EQUIFAX

SOME FACTS ABOUT **RECESSION RISK**

Information from “Gauging U.S. Recession Risk” by Equifax Chief Economist Amy Crews Cutts and Deputy Chief Economist Gunnar Blix

Opinions on recession risk are all over the map

"There's more than 60% chance of a global recession within the next 18 months, economist says."[2]

"Every time a President leaves the White House after two terms, there is a recession within the first year of the new administration. I believe this time will be no different."[3]

"The odds of another recession have fallen from 40% in July to 25%, according to estimates by Morgan Stanley."[1]

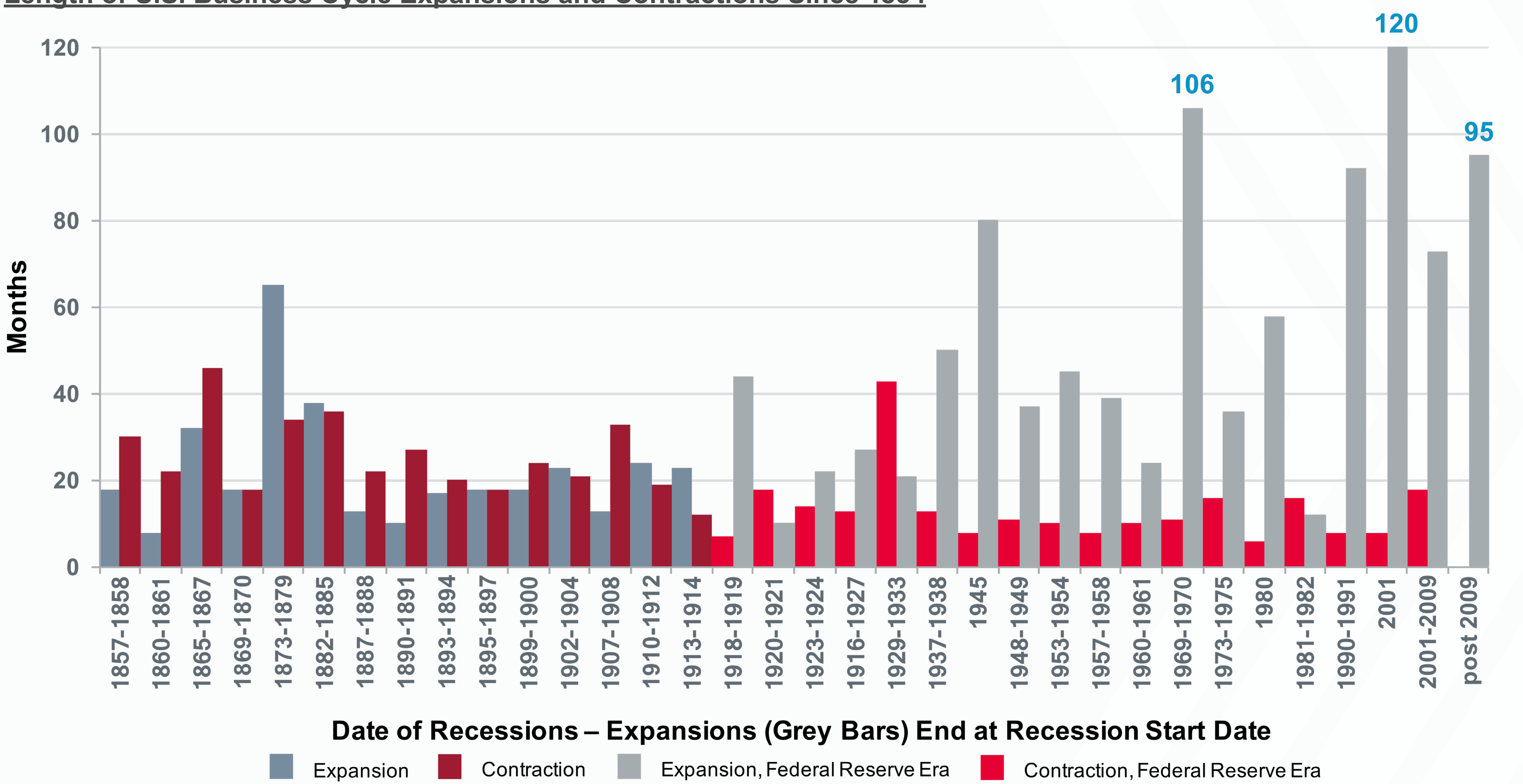
Here are some facts

1 Lucinda Shen, "Morgan Stanley Lowers Odds of Recession Happening This Year," Fortune, May 12, 2017
2 Silvia Amaro, "There's more than 60% chance of a global recession within the next 18 months, economist says," CNBC, April 10, 2017
3 Tyler Durden, "Mark Yusko: 'I'm Telling You Right Now, the U.S. is Going to Have a Massive Crash,' Zerohedge, May 26, 2017

Recessions are getting shorter; recoveries are getting longer

Since 1982, the three recessions have averaged 11.3 months, including the Great Recession, and the four expansions, inclusive of the current one, have averaged more than 95 months and counting.

