by CHRIS KONSTANTINOS

THE RIVERFRONT WRITING TEAM

REBECCA FELTON
Senior Market Strategist

ADAM GROSSMAN, CFA
Global Equity CIO |
Co-Head of Investment Committee

CHRIS KONSTANTINOS, CFA
Director of Investments |
Chief Investment Strategist

KEVIN NICHOLSON, CFA
Global Fixed Income CIO |
Co-Head of Investment Committee

DOUG SANDLER, CFA
Head of Global Strategy

ROD SMYTH
Chairman of the Board of Directors

SUMMARY

- Recession fears are rampant.
- However, our 'Recession Dashboard' tells a different story.
- Five of six indicators suggest the US economy will continue to grow, in our view.

6.06.2022

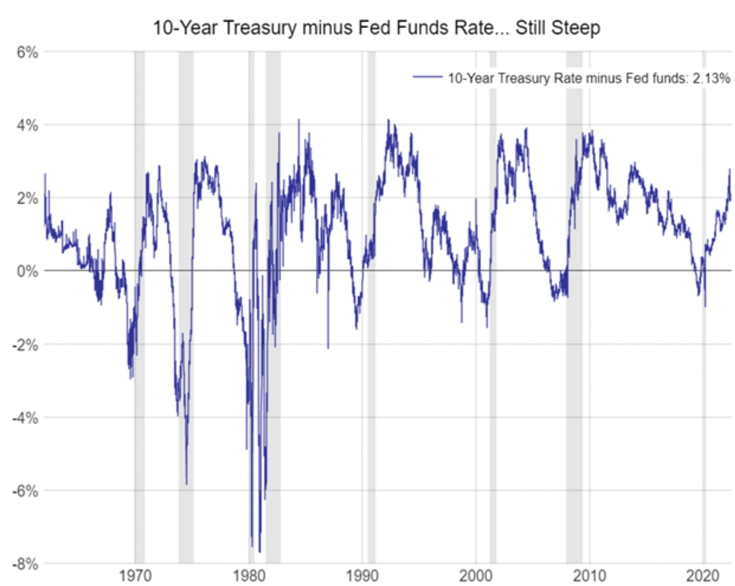
Is the US Headed into a Recession? Glad You Asked! (Part 2)

Our 'Recession Dashboard': Six Indicators to Watch Going Forward

As inflation rages and interest rates move higher, equity markets have felt more pain than the economy. Despite the continued reassurances provided by the monthly economic data releases, worries are mounting that higher prices and borrowing costs will extinguish economic growth. Add to that the growing number of forecasters warning of a US economic downturn, and it is understandable that the question we get most often has become "Is the US headed into a recession?" We think not.

Last week, we focused on recession-tracking primary US economic indicators used by the National Bureau of Research (NBER) (Weekly View 5.31.22), which maintains a chronology of US business cycles. This week we augment the NBER's list with our own 'Recession Dashboard,' a partial list of indicators we have found, in our experience, to be useful recession predictors. No single indicator is infallible; however, taken in aggregate we believe these provide a robust estimation of future recession risks. Shaded regions on the charts below denote historical recessions; each indicator we show has data dating back to at least the 1970s.

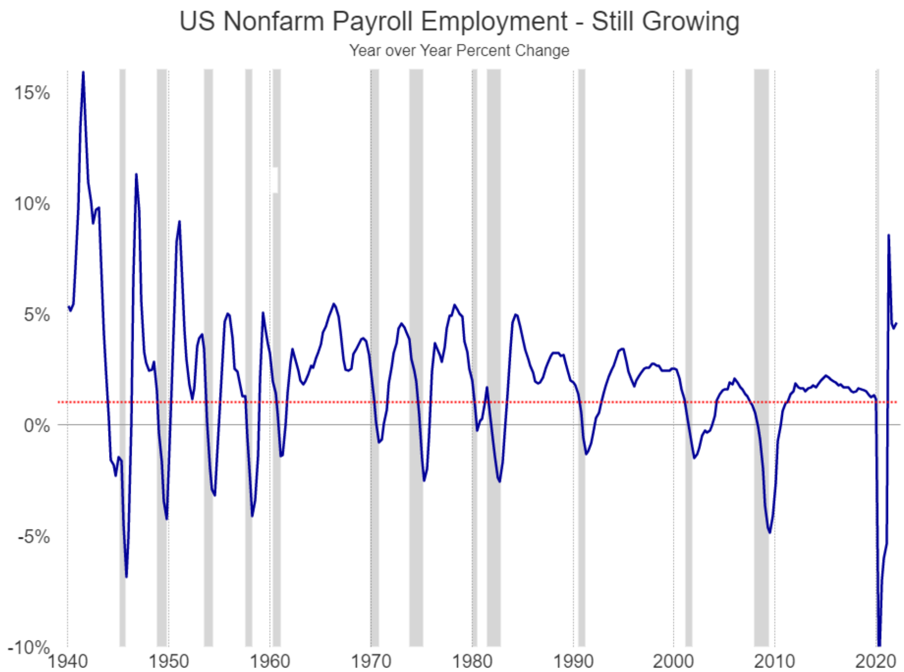
Our conclusion today is the same as last week, in that the weight of this evidence does not suggest an imminent recession. Nonetheless, we are diligently monitoring economic output for signs of further cracks, particularly in consumer confidence. At RiverFront, we believe in 'Process over Prediction,' which means our portfolio positioning is built to adapt as data changes, and thus not predicated solely on accurately forecasting future events such as the next economic downturn.



