

Dutta's Monetary Thoughts

What areas may already be in "recession"?

Neil Dutta

Prepare for data deluge

Axios reports that the procedural steps needed to end the government shutdown are being taken. That's welcome news. Prediction markets see the shutdown ending by the middle of the week. Assuming the shutdown cut US GDP by a little over a tenth each week, we're looking at roughly a 0.8ppt hit to GDP growth in Q4 that will get made up later.

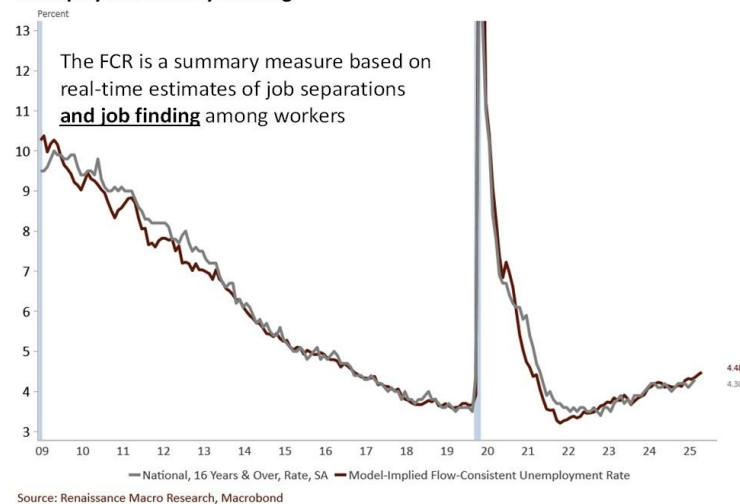
I think one risk, now that we're about to be inundated with a deluge of data, is that if the data are weak investors will discount the news because they'll assume it's largely shutdown related or too stale. On employment, the September data is ready to go, October has not been collected, and the survey collection week for November is next week.

At any rate, in our view, a shutdown (that was going to eventually be resolved anyway) isn't the proximate cause of the weakness in the private economy. I continue to believe that for the real economy, stocks rising will not help as much as rates rising will hurt.

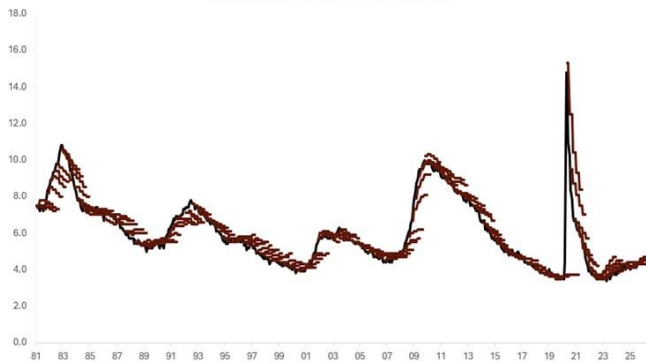
Labor market risks still building

The boilerplate around the labor market appears to be that conditions are gradually cooling, but nothing more, nothing less. I think this consensus thinking misses the fact that downside risks are still climbing. The debate is not about whether things are okay today, but why they ought to stay this way.

Unemployment is likely climbing



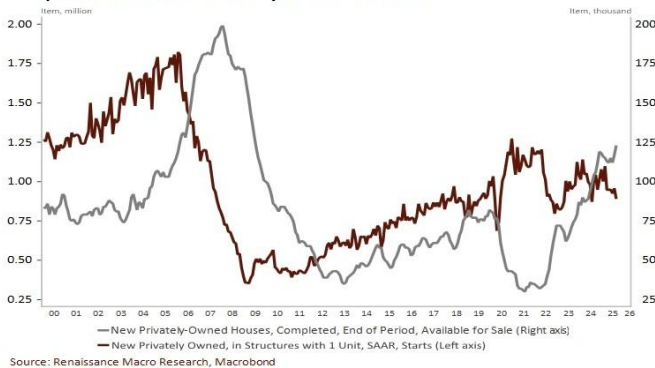
UR with Avg. Bluechip Consensus Forecast



The consensus never really sees it

Our figure shows BlueChip consensus estimates against the actual unemployment rate. In a genuine downturn, the consensus typically assumes a gradual linear increase in unemployment. There is really no way of knowing ex ante if the labor market conditions will transition from linear to nonlinear. Historically, the consensus never sees it even after it has arrived. That things seem to be evolving in a stable fashion now doesn't negate the possibility of an unstable move later.

Completed new home inventory remains elevated



Source: Renaissance Macro Research, Macrobond

Bessent spills the beans on recession

Treasury Secretary Bessent recently acknowledged that sectors of the economy are already in recession. Indeed, as I'll discuss, there are quite a few.

- Residential housing: Homebuilders will need to throttle back construction and focus more on unwinding the elevated stock of unsold homes. This means prices concessions are on the horizon. Moreover, building permits imply weakness in construction activity ahead. The industry is likely holding onto too many workers relative to activity.