Length of U.S. Business Cycle Expansions and Contractions Since 1854

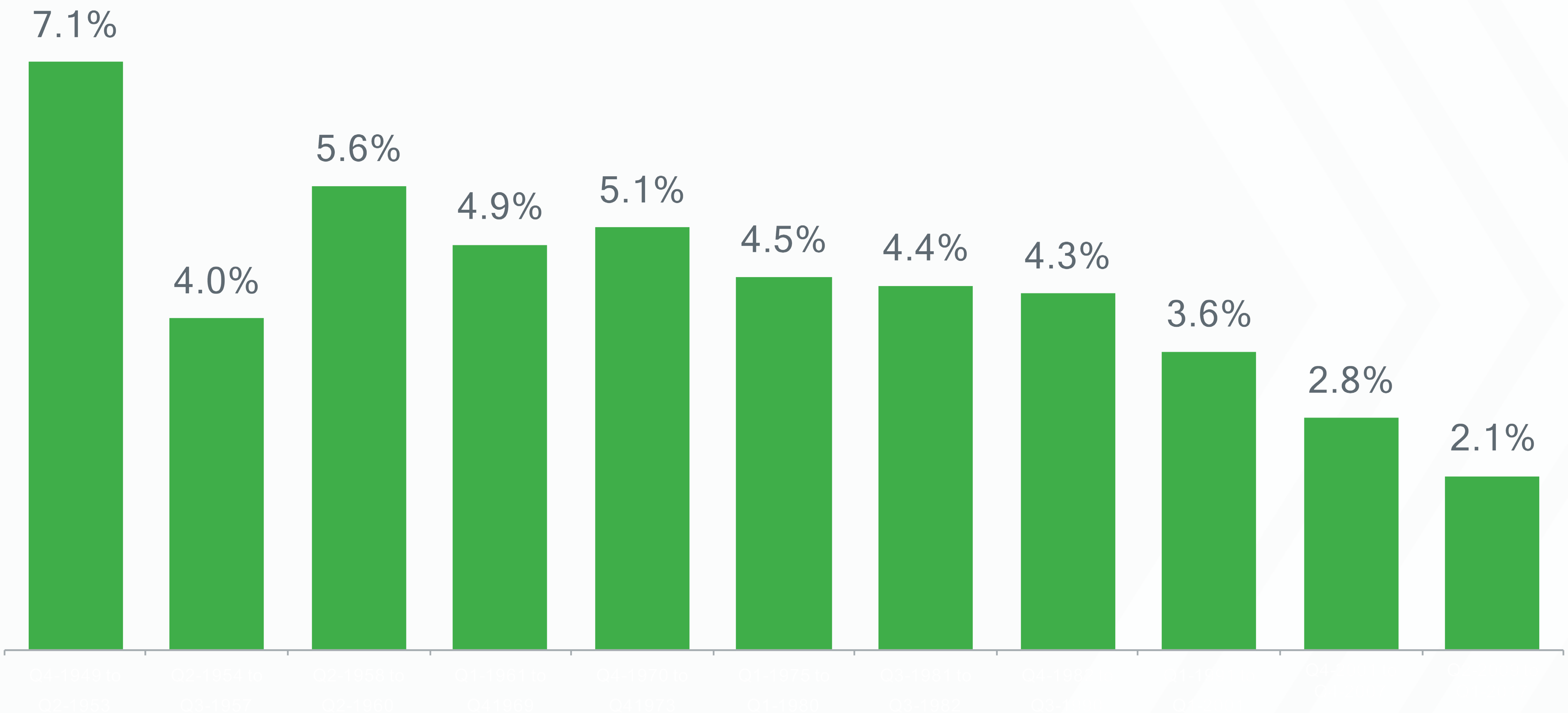


Source: Equifax, National Bureau of Economic Research, Federal Reserve Board of Governors. The Federal Reserve System was created in December 1913. Data reported through June 2017.

The economic growth rate during expansions is slowing

We may be in the seventh year of the expansion, but it hasn't felt like the economy is on firm footing.
2.1% growth is hardly worth getting excited about.

Real GDP Cumulative Annualized Growth Rate for Post-WWII U.S. Economic Expansions

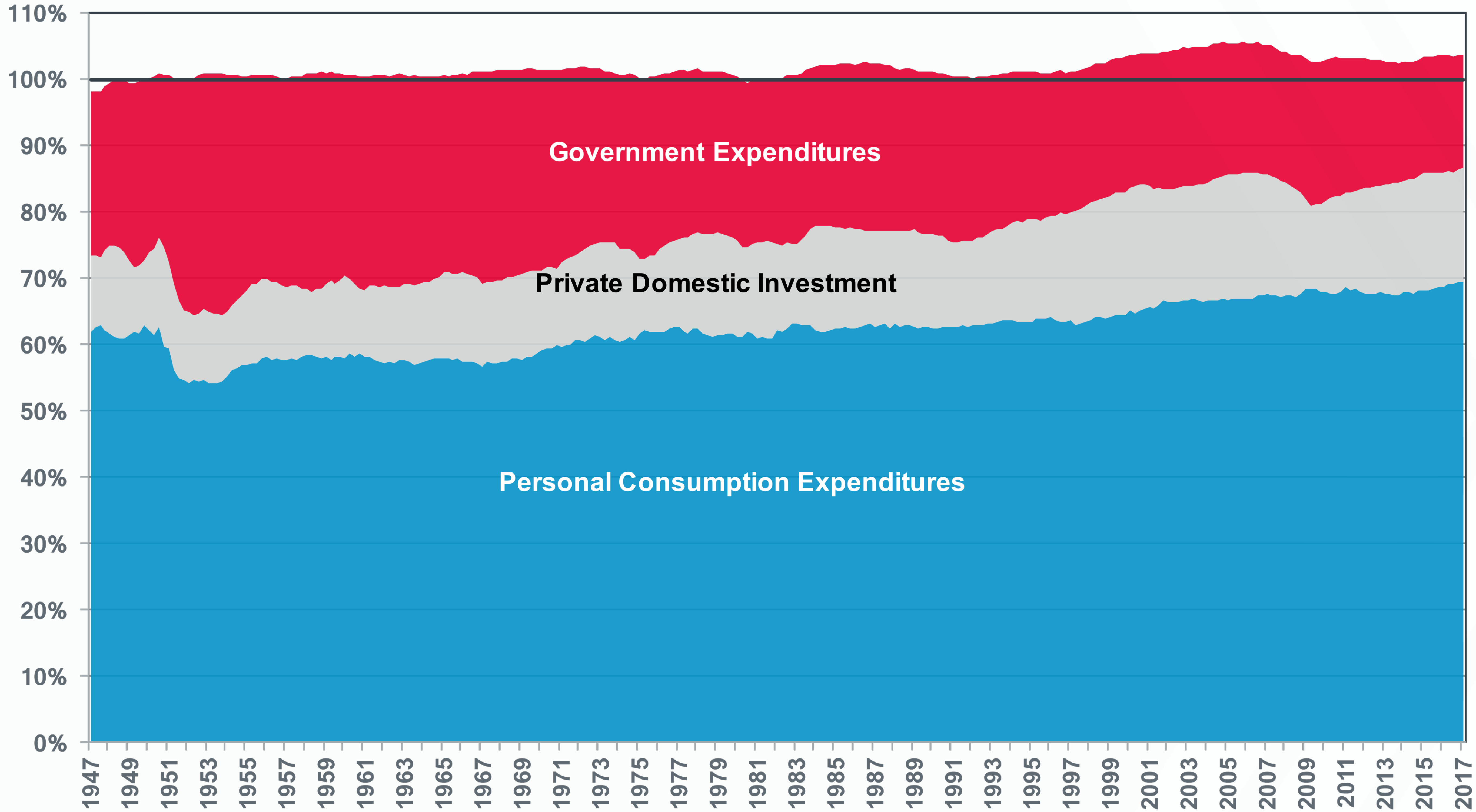


Source: Equifax, Bureau of Economic Analysis, National Bureau of Economic Research; Data as of June 2017.

Personal consumption still drives the economy

Consumption currently makes up **69%** of the real GDP. Government expenditures come in second at **17%**.

Major Segment Contributions to Real GDP



Source: Equifax, Bureau of Economic Analysis: Table 1.1.6. Real Gross Domestic Product, (2009) Chained Dollars (SAAR). Deviations around 100% represent the contributions of net exports. Data through Q1 2017 (June 2017).