Source: Refinitiv Datastream, RiverFront. Data quarterly as of April 2022. Chart shown for illustrative purposes.

Yield curve: *Positive* - Not Flashing Warning Yet

The difference between 10-year Treasury and Federal Funds (Fed Funds) yields -aka the 'yield curve'- is still positive as 10-year yields are higher (see chart, previous page). An 'inverted' yield curve (10-year yields lower than Fed Funds) has historically been a reliable signal of impending recession, in our view. After the 10yr-Fed Funds curve inverts, a recession typically starts a year later.



Source: Refinitiv Datastream, RiverFront. Data quarterly as of April 2022. Chart shown for illustrative purposes.

Since the yield curve is still positive and steepening (see chart, left), we view this as a positive sign that a recession is not imminent.

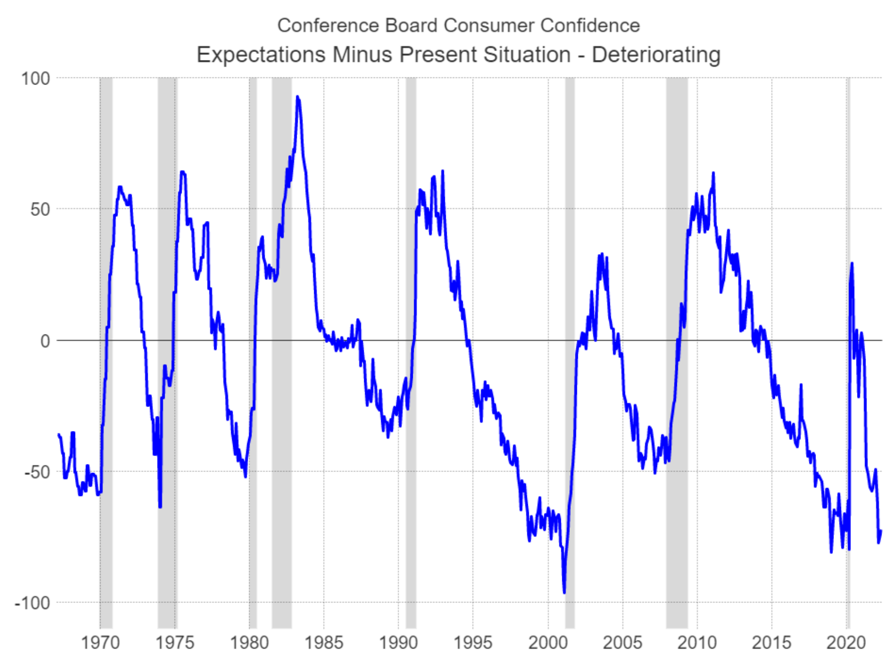
Change in Payrolls:
Slowing in employment trends can give important warning signals concerning the health of the economy. In our experience, a slowing of payroll growth at or below 1% tend to presage recession. Currently, payrolls are growing about 5% year-over-year, and recently reversed back up.

Unemployment: Other employment-related signals we like to follow include the 'Sahm Rule'[1], which is triggered when the three-month moving average of the national unemployment rate rises by at least 0.5% percentage points or more relative to its low during the previous 12 months. Similar to payrolls, this indicator is also in a constructive zone, in our opinion.

Consumer Confidence: *Negative* - Confidence Clearly Slipping

The psyche of the US consumer is important, given that consumer spending represents a significant portion of our economy.