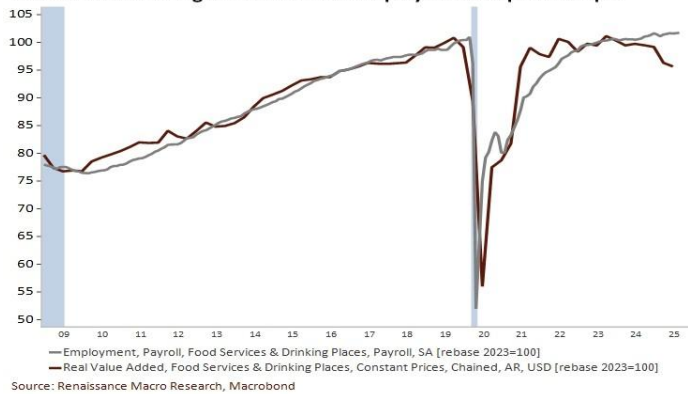
CRE will remain under pressure



Source: Renaissance Macro Research, Haver Analytics

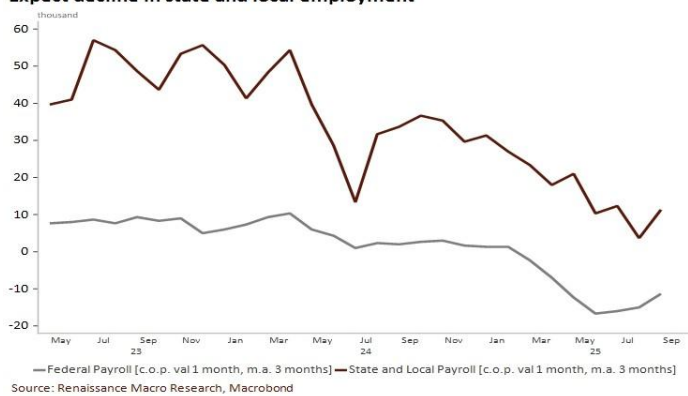
- CRE: Commercial real estate is in recession. Structures investment has been declining for the last six quarters even accounting for the massive data center buildout. Architectural billings remain sluggish. To wit, "The AIA/Deltek Architecture Billings Index (ABI) score of 43.3 for the month is the softest reading since April and represents an increase in the share of firms reporting a decrease from August." Soft conditions are likely to persist next year.

Potential overstaffing as food services employment outpaces output



- Restaurants: We've seen major casual dining establishments post weaker sales growth in recent quarters with many noting they'll absorb higher food input prices, squeezing margins. Our chart shows employment against value added in food services & drinking places. At face value, this implies that productivity per worker is declining, a potential sign of overstaffing.

Expect decline in state and local employment

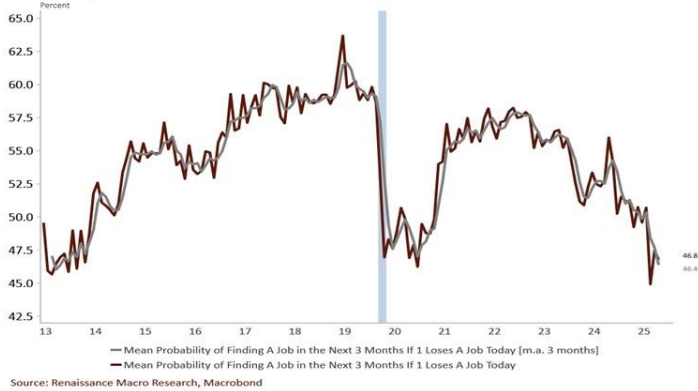


- Government: Public sector employment has declined by design. Up until now, most of the pressure has come at the federal government level. However, state and local governments are expected to be more of a drag on GDP in the quarters ahead. Expecting job losses in state and local governments is a reasonable baseline.

Industries with a smaller employment footprint appear to be softening too.

- Freight: Not as many goods are moving around the country. Ship counts from Asia to the US are down roughly 30 percent from last year. Railcar loadings are down roughly 6% against last year. Finally, capacity continues to come out of the trucking industry.
- Mining: Crude oil prices are somewhat below where they need to profitably invest in new drilling wells. Mining is a very small part of private employment, but it's going down, not up.
- Higher education: Declining enrollment, budget cuts and federal research funding is taxing higher education. Not surprisingly, more colleges and universities are turning to staffing cuts. Employment across colleges and universities has been flat against last year, but it's hard to see why that remains the case.