How to spot **a recession**

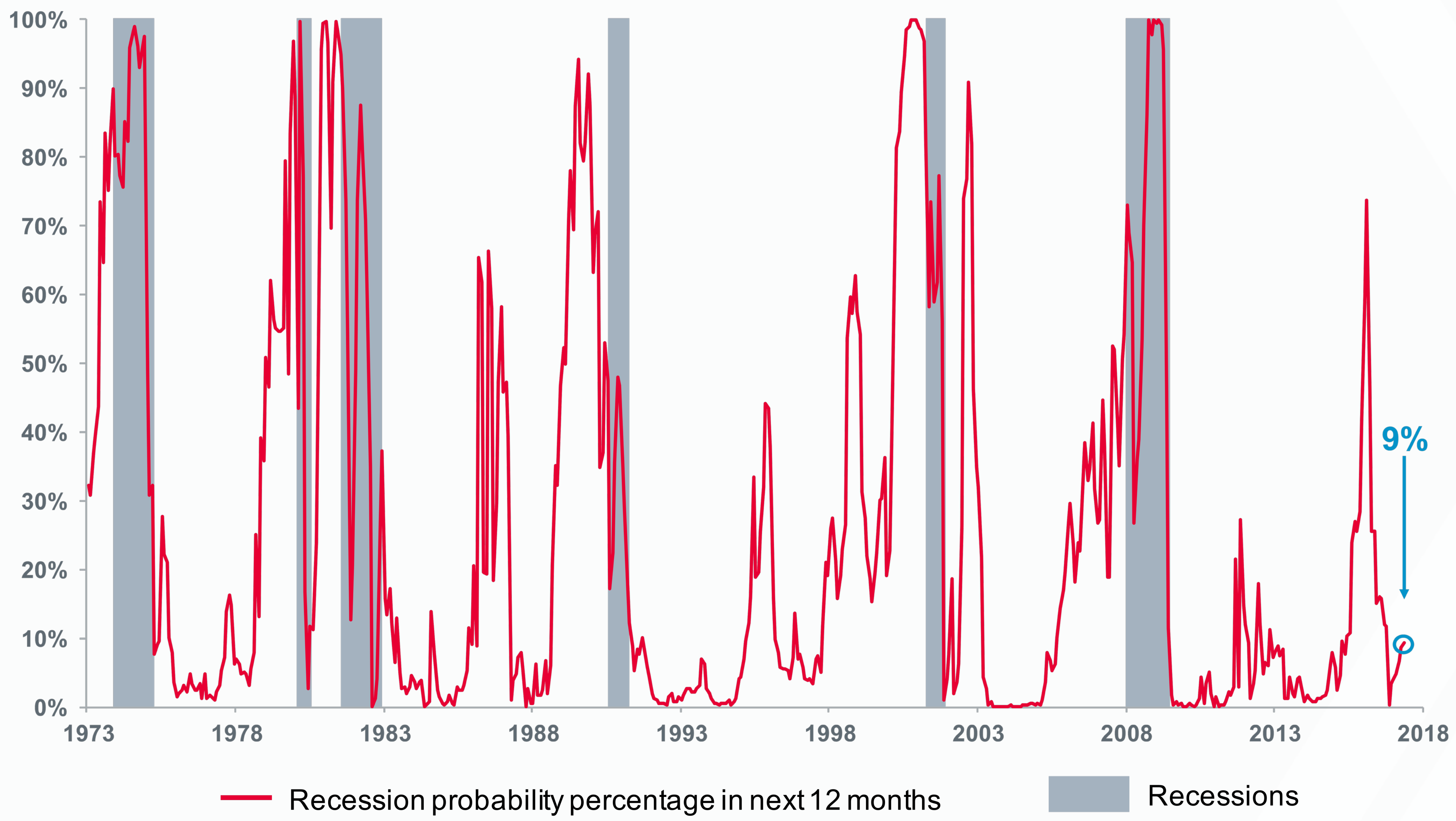
Recessions occur when the aggregate growth rate is negative for two or more consecutive quarters. For that to happen, consumers would have to cut back or government spending must markedly decline.

But consumers have not cut back, and the federal spending cuts have ceased, while local government spending is rising due to increasing property tax revenue.

Correlation is not causation – even in economics

Recessions do not die of "old age," nor do they correlate to any recurring event. Absent any particular event that might make a recession more imminent, the probability of a recession over the next 12 months was put at **23%** by Federal Reserve Bank of San Francisco (FRBSF) economists[4]. Deutsche Bank puts the risk at **9%**

Recession probability in the next 12 months: DB



Source: FRB, Haver Analytics, Deutsche Bank

4 Rudebusch, Glenn D. (2016) "Will the Economic Recovery Die of Old Age?" FRBSF Economic Letter (2016-03, February 4, 2016)
5 MarketWatch, "What market risk? Deutsche Bank sees only 9% change of a recession," June 14, 2017

Recession probability numbers without context **can easily mislead**

The same FRBSF report puts the chance of recession within the next **24 months at 41%**, and the chance within **48 months at 64%**[6].

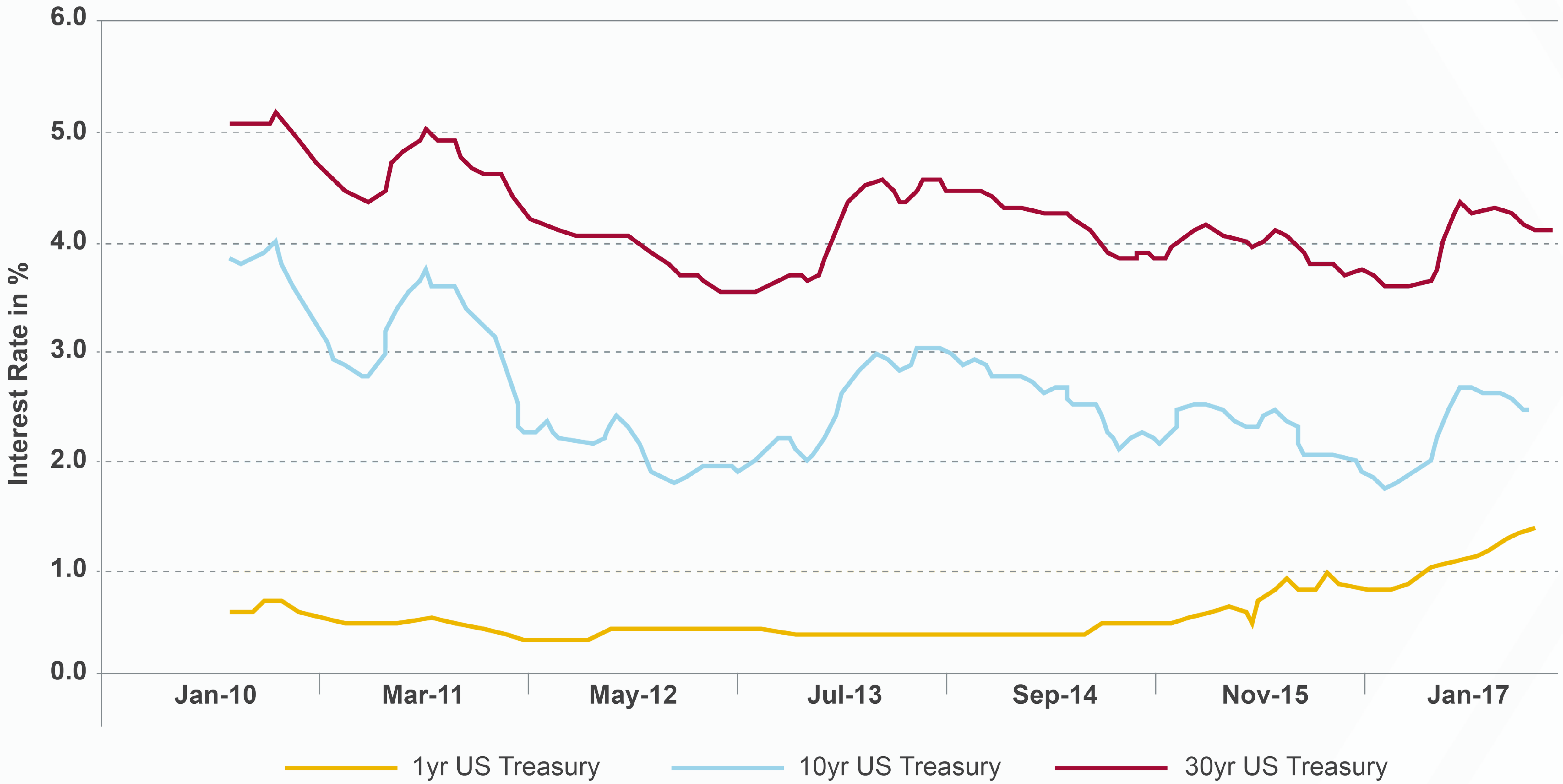
Thus, take care when you read predictive headlines like, "Goldman Sachs Model Shows **31% Chance of Recession in Next 9 Quarters**". Nine quarters is over two years. The 31% number looks alarming compared to other predictions, but within the expanded timeframe, this projection is actually more optimistic than the FRBSF report.

