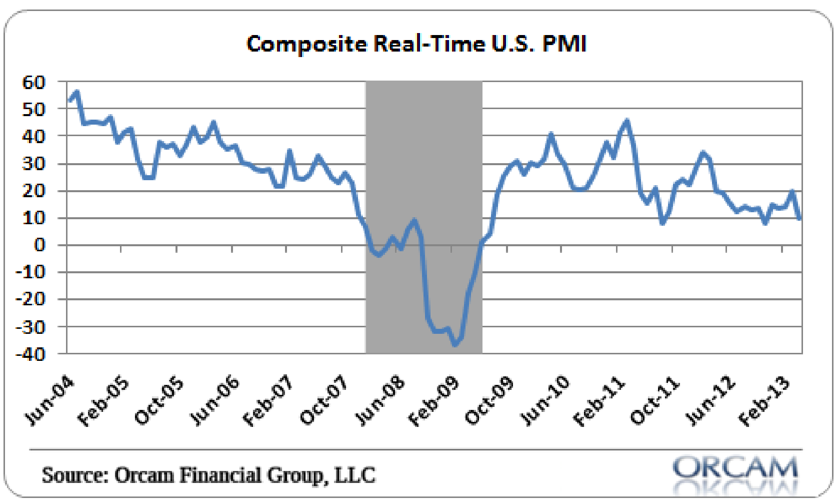
Long story short—
Still no need to panic over US recession.

Regional PMI readings have been universally on the weak side in the USA. Is it time to start fearing a US recession?

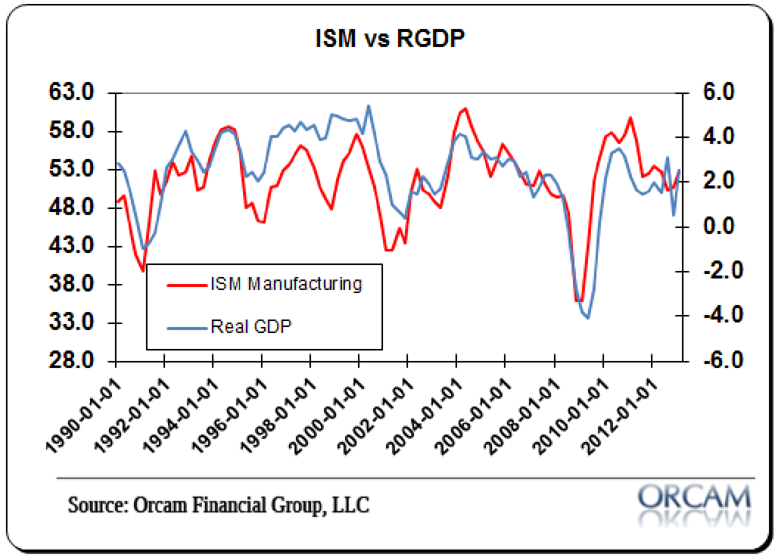
A Granular Look

If we get a bit more granular with some of the recent regional Fed surveys we can see just how weak they've been. The Composite Real-Time U.S. PMI shows a reading of 9.8 which is the third lowest reading since 2009. Clearly, the trend appears to be on a downward slope since 2010. But we shouldn't begin to seriously

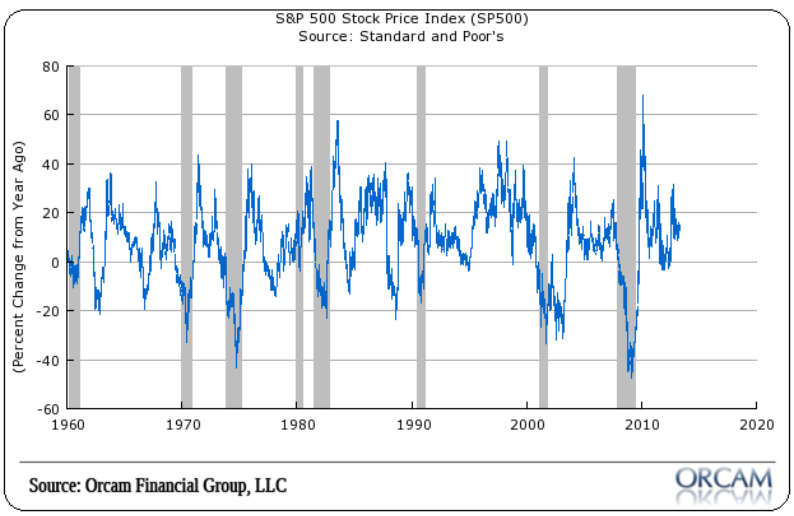


worry about recession until we see consistent negative readings in this data. If we take a bit of a longer view here the 3 month moving average is 14.5 which places us well above a zero reading.

This is also consistent with meager US economic growth. Recent readings in the ISM data are historically consistent with low single digit GDP readings. Clearly, we'll be keeping a close eye on the composite index as it gives us a better idea of the real-time performance of the US economy. Recent data is not alarming, but does begin to make me wonder if the economy isn't much weaker than most presume.



I stress the recession forecasting because we must always remember that the worst periods of capital destruction occur within recessionary periods. As you can see in the chart to the left, every single 30% plus DECLINE in the S&P 500 has occurred within a recession. The only two 40% declines occurred within a recession. Why do I focus on such extremes? Because these periods are where the investment math becomes most extreme. A 20% decline is not intolerable as it requires just a 25% price increase to break-even. A 30% decline, on the other hand, requires a 43% price increase to break-even. And a 40% price decline requires a staggering 68% price increase to break-even. As you can see, the numbers become increasingly cruel as the declines mount.



But the good news is that we can remain at least moderately confident that the current environment is NOT consistent with a recessionary environment and the type of substantial capital destruction that often occurs inside of recessions.

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