

US Macroeconomics

January 30, 2023

Joseph Lavorgna, Chief US Economist | 212.610.1741 | joseph.lavorgna@smbcnikko-si.com

Unemployment Doesn't Walk, it Runs

Investors hoping for a soft landing cite the tight labor market — the unemployment rate is just 3.5% — as a reason to downplay recession risks. At the same time, the tight labor market worries some Fed policymakers that inflation will remain elevated because of rising wage demands. If so, the fed funds rate needs to move higher and stay there. No doubt the behavior of unemployment is central to the broader economic and financial outlook.

The chart below shows a long history of the unemployment rate along with recessions (denoted by the blue bars). One feature of the graph should immediately jump out. When the unemployment rate rises, it does so quickly and sharply from its cyclical low.

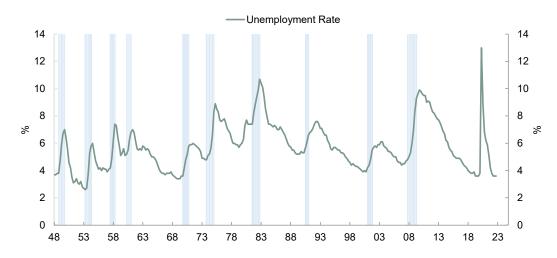
There have been 10 recessions in the post-war period excluding the 1980 and pandemic-recessions, which are not considered in our discussion because of their unique characteristics. While the unemployment rate is a leading indicator of economic downturns, the rate does not have to increase much to signal recession.

Over the last 10 business cycles, the average increase in the unemployment rate from its cyclical low to the peak in economic activity has been just 0.4%. In one instance, the trough in the unemployment rate coincided with the onset of recession. This happened in June 1981 when unemployment fell to 7.2%, and economic activity peaked in the following month with a steady unemployment rate.

Over the remaining nine business cycles, there were two episodes (1953 and 1969) when the unemployment rate increased only a tenth before onset of recession. Another time (in 1973) the rate increased just a couple of tenths ahead of recession. Then there were three instances when the rate rose 0.4% before recession (1948,1957,1960).

The last few recessions have experienced slightly larger increases before the peak in real GDP. The unemployment rate increased half of a point ahead of the 1990 and 2001 downturn, and there was a 0.6% increase ahead of the 2008-09 downturn.

With one exception, the unemployment rate rises before the economy peaks. But the initial increase is not particularly large at just 0.4% on average. This suggest to us that whenever the next downturn begins, most people will not notice until it's too late.



Source: BLS, NBER, Haver, SMBC Nikko



Disclaimer

This presentation is for discussion purposes only and is not intended to be an offer to sell or the solicitation of an offer to buy any securities, or any commitment to underwrite, subscribe for or place any securities, is not an offer or commitment to provide any financing or extension of credit or service, and does not contain any tax or legal advice. This presentation has been prepared by SMBC Group (which may include, collectively or individually, any of the following entities in the Americas Division: Sumitomo Mitsui Banking Corporation ("SMBC"), SMBC Nikko Securities America, Inc. ("SMBC Nikko"), SMBC Nikko Securities Canada, Ltd. ("Nikko Canada"), SMBC Capital Markets, Inc. ("SMBC-CM"), SMBC Leasing and Finance, Inc., JRI America, Inc., and SMBC Rail Services LLC) and is being furnished by SMBC Group solely for use by the client or potential client to whom such materials are directly addressed and delivered. This presentation is confidential and is the property of SMBC Group subject to copyright. Any reproduction of this presentation, in whole or in part, is prohibited, and you may not release these materials to any person, except to your advisors and professionals to assist you in evaluating these materials, provided that they are obligated, by law or agreement, to keep the presentation confidential. These materials do not constitute research, a recommendation or an offer or solicitation to any person to enter into any transaction or adopt any hedging, trading, or investment strategy. Prior to participating in any such transaction, you should consult your own independent, competent, legal, tax, accounting, and other professional advisors.

In preparing this presentation, SMBC Group has relied upon information available from third parties, including public sources, and we have assumed, without independent verification, the accuracy and completeness of such information. Specific prices, indices, or measures, including ranges, listed in this document were prepared at the time the document was prepared, and are subject to change without notice. SMBC Group makes no representations to and does not warrant this presentation's accuracy or completeness. SMBC Group expressly disclaims any liability for any use of the information set forth herein, including, without limitation, any use of the information set forth herein in the preparation of financial statements or accounting material.

These materials may contain forward-looking statements, which may include projections, forecasts, income estimates, yield or return, future performance targets or similar analysis. These forward-looking statements are based upon certain assumptions. All forward-looking statements are based upon currently available information and SMBC Group is not obligated to provide an update. Actual events may differ from those assumptions. Opinions, projections, price/yield information and estimates are subject to change without notice. There can be no assurance that estimated returns or projections will be realized, that forward-looking statements will materialize or that actual results will not be materially lower than those presented. Past performance is not necessarily indicative of future results. Any transactions or strategies addressed may not be suitable for all parties. The value, price or income from transactions or strategies may fall as well as rise. SMBC Group or an affiliate may have a position in any of the underlying instruments, assets, indices, or rates mentioned in this document. You should make your own independent judgment or seek independent financial and tax advice with respect to any matter contained herein.

SMBC is subject to Japanese firewall regulations and therefore absent client consent, non-public client information may not be shared with SMBC Nikko Securities Inc.

SMBC Nikko is a U.S. registered broker-dealer of SMBC Group. Nikko Canada is a U.S. and Canadian registered broker-dealer of SMBC Group. SMBC-CM is provisionally registered as a U.S. swap dealer with the CFTC. Capital markets and other investment banking activities for SMBC Group are performed by a combination of SMBC Nikko, Nikko Canada, SMBC Nikko Securities Inc. and SMBC-CM. Lending and other commercial banking activities are performed by SMBC and its banking affiliates. Derivative activities may be performed by SMBC-CM or SMBC. SMBC Group deal team members may also be employees of any of the foregoing entities. SMBC Group does not provide tax advice. Accordingly, any discussion of U.S. tax matters contained herein (including any attachments) is not intended or written to be used, and cannot be used, in connection with the promotion, marketing or recommendation by anyone unaffiliated with SMBC Group or for the purpose of avoiding U.S. tax-related penalties. © 2022 SMBC Group. All rights reserved.