6 CNBC Market Insider, "Goldman says this may become the longest economic expansion in history," May 8, 2017

Bond spreads and treasury yields as indicators

Leading indicators can give a little warning that a turning point is coming. These are correlated measures with economic performance that react earlier than the overall economy to changing conditions. Corporate bond spreads and the slope of the Treasury yield curve (that is, the term spread) are two financial indicators that are especially informative about the likelihood of an economic downturn over a medium-term horizon.

U.S. Treasury Bond Rates - Yield Curve Flattening But Not Flat



> "The slope of the yield curve has been flattening in recent days, with short-term rates rising faster than longer-bond yields. This typically happens when monetary policy is tightened.[7]"
>
> \- Jennifer Alban, Reuters

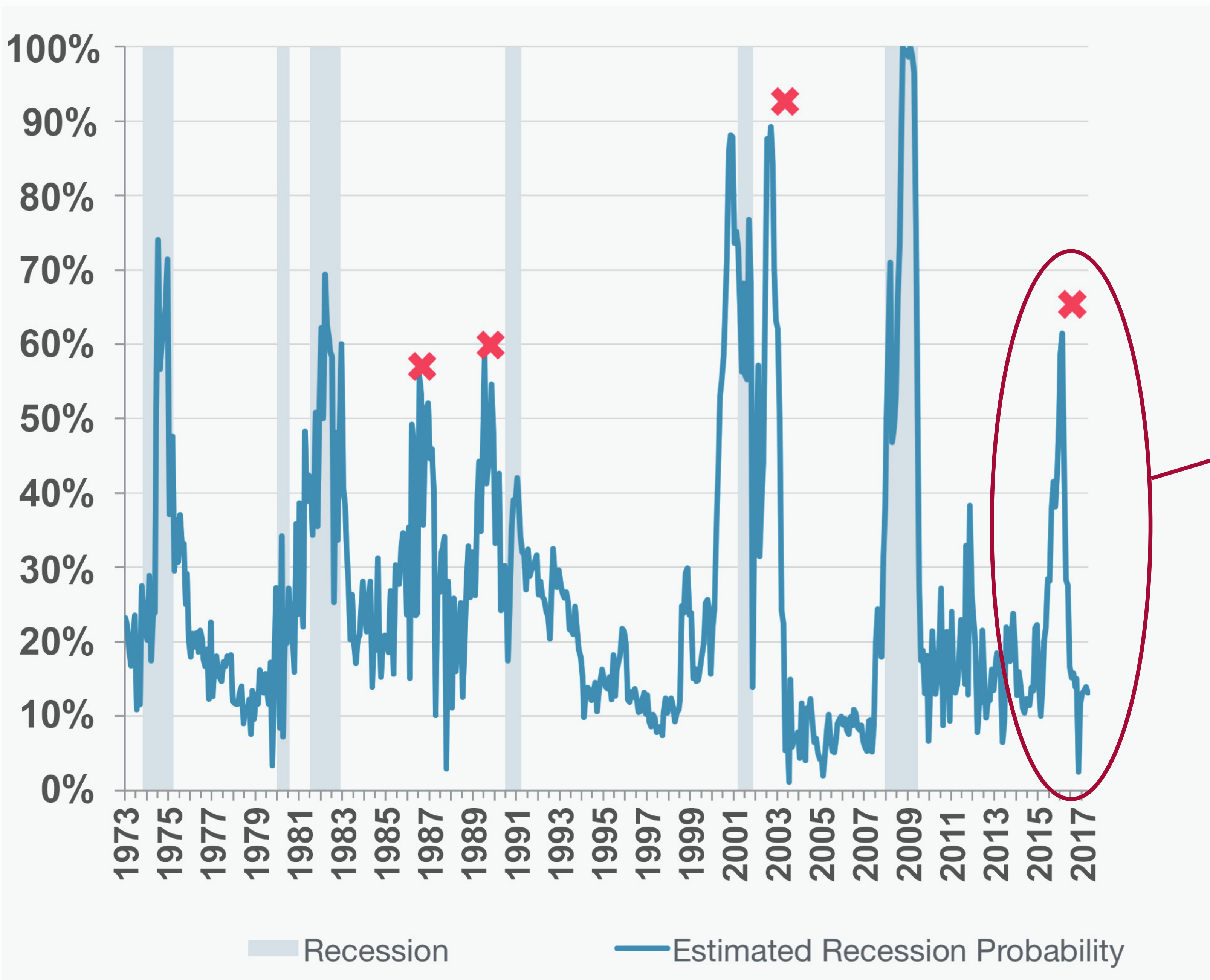
Source: Equifax, Inc., Federal Reserve Bank of St. Louis (FRED)

