October 2019

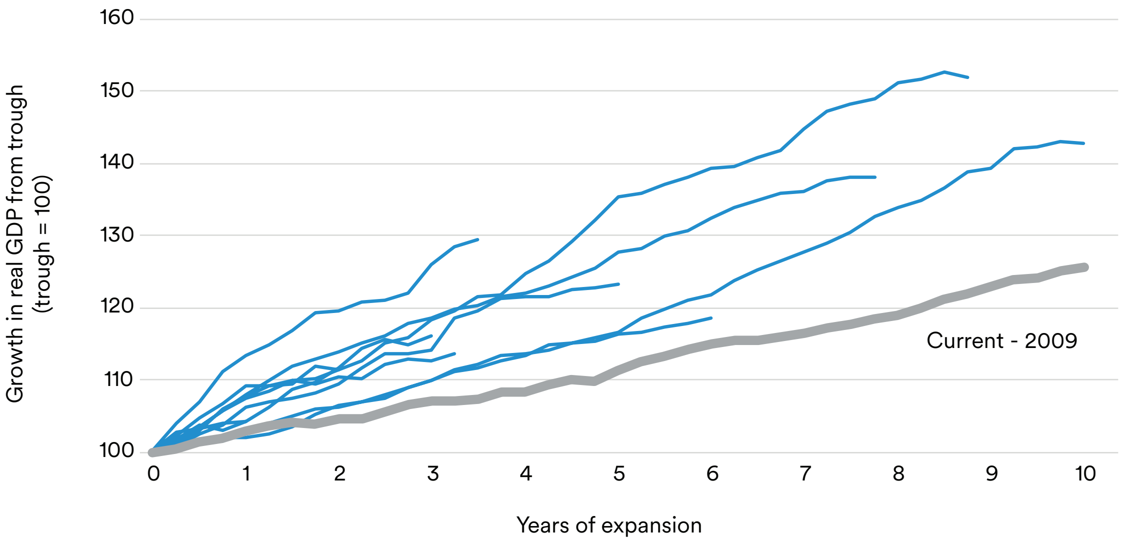
# Is the End Near?

## WHY WE FEEL THE U.S. ECONOMIC EXPANSION IS NOT OVER YET

MetLife Investment Management

Key variables suggest a healthy U.S. consumer is offsetting the only modest fallout from the ongoing U.S.-China trade war and other global uncertainties. Despite the duration of economic expansion, the rate of expansion has been slow. As a result, there has not been a buildup of excesses that has typically worked against future growth historically. Given the strength of the economic indicators and the lack of an obvious triggering mechanism for a downturn, we feel it is more likely that the next recession will occur after the 2020 U.S. presidential election, not before.