A large drop in the difference between the Conference Board's Consumer Expectations Index and the Present Situation Index usually precedes recession (see chart, right).



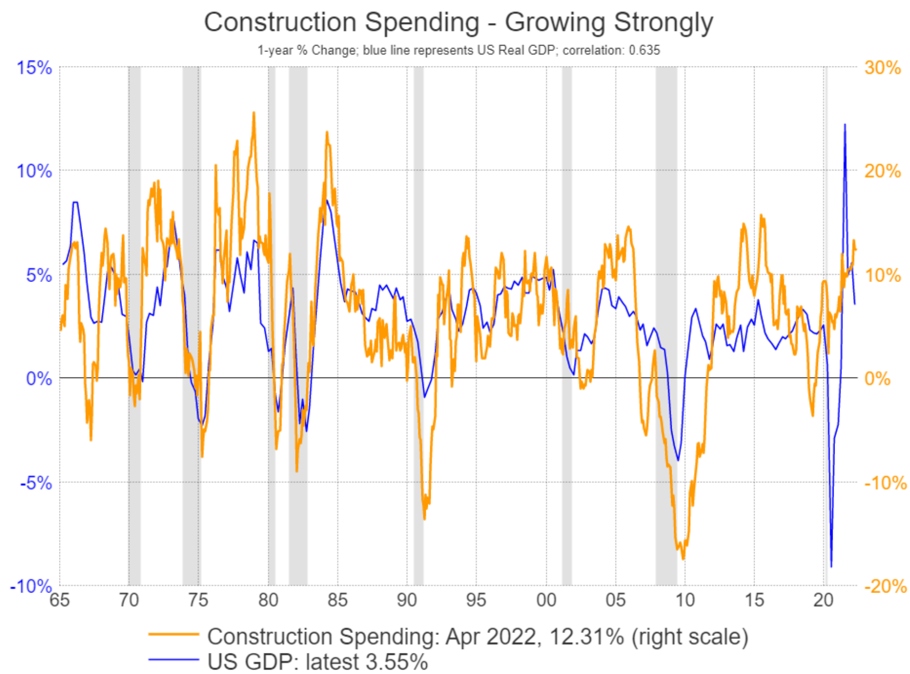
Source: Refinitiv Datastream, RiverFront. Data monthly as of May 2022. Chart shown for illustrative purposes.

[1] The Sahm Rule With The Eponymous Economist : The Indicator from Planet Money : NPR

We believe, this is arguably the only concerning data point in our 'dashboard'. Currently, it is near levels that have suggested recession in the past. We will continue to monitor health of the consumer closely from here.

Construction Spending and Heavy Truck Sales: *Positive* - Data Remains Strong

Construction Spending: Construction plays an important role as a job creator across many industries and as a driver of demand for both natural resources and finished goods. Currently, construction spending is growing at around 12%, a positive in our opinion, for future GDP growth.

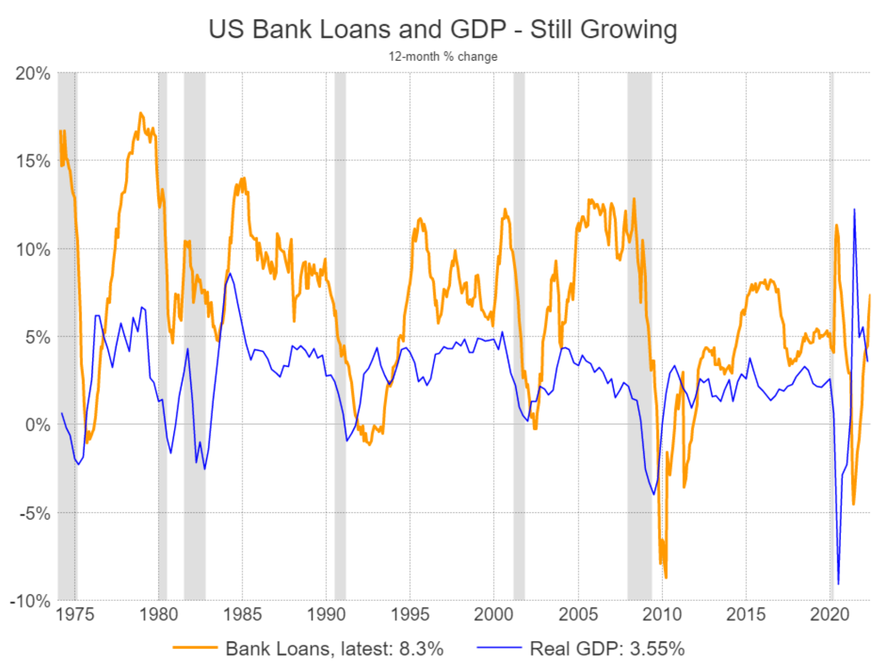


Source: Refinitiv Datastream, RiverFront. Construction data monthly as of April 2022. GDP data as of Q1 2022. Chart shown for illustrative purposes.

