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Part 1: Recession and Low Sales Looming. How to make 2MEOGA Companies Recession-proof to Reduce the Scorching Impact

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When the US economy sneezes, the world catches cold - Anonymous

1.0 The Announcement of Likely Recession

Is the US, the world's largest economy heading for a recession? Or is the economy simply hitting a rough spot? Recent economic indicators in the United States seem to point towards that direction with many analysts, and many more joining every day, saying the economy could be in a recession later this year or early next year. Comprehensive sales have been low for most of the year in most of the economies of the world. While the sales have been mostly dull, the basic question is whether the situation will persist or degenerate.

Explaining Recession

Recession is a period when the economy of a country is not doing well, industrial production and business activity are at a low level, and there are many people unemployed due to job losses and low job availability in the market. It is a period, usually at least six months, of low economic activity, when investments lose value, businesses fail, and unemployment rises

How will you know you are before the recession cliff? The historical indicators

The indicators are:

1) Inverted Yield Curve

The yield curve represents the difference in interest rates across different maturities. For example, a Treasury bill might have a much different yield to maturity than a 30-year government bond. The rates at different maturities are called the yield curve or the 'term structure.'

When long-term bonds have a lower yield than short-term bonds, it can indicate that investors are losing confidence in the short-term economy and expect interest rates to fall. Investors observe the shape of the Treasury yield curve - which plots the yields of all Treasury securities - because it reveals market expectations on monetary policy and the economy. An inverted yield curve, which occurs when short-term debt yields more than long-term paper, has been a harbinger of a recession in nine out of 10 instances over the last 70 years, according to the Deutsche Bank data. In other words, normally one expects one's investment/savings will have more value with time (normal yield curve) , but the future uncertainty ,and reducing scope of investment and expectations of reduced purchasing power of savings can make the future value less than what is currently now (Figure 1).

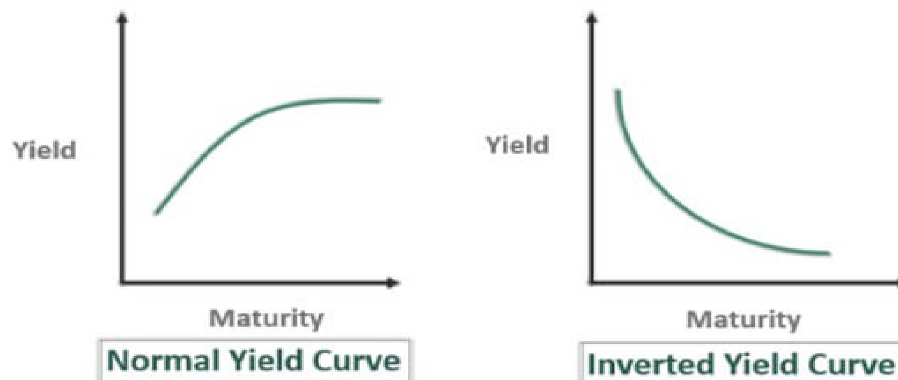

Figure 1. Inverted Yield Curve.

(Courtesy:https://www.google.com/url?sa=i&url=https%3A%2F%2Fwww.wallstreetmojo.com%2Finverted-yield-curve%2F&psig=AOvVaw1yAVCPsAE6ExffW1Hl97Tp&ust=1722798945737000&source=images&cd=vfe&opi=89978449&ved=0CBEQjRxqFwoTCLjc5v3W2ocDFQAAAAAdAAAAABAE)

(Reading aid: In the US, **The Treasury** manages federal spending, collects taxes, issues bonds, bills, and notes, prints money, and advises the president on economic policy. The Treasury also manages government debt through the Treasury General Account (TGA), which receives proceeds from Treasury securities, holds funds to pay interest on debt, and redeems maturing securities. **The Federal Reserve** conducts monetary policy, controls the money supply, and keeps the economy stable. The Fed's primary tools include interest rate setting, Open Market Operations (OMO), and changing the mandated reserves requirements for commercial banks. The Fed can also act as a lender of last resort to rescue failing banks.)