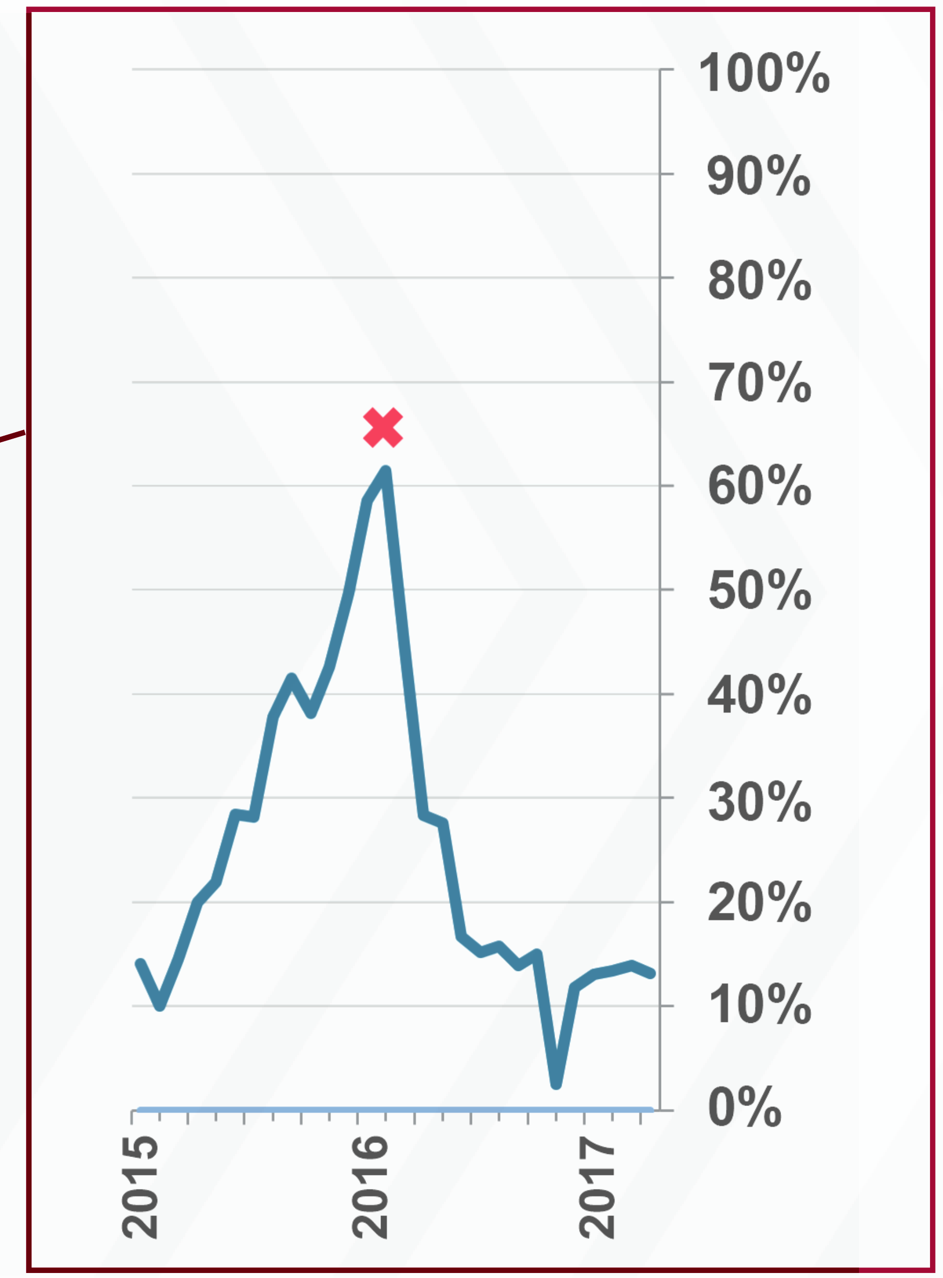
7 Jennifer Alban, "Gundlach says flatter Treasury yield curve could become a concern," June 21, 2017

Excess bond premium (EPB) as an indicator

EPB measures investor sentiment or risk appetite in the corporate bond market. The measure is complicated to estimate, but is well described in this Federal Reserve FEDS Note Link[8] and this FEDS Note Update[9]. This method has successfully predicted some recessions—and it has produced false positive indicators of recession on three occasions since 1973.

Excess bond premium method of estimated probability of recession





Source: Equifax, Inc., Board of Governors of the Federal Reserve System

8 Giovanni Favara, Simon Gilchrist, Kurt F. Lewis, and Egon Zakrajsek, "Recession Risk and the Excess Bond Premium," FEDS Notes, April 8, 2016

9 Giovanni Favara, Simon Gilchrist, Kurt F. Lewis, and Egon Zakrajsek, "Updating the Recession Risk and the Excess Bond Premium," FEDS Notes, October 6, 2016

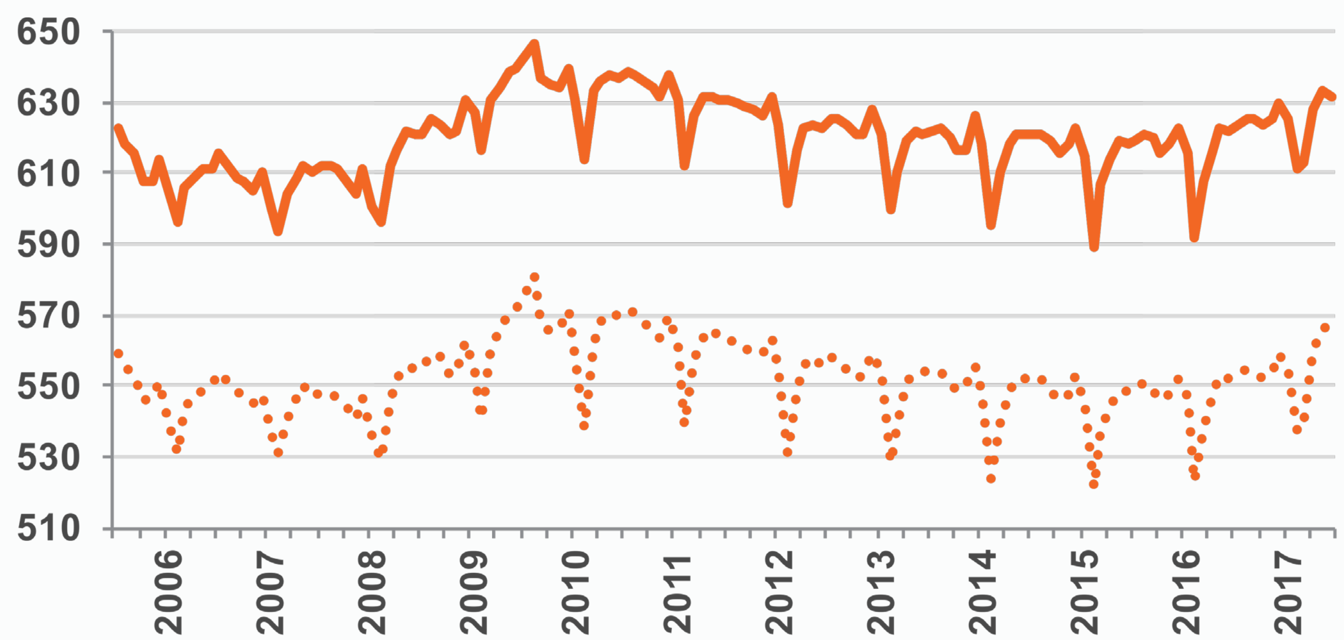
Credit scores show little indication of weakening credit standards

One indicator of possible weakness is lowering of credit standards, a race to the bottom in the hopes of capturing greater market share. Looking at credit score distributions, we see little indication of weakening credit standards with respect to credit scores.