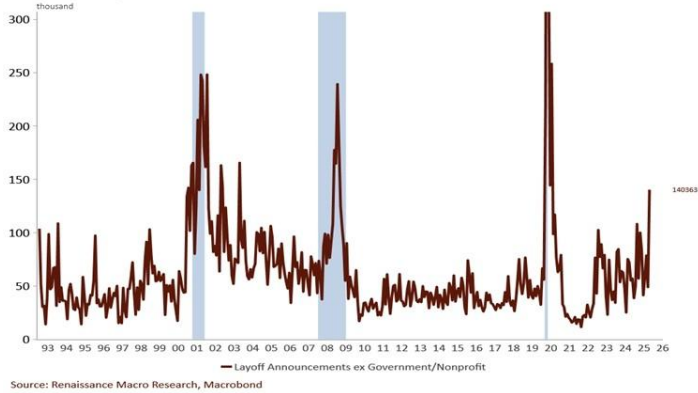
Job finding rate has declined



Downside risks remain high

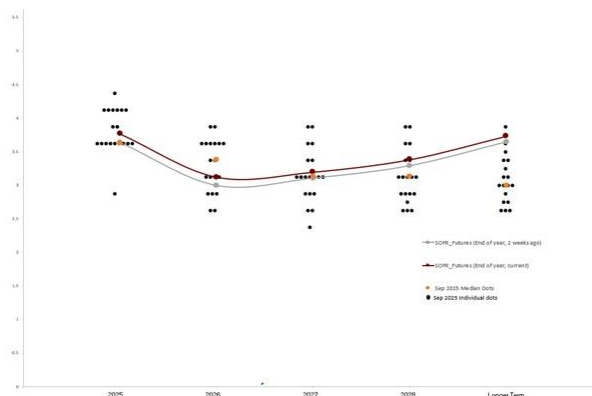
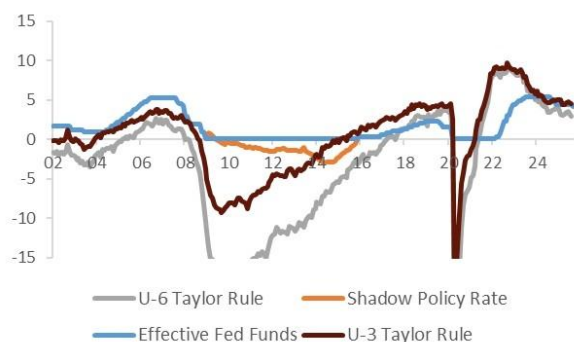
It's taken a while to play out but the labor slowdown has played out in a standard way: job openings have declined, hiring rates have cooled as recruiting intensity has dropped, and we're now beginning to see an increase in layoffs from low levels. The workers at the margins have felt it more than others, also not unusual.

This can't be good news!

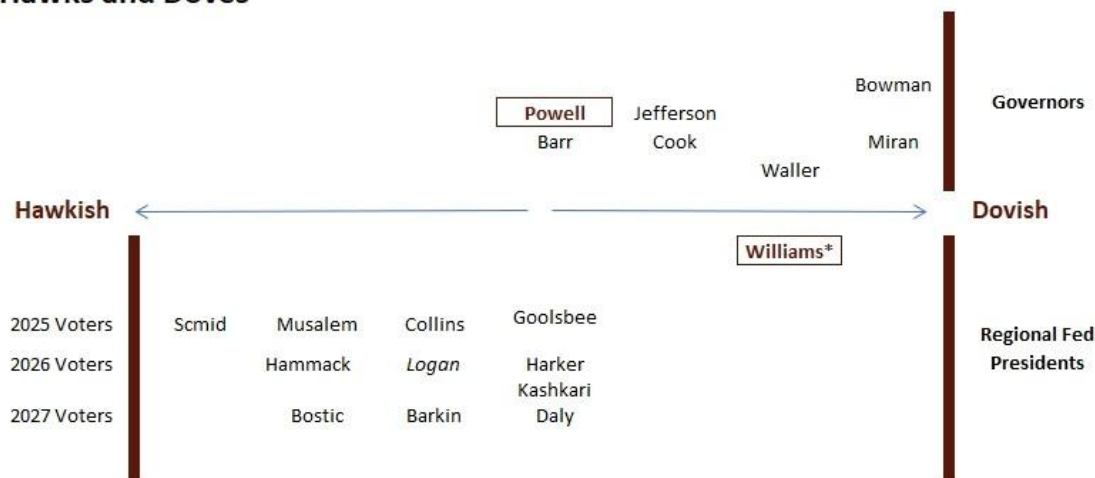


Recession-like dynamics across several different industries increases the risk of additional layoffs in the quarters ahead. Because the hiring rate is low, a small increase in layoffs may have outsized effects on unemployment. Just because conditions seem to be gradually cooling today does not close the door on a more abrupt shift in labor market conditions later. Downside risks remain high.