2) More on the Yield Curve

The yield curve represents the difference in interest rates across different maturities. For example, a Treasury bill might have a much different yield to maturity than a 30-year government bond. The rates at different maturities are called the yield curve or the 'term structure.' Normally, long-term interest rates are higher than short-term rates. Think of a Certificate of Deposit (CD) at your bank. If you lock your money in for 5 years, it is almost always for a higher rate than for, say, a six-month CD. So a normal yield curve is positive, meaning longer maturity at a higher rate. However, in rare occasions, this can flip around and we get short-term rates that are higher than long-term rates.

3) Leading Economic Index

The Leading Economic Index (LEI) provides an early indication of significant turning points in the business cycle and where the economy is heading in the near term. Sustained declines in this index have historically

When people believe there is increased risk of a crisis or a recession, they shift their assets into this bond. This is sometimes known as a 'flight to quality'. Buying pressure on the 10-year drives prices up, thereby lowering yields. The long-term yield can be lowered to such an extent that it ends up below the short-term yield – an inverted yield curve. So think of the yield curve as an indicator of sentiment about the future of the economy and the risks we face. Yield curves are 90 percent of the time 'normal' (meaning longer-term rates exceed short-term rates). However, on those occasions when they are inverted, it is almost always bad news.

(LEI) for the U.S. declined by 0.2 percent in June 2024 to 101.1 (2016 = 100), following a decline of 0.4 percent (upwardly revised) in May, 24. Over the first half of 2024, the LEI fell by 1.9 percent, a smaller decrease than its 2.9 percent contraction over the second half of last year.

Figure 2. Since 2021, LEI has been decreasing only to reverse by the end of 2023; but the increase seems more and more unsustainable as the global demand stagnating.

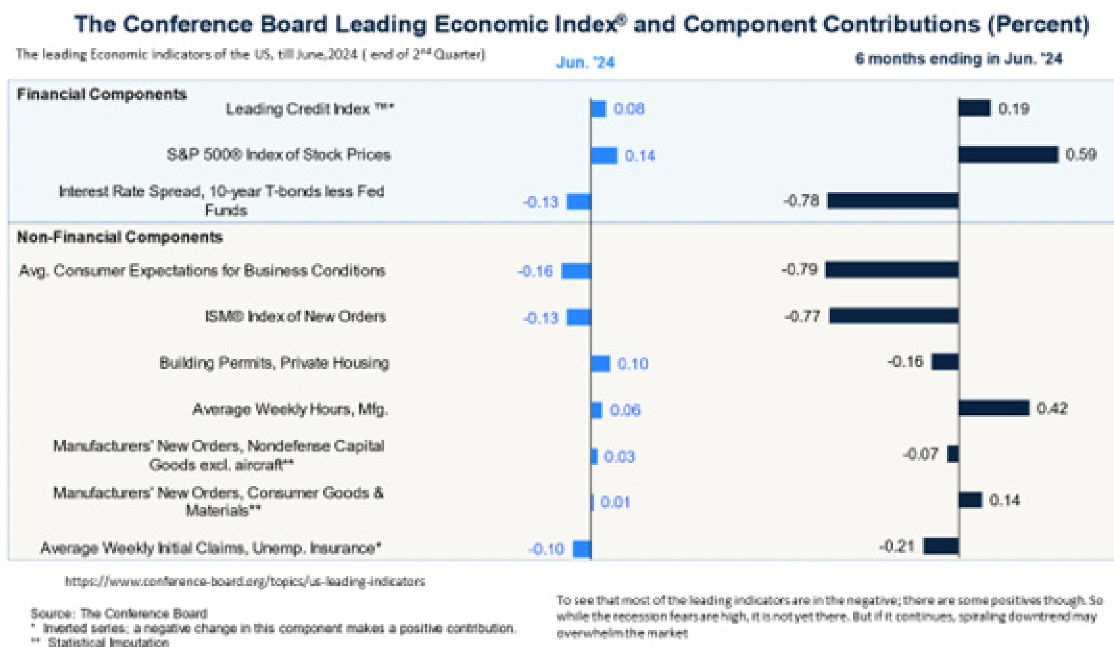

Figure 3. The majority of the LEI increase is much because of no alternative investment positions *vis-a- vis* US market but the growth is feeble and vulnerable.

foreshadowed a recession. The decline continued to be fueled by gloomy consumer expectations, weak new orders, negative interest rate spread, and an increased number of initial claims for unemployment (Figure 2 and Figure 3).