Heavy Truck Sales[2]: Another related data point is yearly heavy truck sales which are running at 37k units/month - at the high end of its historical range - suggesting a strong economy, in our view.

Lending: *Positive* – Access to Capital Remains Robust

Capital represents 'lifeblood' for most businesses. Without access to capital, companies are unable to grow and may even need to restrict existing operations.



Source: Refinitiv Datastream, RiverFront. Bank Loan data monthly as of May 2022. GDP data as of Q1 2022. Chart shown for illustrative purposes.

Bank loan creation grew at a historically strong year-over-year rate in May of this year (see chart, left), suggesting to us that companies still are both willing and able to access capital for growth initiatives, hiring, and recapitalization.

Leading Economic Indicators (LEI): *Neutral* – Well Above Zero, Decelerating

The Conference Board's 'Leading Economic Indicators' (LEI) is a predictive variable that is designed to anticipate turning points in the business cycle by roughly seven months.

The LEI is comprised of 10 indicators related to employment, business orders, residential housing demand, stock market prices, and bond market credit conditions.

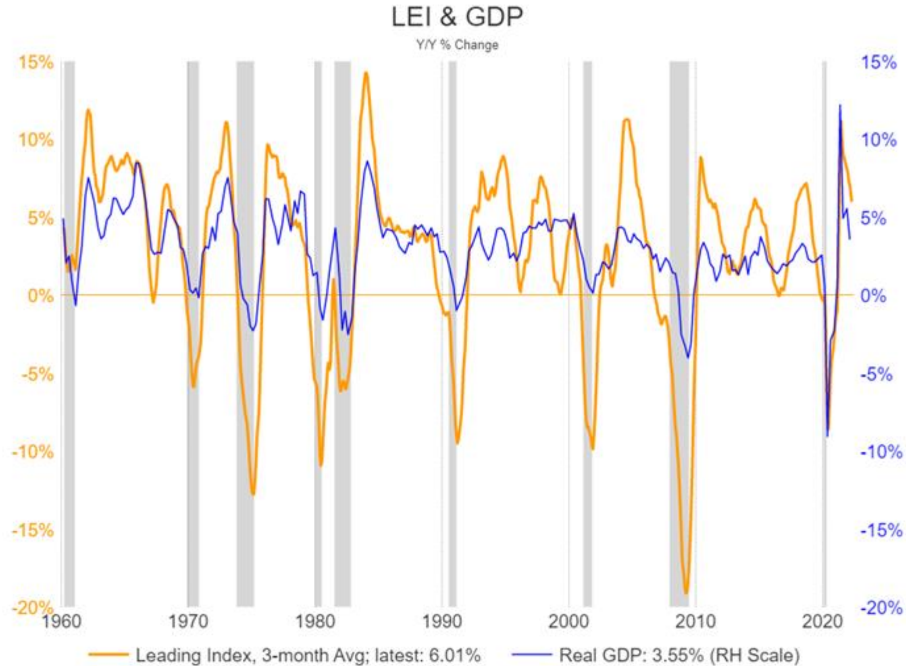
[2] *Heavy trucks weigh over 26,000 pounds and include 18-wheeler tractors, cement mixers, and city buses.*

The change in LEI is still well above zero (see chart, right), suggests to us, positive GDP growth in the future. The LEI has declined back to levels we associate with a healthy economic backdrop.

