First Trust
Monday Morning OUTLOOK

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A Plow Horse With Shin Splints

Our position on the economy has been that the US is headed for a recession, but we're not quite there yet. Nothing in all the recent data reports changes our minds. Look for a recession to start in the second half of 2023, with some possibility of it starting earlier in 2023 and some possibility of a delay until early 2024. Until then, expect mediocre economic growth.

We called the recovery after the Financial Panic and Great Recession of 2008-09 the "Plow Horse Economy." Real GDP growth averaged 2.2% annualized in the eight years after that recession ended. That was very slow by historical standards and we think it was due to a large expansion in the size and scope of government. The bigger the government, the smaller the private sector, creating slower real growth.

It's hard to tease out the underlying pace of growth so far in the current recovery because of the nature of COVID-related shutdowns. However, it looks like real GDP growth will be roughly +0.5% in 2022 (Q4/Q4), which would be slower than any calendar year without a recession since the end of World War II. Call it a "Plow Horse with Shin Splints."

This description of the economy might surprise some investors, particularly given Friday's robust increase in payrolls. But we think many journalists, analysts, and investors misinterpreted the employment report, which wasn't as strong as the headline. Yes, payrolls rose a very solid 263,000 in November. But the most important data point each month is the change in the total number of private-sector hours worked, which declined 0.2% for the month. That's the equivalent of losing about 250,000 jobs. Total hours worked are up at a modest 1.1% annual rate in the past three months, signaling slower job growth ahead.

The Atlanta Fed's "GDP Now" model suggests real GDP growth at a 2.8% annual rate in the fourth quarter, but we think growth is very likely going to fall short of that pace; we're penciling in growth at only a 1.5% annual rate, instead. In particular, look for the trade sector, which was the key behind more rapid growth in the third quarter, to be a major drag on growth in the final quarter of the year.

Another report we're concerned about is the upward creep in continuing jobless claims. Continuing claims averaged 1.363 million in the four weeks ending October 1. In the four weeks ending November 19, they averaged 1.539 million. A jump like that is not the end of the world, nor does it show we're in a recession already. But it probably signals that the low point in the unemployment rate is behind us (at 3.5%) and is another reason to think job growth will be slower in the months ahead.

The factory sector, in particular, is showing early signs of softness, with the ISM Manufacturing index coming in at 49.0 for November, the first sub-50 reading since the early days of COVID. Yet, the ISM Services index came in at 56.5, reflecting a catch-up from all the service closures during COVID.

If you want to weave a very negative story, you have the data to do it with. But it's important to look at a full range of reports and not get captured by your own narrative. Some key parts of the economy remain solid. For example, sales of medium and heavy trucks were up 11.4% in November versus a year ago. Usually, this measure goes negative at least several months before a recession starts.

Put it all together and you have a weak economy that's still growing but showing some signs of wear and tear. A Plow Horse, with shin splints. Stay tuned: rougher times are ahead, a recession is still in the future, but not happening today.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
12-5 / 9:00 am	ISM Non Mfg Index – Nov	53.5	**53.7**	56.5	54.4
9:00 am	Factory Orders – Oct	+0.7%	**+0.7%**	+1.0%	+0.2%
12-6 / 7:30 am	Int'l Trade Balance – Oct	-$80.0 Bil	**-$80.1 Bil**		-$73.3 Bil
12-7 / 7:30 pm	Q3 Non-Farm Productivity	+0.6%	**+0.4%**		+0.3%
7:30 am	Q3 Unit Labor Costs	+3.1%	**+3.0%**		+3.5%
2:00 pm	Consumer Credit – Oct	$28.0 Bil	**$29.4 Bil**		$25.0 Bil
12-8 / 7:30 am	Initial Claims – Dec 3	230K	**228K**		225K
12-9 / 7:30 am	PPI – Nov	+0.2%	**+0.3%**		+0.2%
7:30 am	"Core" PPI – Nov	+0.2%	**+0.1%**		0.0%
9:00 am	U. Mich Consumer Sentiment- Dec	56.9	**57.0**		56.8