Monetary metrics



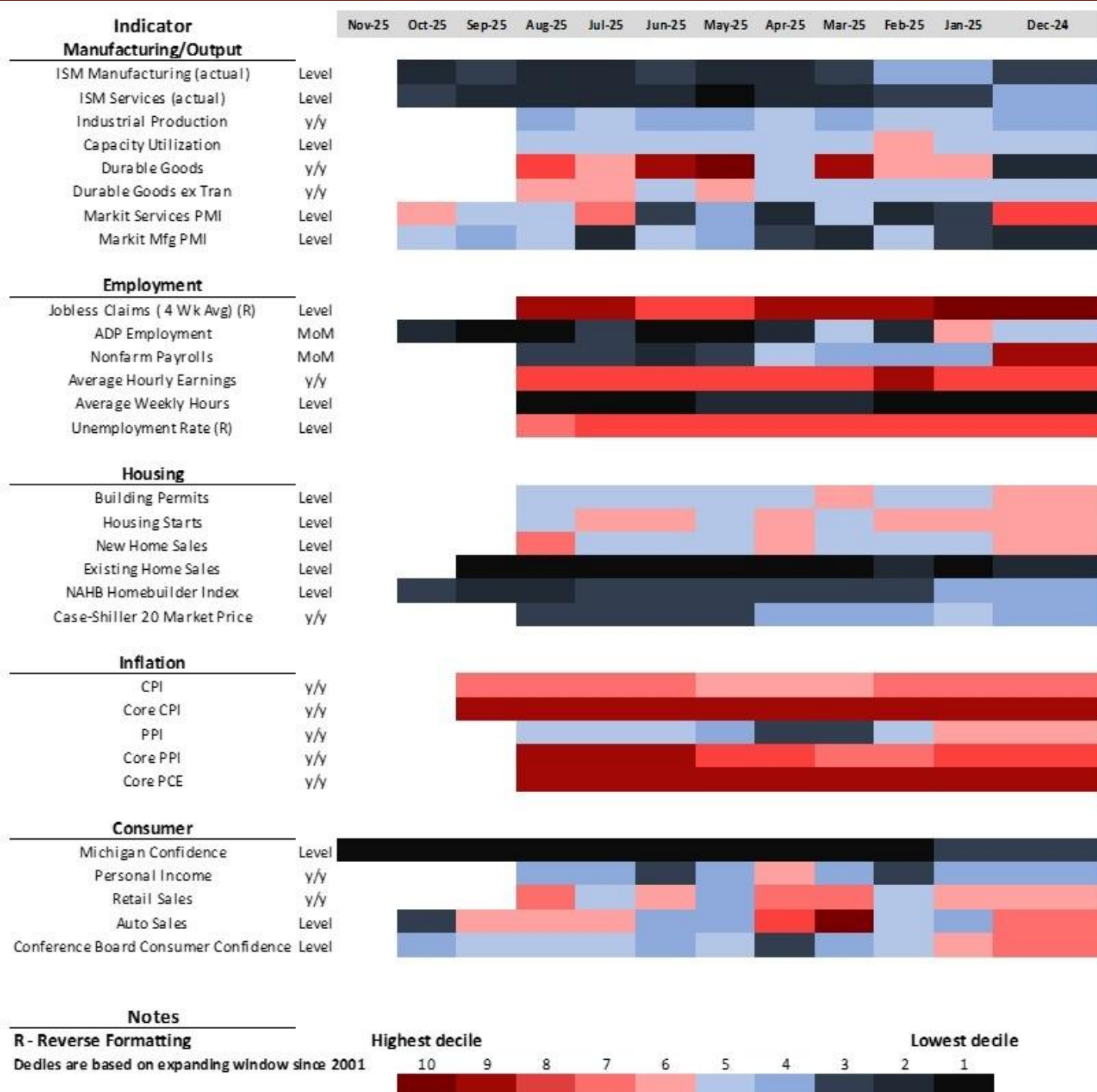
Hawks and Doves



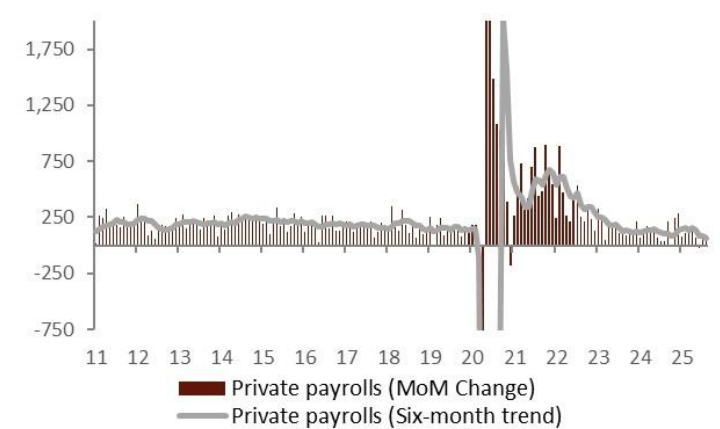
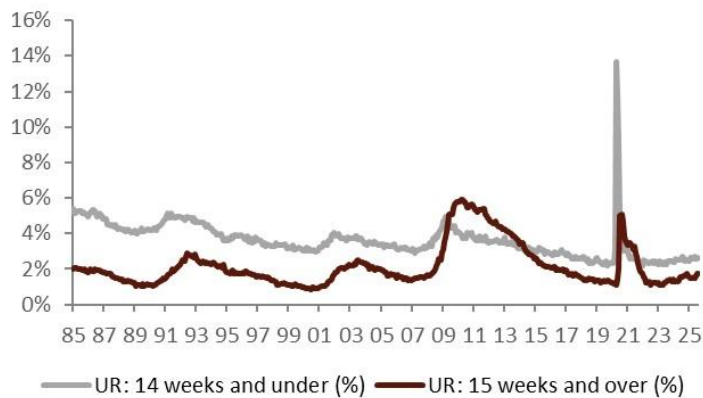
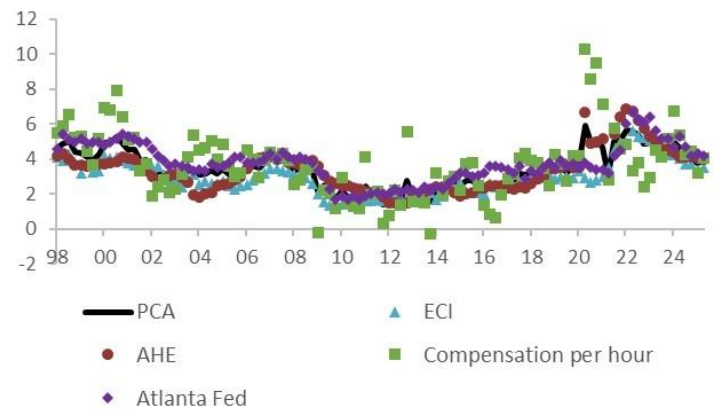