However, due to the smaller month-on-month rate of decline, the LEI's long-term growth has become less negative, pointing to a slow recovery. Taken together, June's data suggest that economic activity is likely to continue to lose momentum in the months ahead. "The current forecast is that cooling consumer spending will push US GDP growth down to around 1 percent (annualized) in Q3 of 2024."

4) Gross Domestic Product

A recession is a significant decline in economic activity that lasts for months or years. A common rule of thumb is that a recession is indicated by two consecutive quarters of negative Gross Domestic Product (GDP) growth. When GDP is falling, it means the economy is shrinking,

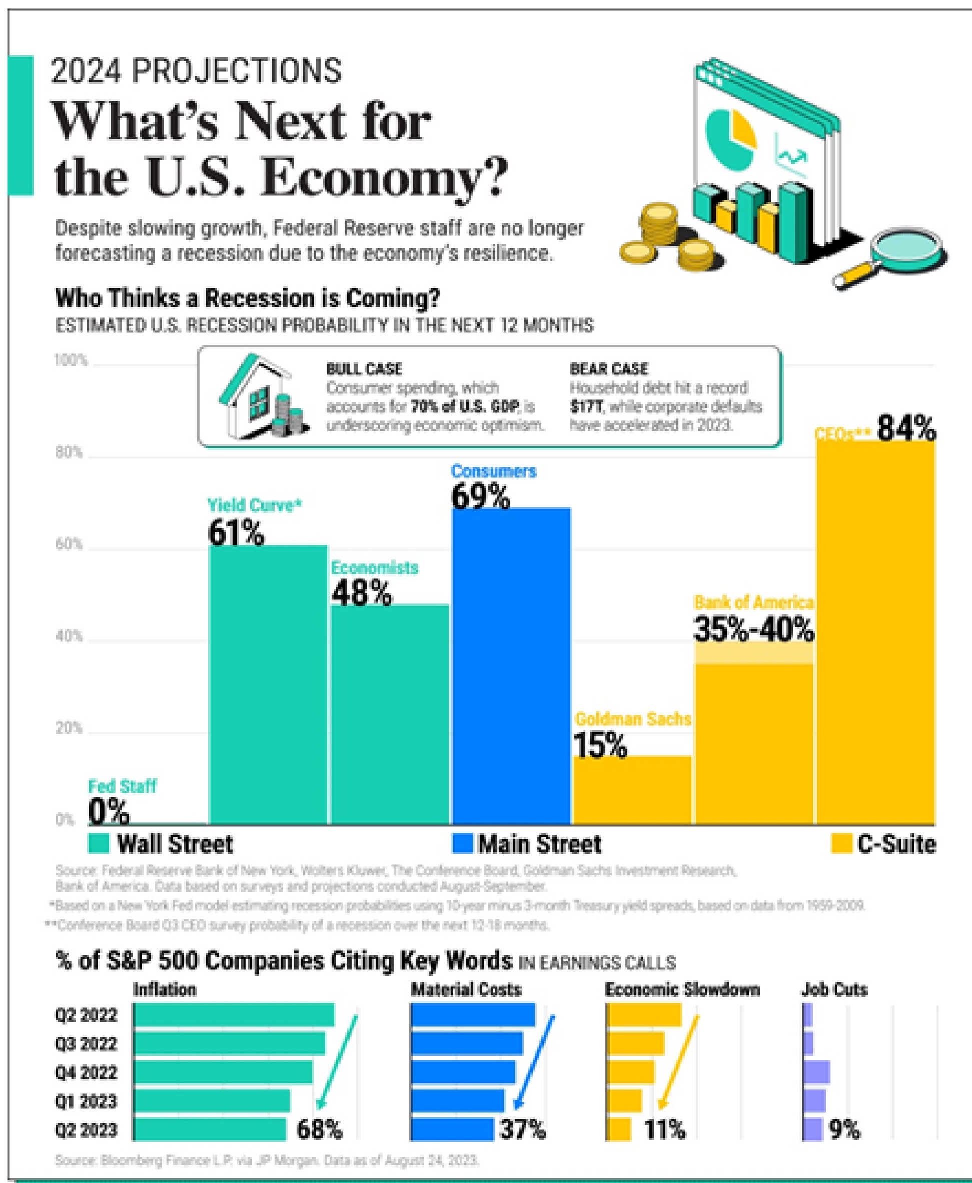

Figure 4. The US now has an 85% chance of recession in 2024, the highest probability since the Great Financial Crisis, says one economist Unemployment.