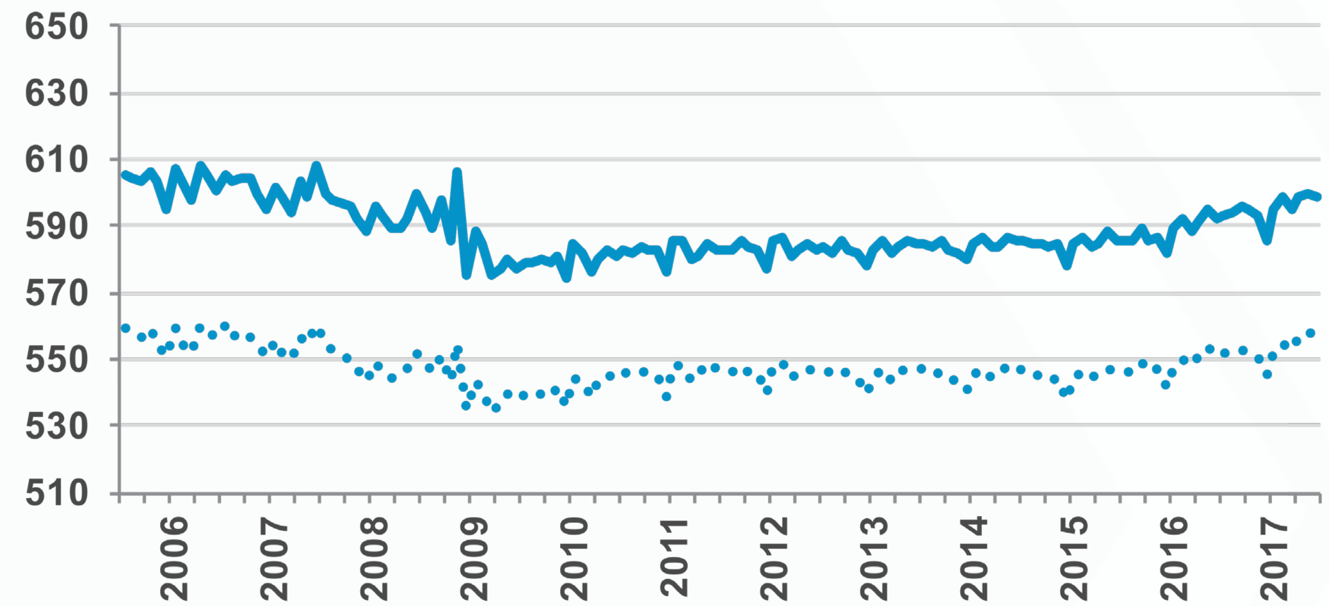
Currently there is no degradation of credit standards occurring