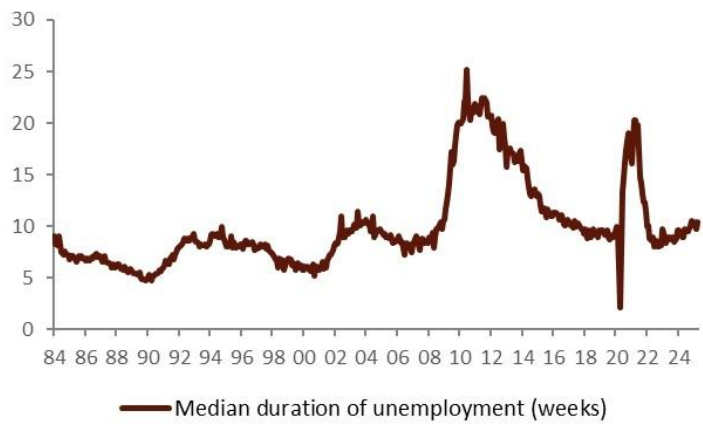
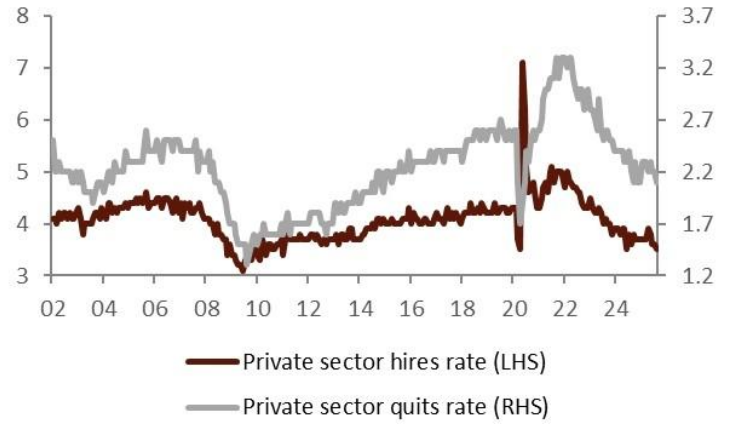
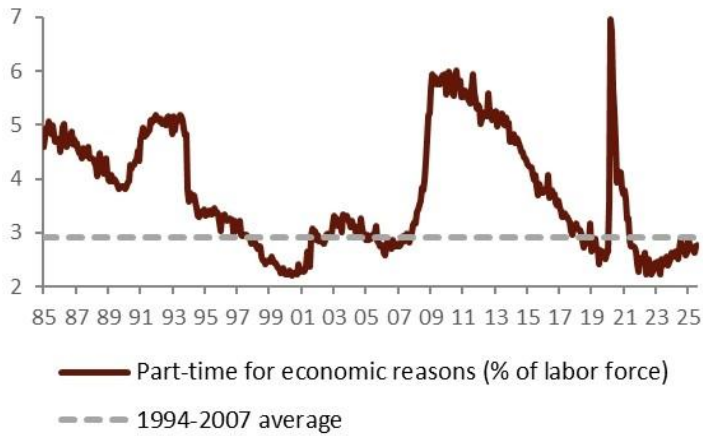
*Federal Reserve Bank of NY President always votes
 Boxed individuals represent FOMC core