which can be bad news for businesses and workers. A decline in real GDP for two or more quarters can indicate a recession, and is often accompanied by other factors like rising unemployment and reduced production[2].

a. Recessions typically last about a year and often result in a significant output cost. In particular, a recession is usually associated with a decline of 2 percent in GDP. In the case of severe recessions, the typical output cost is close to 5 percent.
b. The fall in consumption is often small, but both industrial production and investment register much larger declines than that in GDP.
c. They typically overlap with drops in international trade as exports and, especially, imports fall sharply during periods of slowdown.

5) High Unemployment

High unemployment can be an indicator of an upcoming recession, as it can lead to lower consumer spending and income. Recessions are periods of low economic activity, which can cause unemployment to rise. During a recession, companies may lay off workers because demand for goods and services is lower, and they may also refrain from raising prices. This can lead to a rise in unemployment and a fall in inflation. The U.S. unemployment rate jumped to near a three-year high of 4.3% in July amid a significant slowdown in hiring, heightening fears the labor market was deteriorating and potentially making the economy vulnerable to a recession. The increase in the unemployment rate from 4.1% in June marked the fourth straight monthly increase, the Labor Department reported on 7th August, 2024. Its rise from a

Figure 5. The US unemployment rate is stubbornly near constant.

five-decade low of 3.4% in April 2023 to now the highest level since September 2021[3].

6) Manufacturing

A decline in manufacturing jobs can be a sign of decreased consumer spending, which can lead to cuts in other sectors. Manufacturing is often affected by recessions because demand for products decreases and businesses cut back on production due to rising raw material costs. This can lead to a decrease in exports and overall economic activity. For example, during the Great Recession, manufacturing activity in the U.S. fell sharply, with employment in manufacturing declining by 10%.

A measure of U.S. manufacturing activity dropped to an eight-month low in July, 2024 amid a slump in new orders, but that likely exaggerates the industry's struggles as production at factories rebounded sharply in the second quarter .The Institute for Supply Management (ISM) said on 3rd August, 2024 that its manufacturing PMI dropped to 46.8 last month, the lowest reading since November, from 48.5 in June. A PMI reading below 50 indicates contraction in the manufacturing sector, which accounts for 10.3% of the economy[4,5].

(To be continued in Part-2)

In the US, the ISM survey's forward-looking new orders sub-index fell to 47.4 last month from 49.3 in June. Output continued to decline, with the production sub-index sliding to 45.9 from 48.5 in June. Despite subdued orders, manufacturers faced higher prices for inputs, likely reflecting soaring freight rates. The survey's measure of prices paid by manufacturers increased to 52.9 from 52.1 in June. Its measure of supplier deliveries rose to 52.6 from 49.8 in June. A reading above 50 indicates slower deliveries.

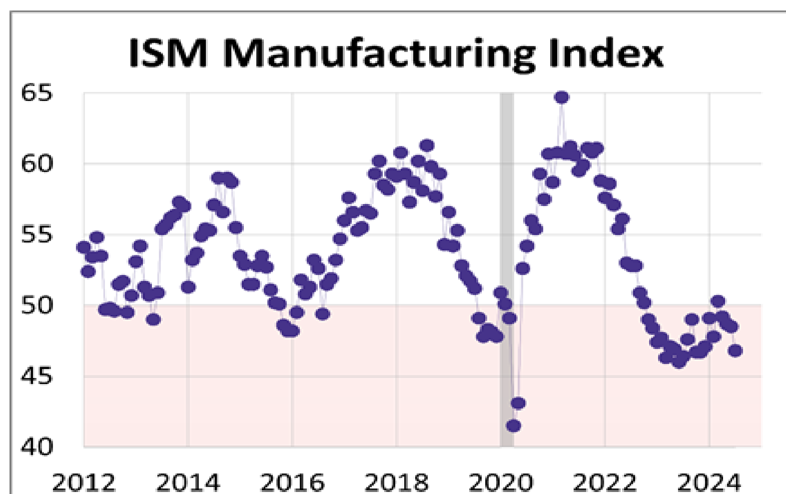

Figure 6. ISM US Manufacturing Index Drops to 8-Month Low.

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