## A Record Expansion - Longest And Shallowest

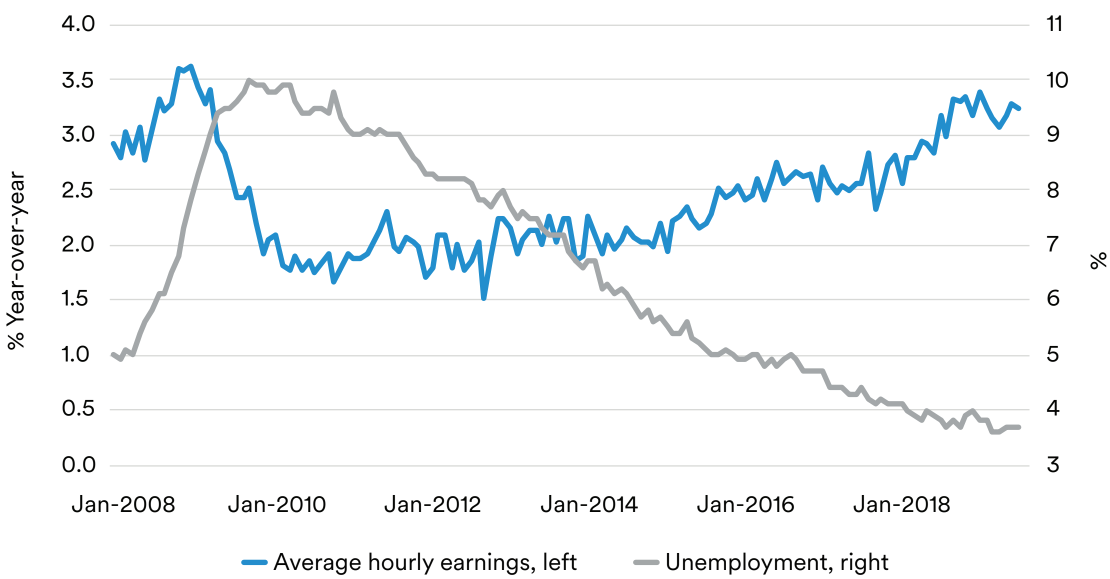



*Source: Bureau of Economic Analysis, National Bureau of Economic Research and MetLife Investment Management*

We believe that any outlook on the U.S. economy must begin with the outlook for the U.S. consumer. Consumption has historically been the most significant contributor to economic activity. With this in mind, we should consider whether the U.S. consumer has the means and the will to continue spending.

The means primarily come from wages but are also a function of wealth, savings and credit availability. Wage growth as measured by average hourly earnings has accelerated and has been keeping up with inflation. A still-tight labor market suggests the current rate of wage growth may be sustained, at least until we see weakness in the labor market. The Federal Reserve recent Flow of Funds report showed that U.S. consumer net worth reached a record high $113 trillion in Q2 2019, or 693% of disposable income, significantly above the post-crisis low of 556%. The savings rate is currently at a healthy figure. Finally, consumer credit is seeing reasonable growth (see chart) even as consumer debt service metrics remain near all-time lows.

## Wages Have Been On The Rise




*Source: Bureau of Labor Statistics and MetLife Investment Management*

Given all the good news about the consumer, the two things consumers should fear are a possible rise in layoffs and a further decline in interest rates. Regarding the former, initial unemployment insurance claims measured as a percentage of the labor force are near all-time lows (since 1971) (see chart) and the economy continues to add to payrolls each month. The unemployment remains near a 50-year low and the number of job openings still surpasses the number of unemployed. We believe it would take some time for the labor market to turn far enough for the average worker to have to seriously worry about the possibility of losing their job and income. Lower interest rates pose a more unique risk as aging workers look ahead to lower fixed-income rates as they approach retirement, prompting additional savings. While this remains a risk, rates are already quite low, and we believe the prospect of negative rates in the United States remains low so long as the Federal Reserve maintain a positive policy rate.

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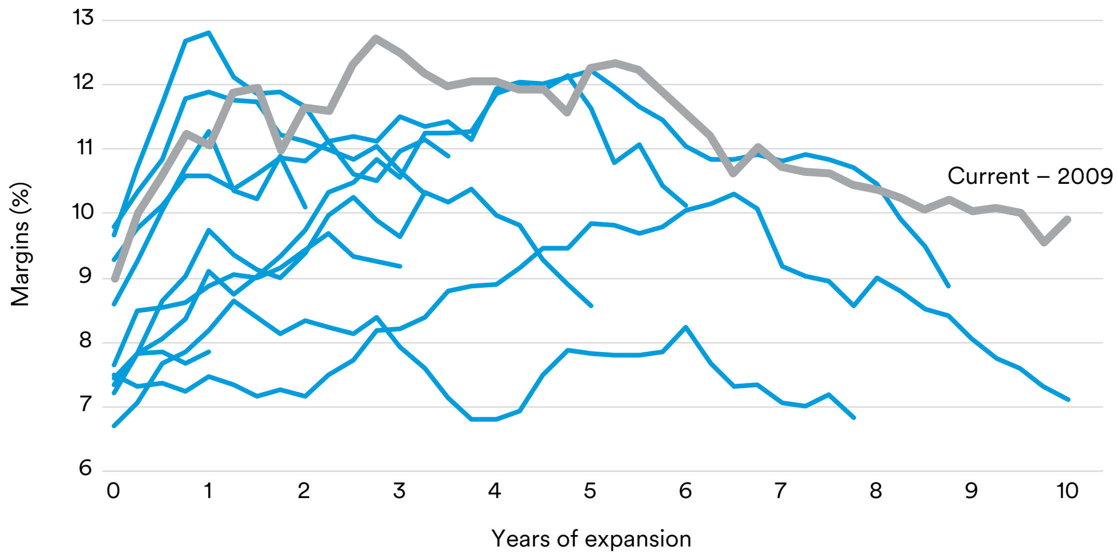
## With All This Good News, Why Is The Clock Ticking At All?