FOMC Forecasts	Median					Central Tendency				
	2025	2026	2027	2028	Longer run	2025	2026	2027	2028	Longer run
Change in real GDP										
June projection	1.6	1.8	1.9	1.8	1.8	1.4–1.7	1.7–2.1	1.8–2.0	1.7–2.0	1.7–2.0
Unemployment rate										
June projection	4.5	4.4	4.3	4.2	4.2	4.4–4.5	4.4–4.5	4.2–4.4	4.0–4.3	4.0–4.3
PCE inflation										
June projection	3.0	2.6	2.1	2.0	2.0	2.9–3.0	2.4–2.7	2.0–2.2	2.0	2.0
Core PCE inflation										
June projection	3.1	2.6	2.1	2.0	2.0	3.0–3.2	2.5–2.7	2.0–2.2	2.0	2.0
Projected policy path										
Fed funds rate										
June projection	3.6	3.4	3.1	3.1	3.0	3.6–4.1	2.9–3.6	2.9–3.6	2.8–3.6	2.8–3.5
	3.9	3.6	3.4		3.0	3.9–4.4	3.1–3.9	2.9–3.6		2.6–3.6

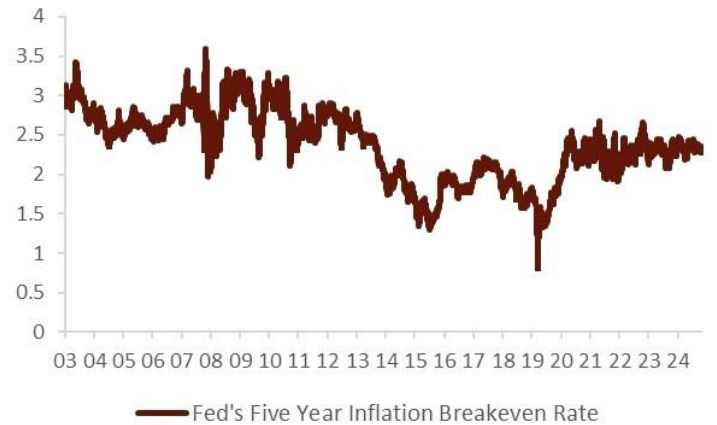
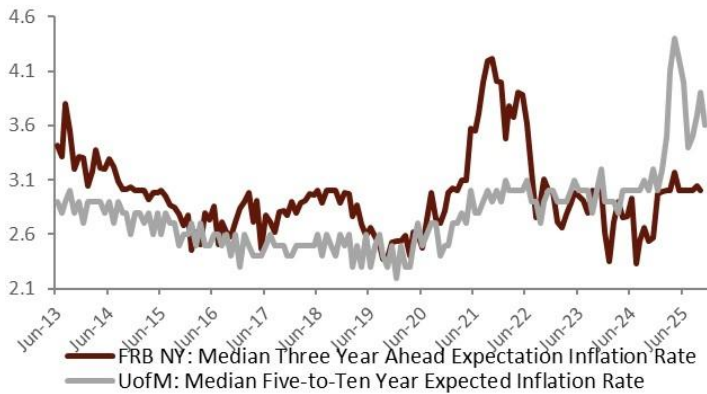
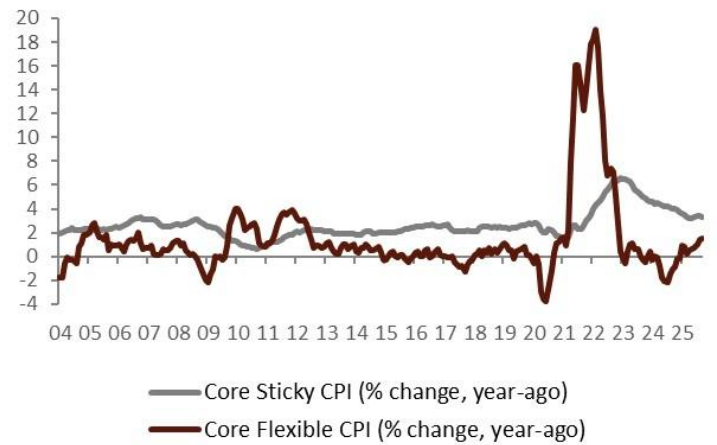
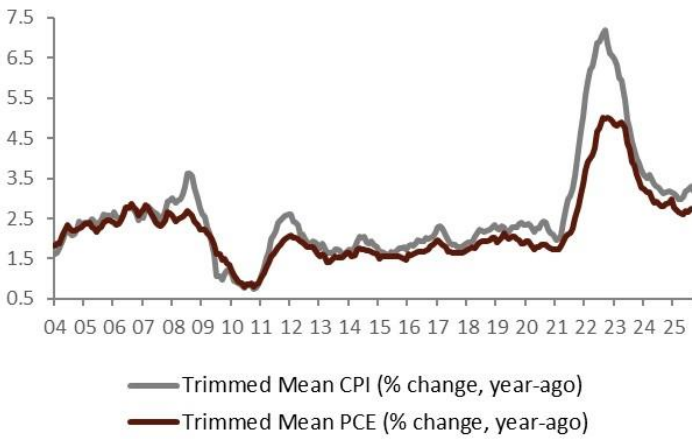
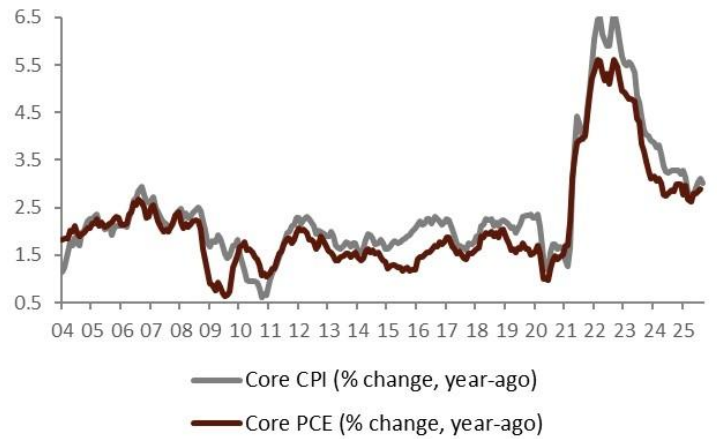
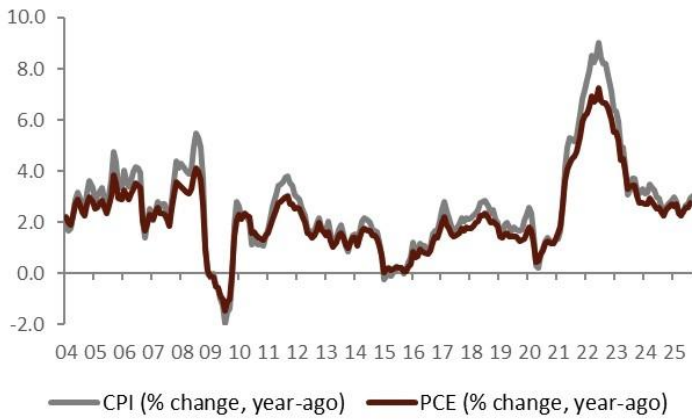
High frequency data heat-map