LEI From a Historical Perspective: Current Expansion Appears to Have Plenty of Room to Run

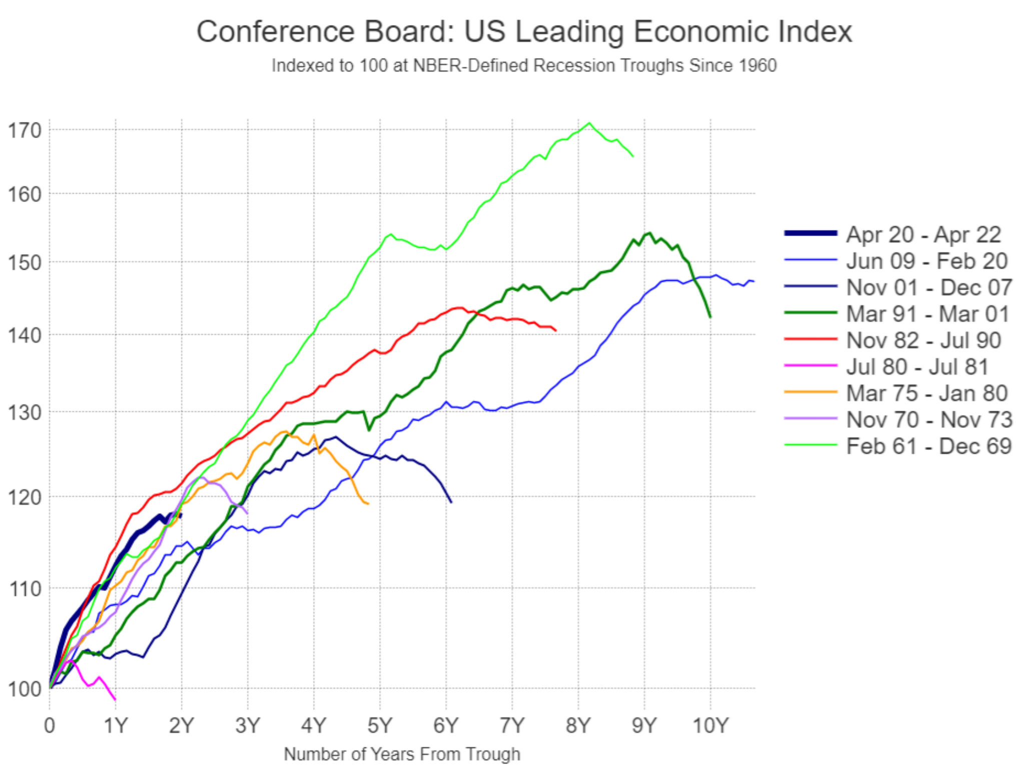
In analyzing LEI behavior during economic expansions over the last 60 years, we think it is worth pointing out that the current expansion (4/2020 to today – thick blue line, chart below) appears early in its lifecycle relative to most others.

As measured by the LEI reading, the current expansion has also been the strongest through its first two years coming out of recession.



Source: Refinitiv Datastream, RiverFront. LEI data monthly as of April 2022. GDP data as of Q1 2022. Chart shown for illustrative purposes.

This suggests to us that the current economic expansion is likely to continue for the foreseeable future, but its pace may need to cool further, creating uncertainty.



Source: Refinitiv Datastream, RiverFront. Data as of April 2022. Chart shown for illustrative purposes.

Conclusion

A strong economy, such as we have had, usually causes the Federal Reserve to raise rates. This tends to make investors nervous as to whether rising rates will end the expansion. If, as we expect, economic growth slows, but remains positive, we think the bull market in stocks can resume. However, it may take many more months for the fear of recession to die down.

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Gross domestic product (GDP) is the total monetary or market value of all the finished goods and services produced within a country's borders in a specific time period. As a broad measure of overall domestic production, it functions as a comprehensive scorecard of a given country's economic health

The Conference Board (CB) is a not-for-profit research organization that distributes vital economic information to its peer-to-peer business members. The Composite Index of Leading Indicators, otherwise known as the Leading Economic Index (LEI), is an index published monthly by The Conference Board

The Sahm Rule identifies signals related to the start of a recession when the three-month moving average of the national unemployment rate rises by 0.50 percentage points or more relative to its low during the previous 12 months.

In a rising interest rate environment, the value of fixed-income securities generally declines.

Stocks represent partial ownership of a corporation. If the corporation does well, its value increases, and investors share in the appreciation. However, if it goes bankrupt, or performs poorly, investors can lose their entire initial investment (i.e., the stock price can go to zero).

Bonds represent a loan made by an investor to a corporation or government. As such, the investor gets a guaranteed interest rate for a specific period of time and expects to get their original investment back at the end of that time period, along with the interest earned. Investment risk is repayment of the principal (amount invested). In the event of a bankruptcy or other corporate disruption, bonds are senior to stocks. Investors should be aware of these differences prior to investing.

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