10th and 25th Percentiles for Origination VantageScore® 3.0 Credit Scores

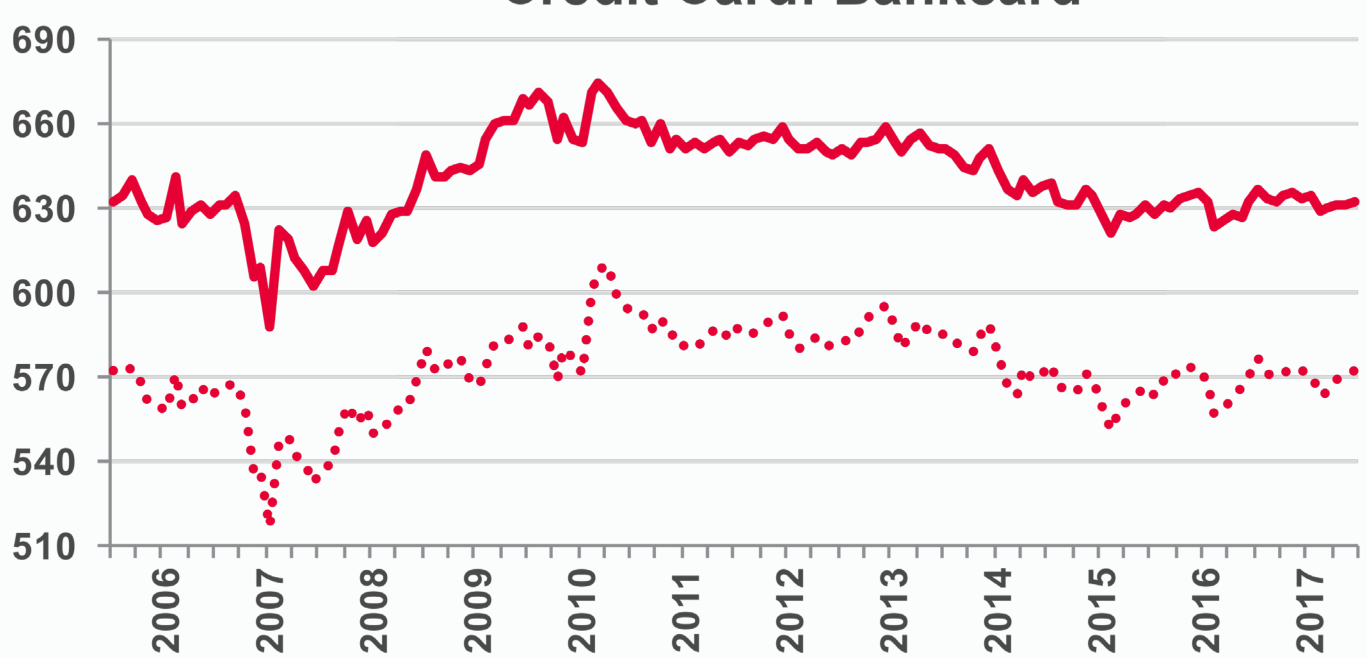
Auto Loans



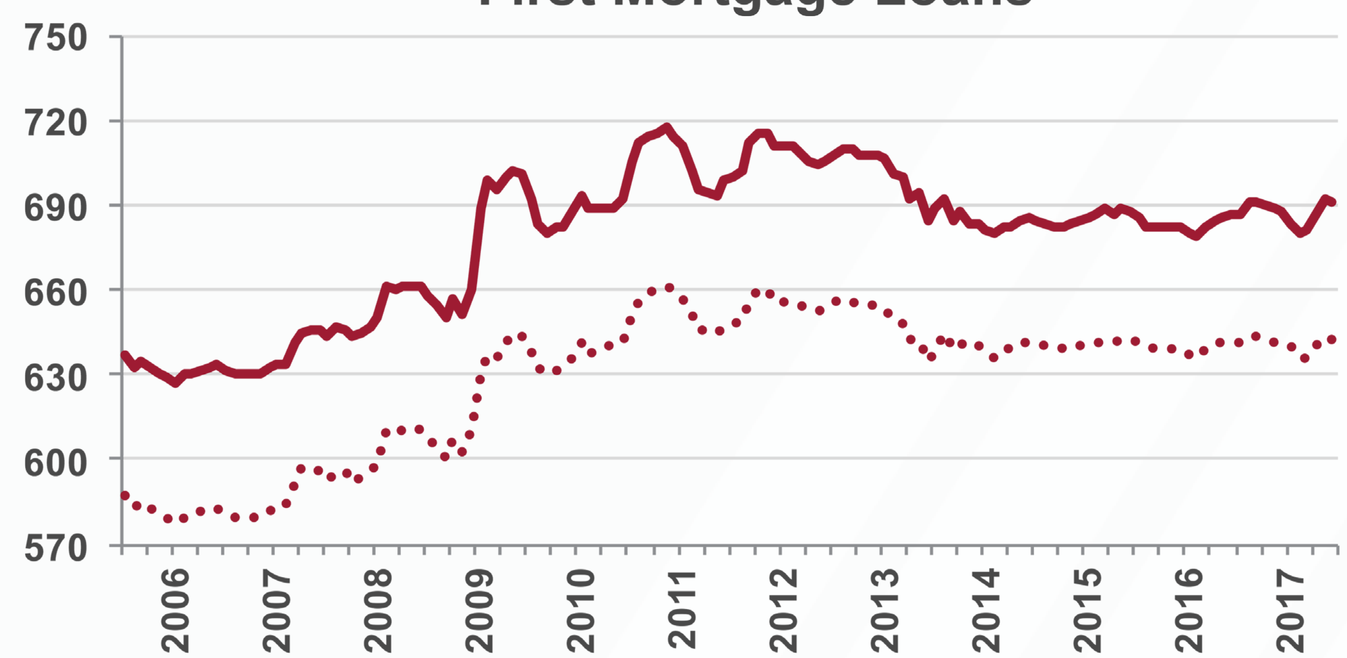
Consumer Finance



Credit Card: Bankcard



First Mortgage Loans



Visit the white paper for more tradeline comparisons, including home equity installment loans, lines of credit, and more.

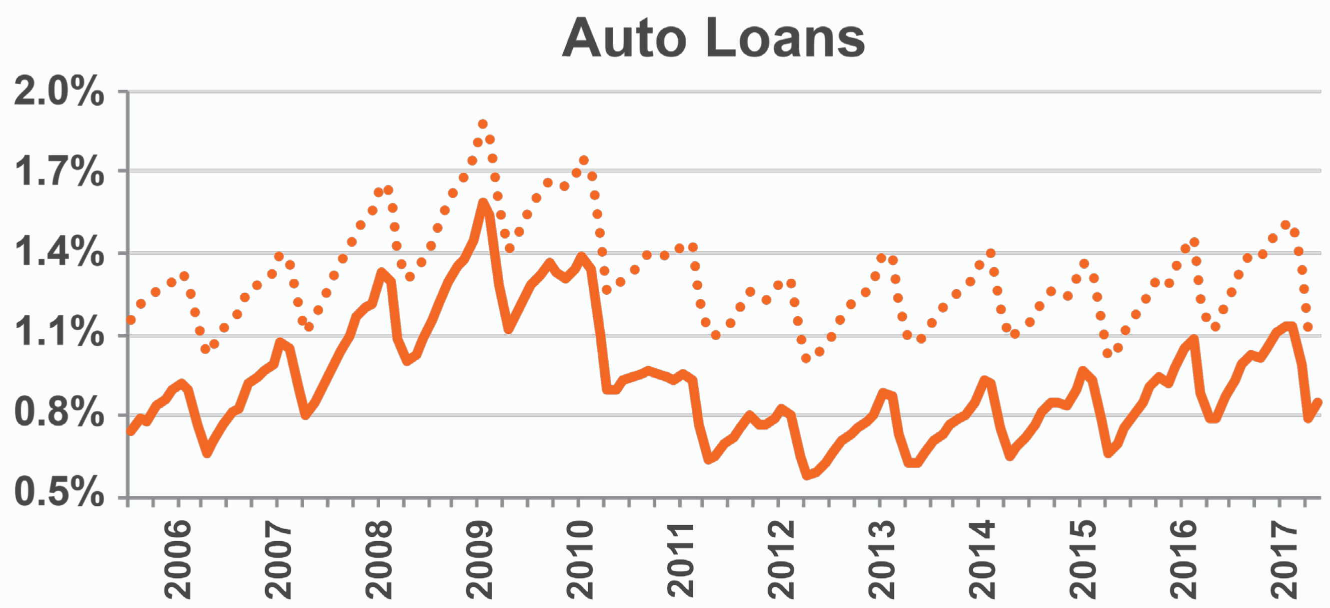
Source: Equifax, Inc.

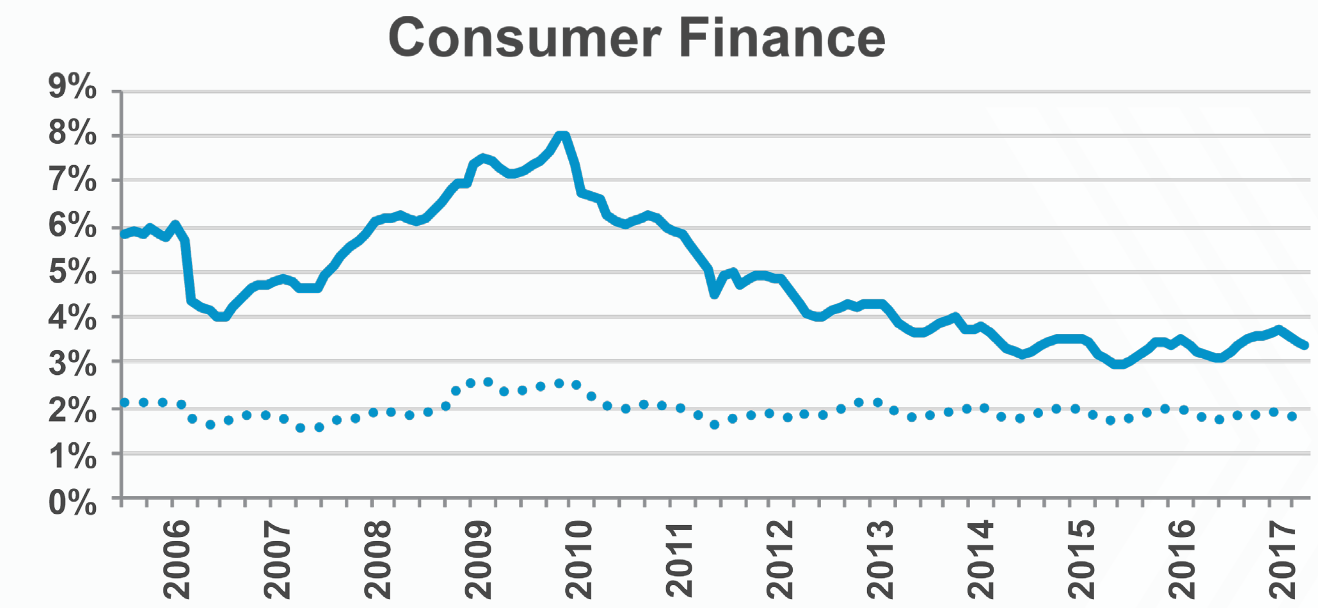
Delinquency rates are mixed, but raise no alarms