Labor market indicators

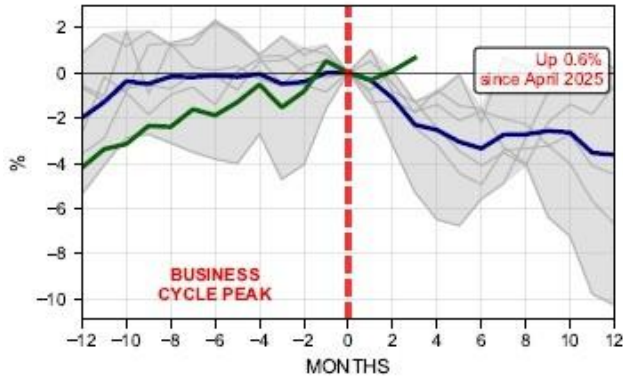


Inflation indicators

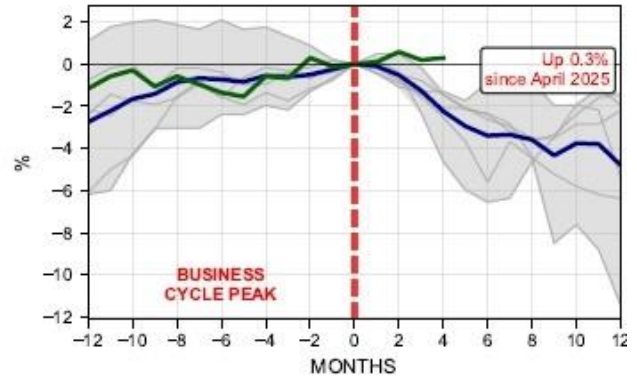


NBER RECESSION INDICATORS DASHBOARD

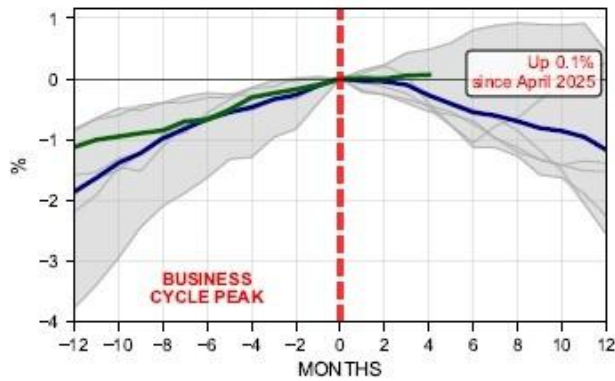
REAL SALES: MANUFACTURING AND TRADE INDUSTRIES



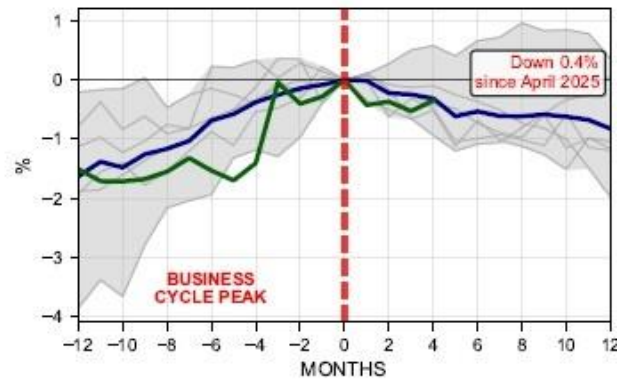
INDUSTRIAL PRODUCTION



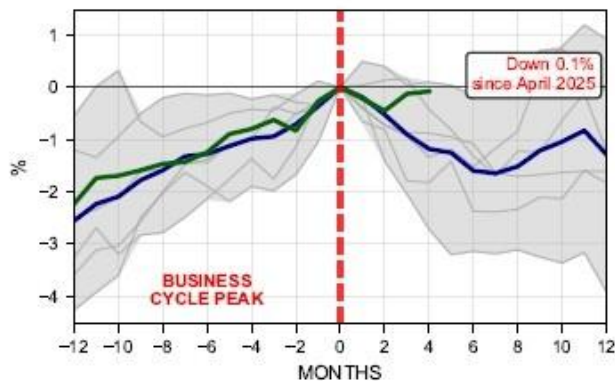
US NONFARM PAYROLLS



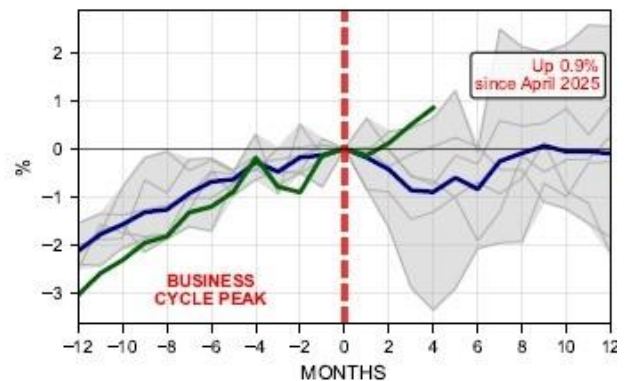