Economy-wide margins have been declining since the corporate profit recession of 2015-2016. Margins had appeared to stabilize in late 2016 at 10.7%. Since that time, they have drifted down to 10.0% (see chart). We see a two-percentage point decline as being a sign that a recession is more likely. As a move to lower in margins has already begun and we have dropped roughly 60 basis points lower in one year. We believe a continued erosion of margins at that pace would suggest a potential recession between one and two years out or 2021.

## Economy-Wide Margins Are Gradually Slipping

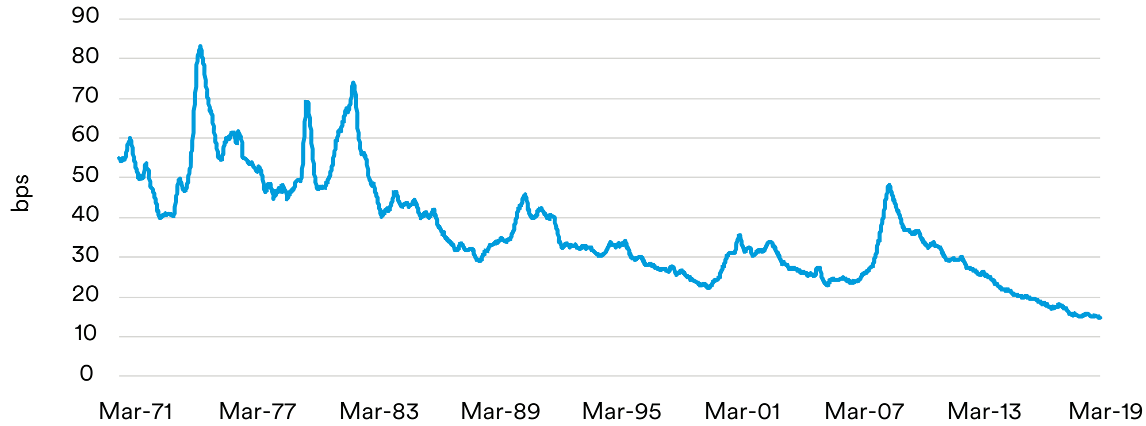



*Source: Bureau of Economic Analysis and MetLife Investment Management*

## Warning Signs

Given the importance of the U.S. consumer to our outlook, we are watching the unemployment insurance claims data carefully. This data is basic, an adding up of filed forms, and timely, as the data is provided weekly. The data currently shows claims at an all-time low (data back to 1971). A sustained uptick in claims would be an indication that the cycle could be nearing its end.

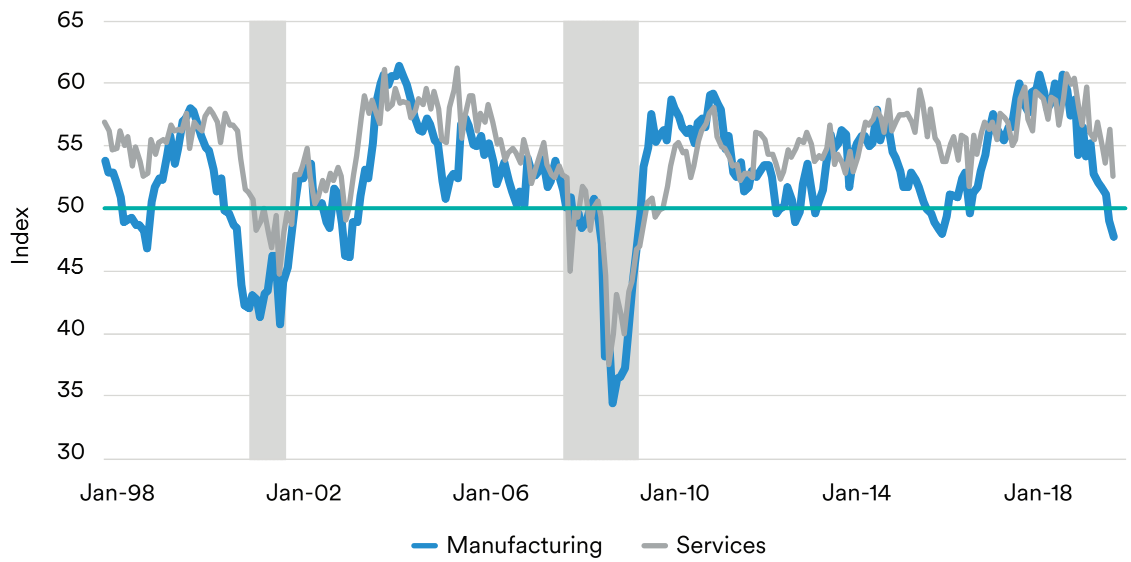
## Unemployment Claims, % of Eligible Employees, 3M Avg