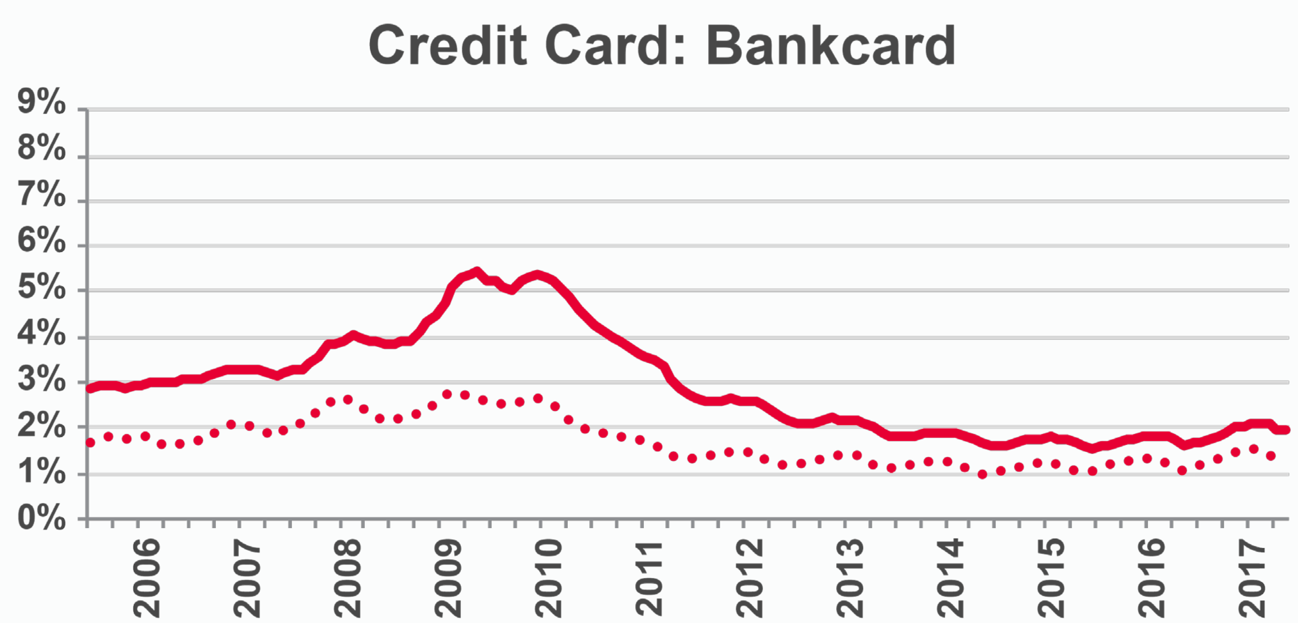
Looking at delinquency rates, performance on some tradelines is degrading while others are steadily improving.

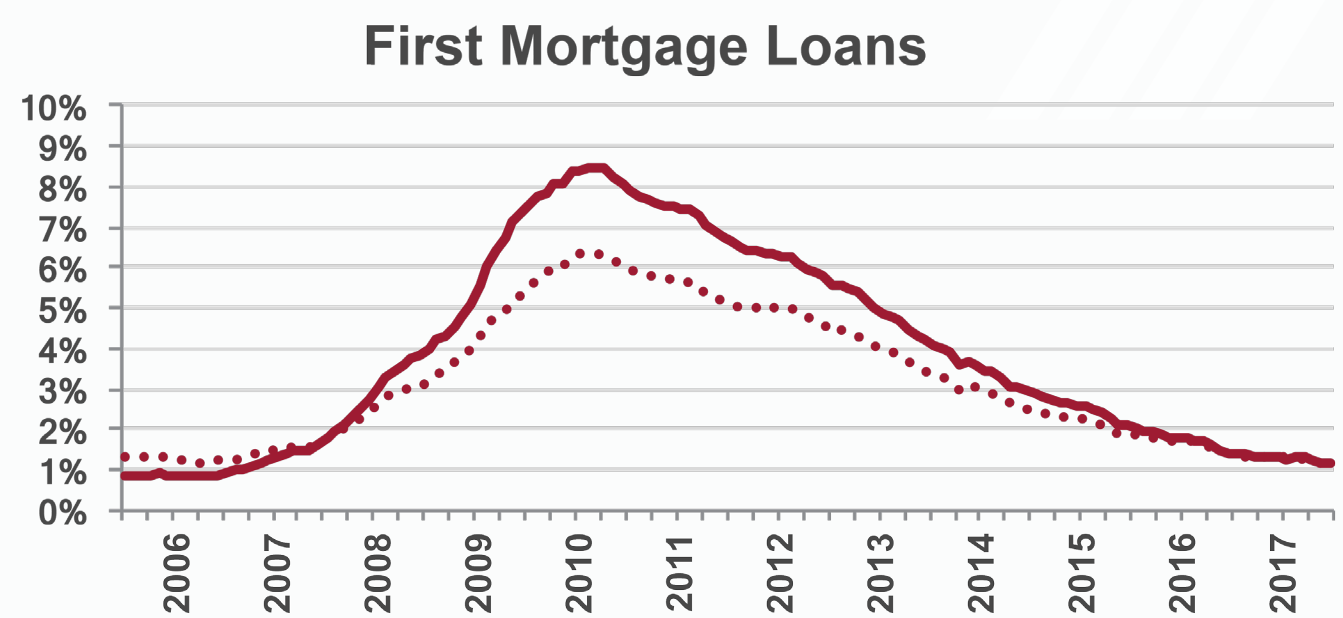
- Auto loans and bankcard are clearly showing rising delinquency rates, but from low levels.
- First mortgage loans are showing a declining incidence of delinquency.
- Consumer finance loan performance is essentially unchanged.

Severe delinquency rates by tradeline type









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Source: Equifax, Inc.

Learn more about **assessing recession risks**

The information in this ebook is a sampling of the insights found in the paper, “Gauging U.S. Recession Risk” by Equifax Chief Economist Amy Crews Cutts and Deputy Chief Economist Gunnar Blix.

Contact Equifax today to learn more about trends in consumer credit and their potential impact on the economy.