CIVILIAN EMPLOYMENT



REAL PERSONAL INCOME MINUS CURRENT TRANSFER RECEIPTS



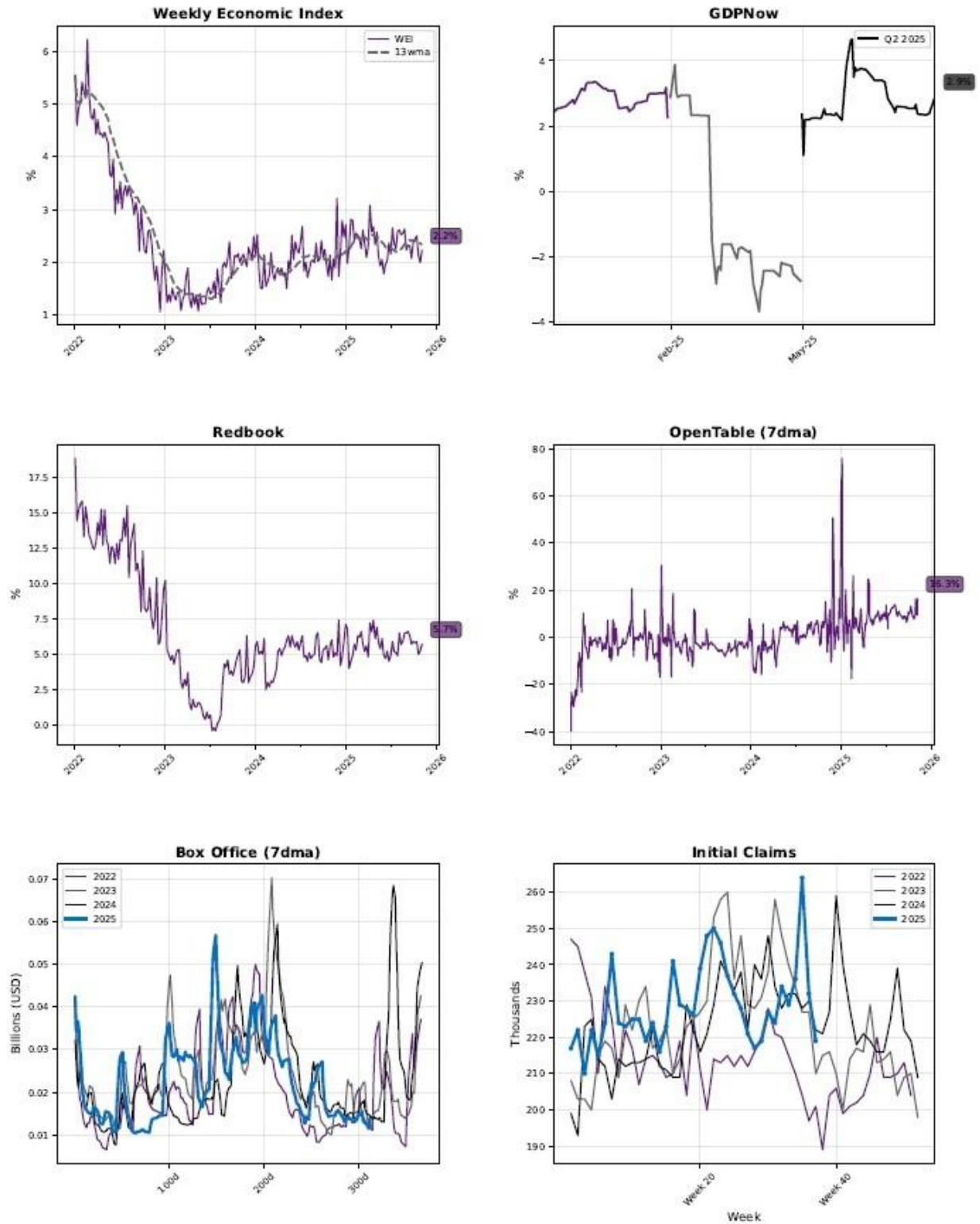
REAL PCE



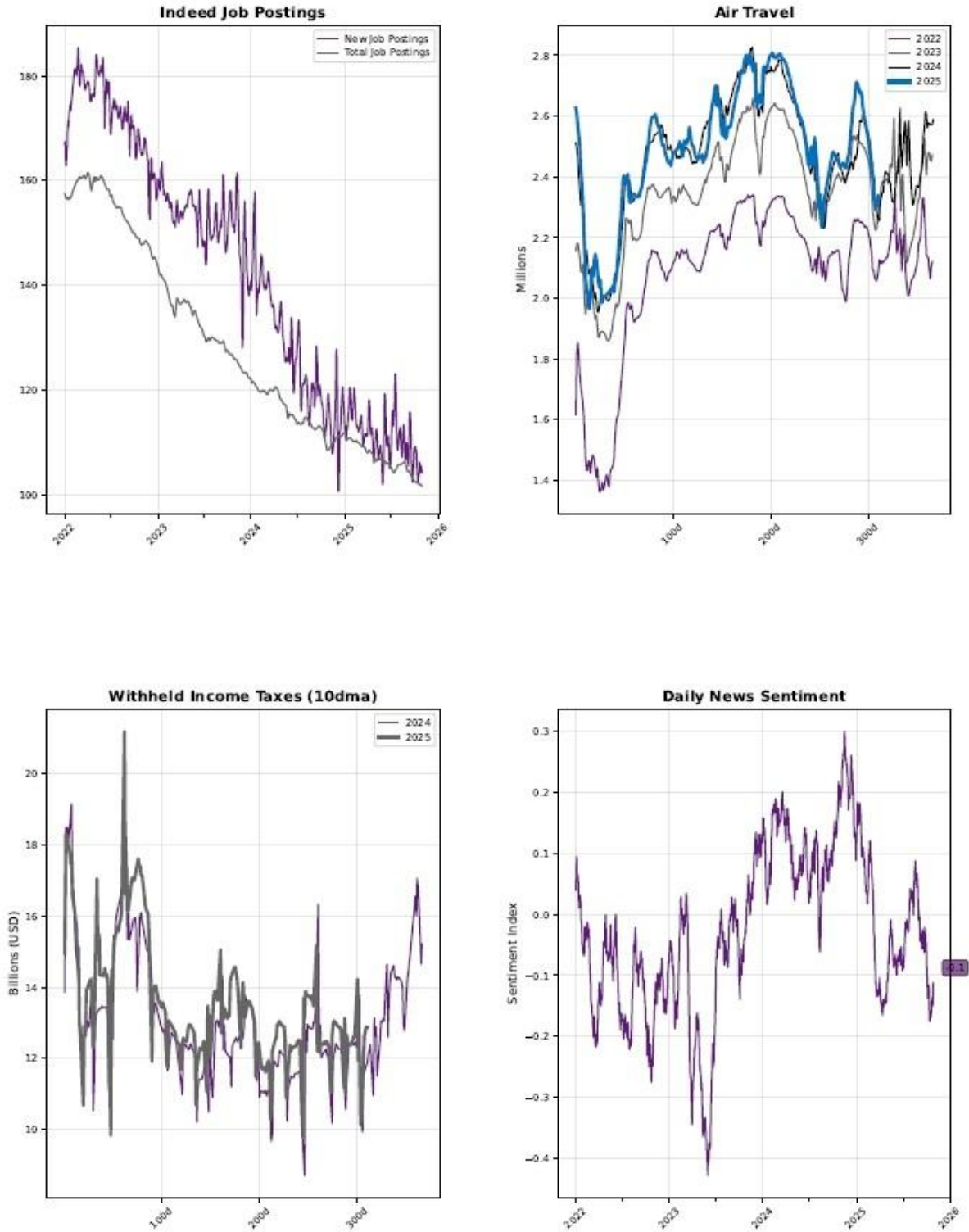
PAST CYCLES (RANGE) — PAST CYCLES — PAST CYCLES (MEAN) — CURRENT CYCLE

Past 7 cycles excluding Covid-19 period

High Frequency Economic Dashboard



High Frequency Economic Dashboard



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