*Source: Department of Labor and MetLife Investment Management*

Similarly, weakness in the ISM surveys, particularly the service sector index, would heighten our level of concern. While the manufacturing survey continues to exhibit a cyclical pattern, the service sector survey has not. The data shows the service sector index at a still-healthy level. As such, a move in the service sector ISM index below 50 would be an indication that the cycle could be nearing its end.

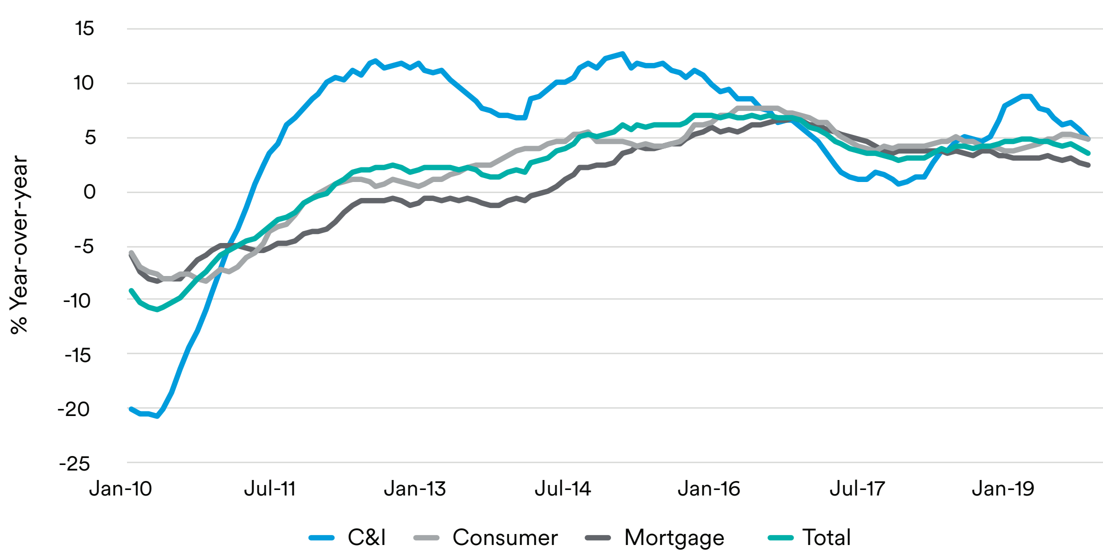
### Activity Indices Still At Levels Associates With 2%+ Growth




Note: Shaded area denotes recession
*Source: ISM, National Bureau of Economic Research and MetLife Investment Management*

Finally, weakness in core bank loans (i.e., loan to the real economy not to other areas of the financial sector) would be a source of concern. For now, continued loan growth suggests "animal spirits" remain in the economy with businesses and consumers willing to borrow based on their outlook for the future.

### Core Bank Loan Growth Continues




*Source: Federal Reserve Board of Governors, Haver Analytics and MetLife Investment Management*

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MetLife Investment Management leverages a disciplined credit research and underwriting process to provide institutional investors with asset origination and acquisition opportunities and proprietary risk management analytics across public fixed income strategies, private capital, and commercial real estate debt and equity investing, among others.

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