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Six Reasons Why I am Forecasting a Recession for 2020

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IT'S TIME TO COMMIT

You are probably long tired of my shrill series of recession warnings as this recovery has matured. I've had that viewpoint due to the extraordinary length of this recovery and the continued uncertainty of global markets. We now know that a combination of unprecedented governmental stimulus and the relatively modest growth of this recovery have created the longest recovery since the U.S. government began keeping statistics in the first half of the nineteenth century. Nonetheless, I am changing my ***warning*** to a ***forecast*** because a sufficient number of indicators have turned negative creating an economy consistent with a pre-recessionary economy. If it looks like a duck, walks like a duck, and quacks like a duck – I will call it a duck. That's not to say we are ***in a recession*** as many trucking commentators are saying, nor is a recession certain. The politicians are still bragging about having created a booming economy, and consumer-oriented stats are still often strong (like the retail sales numbers released this week). Still, the six issues addressed below have pushed recession from merely a possibility to the most likely outcome.

THE SIX ISSUES

1. The classically cyclical sectors of the economy are headed south.

2019 was a surprisingly strong year for manufacturing and investment – two of the strongest cyclical sectors of the economy. By cyclical, I mean such spending is characterized by the typical overbuys then underbuys of the classic business cycle. It's these ups and downs in spending that create the business cycle and why it's called the business cycle. Look at the bars representing 2019.2 for those cyclical sectors: manufacturing and investment. Both are going negative. If all the sectors were negative, or close to, we would be in recession. Not so – we are in conditions consistent with the approach of recession.

2. But transport is 'in recession' – or close to it!

This is another condition consistent with the approach of recession. Transport growth, including that of trucking, usually goes flat or slightly negative the year before recession. Look at the bars at the far right of the graph. Truckload growth has been very low in both quarters of 2019. Is trucking a leading indicator, then? Not technically. It is a coincident indicator to things like manufacturing and investment – things that do tend to go slow ***before*** recession. So, it is safe to say that trucking is either in or very close to recession – particularly the spot market.

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3. **Beware of a negative yield curve!**

   Economists worried about recession keep close tabs on the relationship between long- and short-term interest rates. Usually, long rates are higher than short rates because the risk in lending money for a long time is higher than lending it for a short time. When short rates are higher than long rates, the relationship is called a negative yield curve. Since World War II, every time we've had a negative yield curve, recession has followed. We currently have a negative yield curve.

4. **Will we import recession?**

   The U.S. easily has the strongest current economy among the major economic powers. China is growing more slowly than usual, much of Europe is at or near recession, and there are multiple problems in South America and among less developed economies. Such conditions are probably a stronger reason for the drops in American exports than the President's saber-rattling. Moreover, American decisionmakers are often part of multinational companies. As such, they are already concerned about economic growth and will be cautious with American investment.

5. **My classmate is a risk taker.**

   My college classmate in the White House is a born risker taker who is encouraged in that behavior by his political base. He is but one important element in a global political environment that is increasingly risky: the Chinese are dealing with unrest in Hong Kong, and don't forget about Brexit. International markets are already spooked by those risks. A round of incidents could easily send markets into tailspins. That is particularly true with the oil economies of the Middle East.

6. **Brave economists?**

   As made clear in an extensive collection of jokes, economists are hard to pin down. I have been warning of recession for quite some time but leery of saying exactly when it would happen. "Is next year the year, Noël?" "Maybe!" I cite this issue because last week I attended a meeting of 25 very well-known economists. I am not allowed to reveal specific quotes or a tally. Suffice it to say that the mood of the people was decidedly pessimistic. When that many economists agree on anything, I take notice.

ARE YOU SURE ABOUT THIS RECESSION?

I have been putting the probability of recession at between 30-40%, making the chance of something so important large enough to seriously consider, but not strong enough to plug in as one's base planning case. This is what has changed: I see the chance of recession above 50%; I say 60% for now. That makes it the base case. Will I be wrong again on this topic? Here's the point: you can't afford to ignore this threat.

HOW COME?

Well, if you are in the spot market, it means that what you're suffering through right now, the spot freight recession of 2019 will continue for another two years—and get worse in the process. Prices that are already down 14% from 2018 will fall another 5% or so in 2020. Throw in a 5% drop in loads, and you get a 9 or 10% decline in revenue in 2020; that is for the carriers. Historically, brokers suffer a bit less – perhaps by 20% less. On the contract side, the contraction is less (as usual), down 1.1% on loads, 1.2% on price, and 3% on revenue.

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THERE IS SOME GOOD NEWS

Because we have no bubble bursting and the recovery was relatively weak, this should be a mild recession. It should be very much like the 2001 event when volumes and prices reacted about the same as I am forecasting now. That compares VERY favorably with the 2008-2009 event, also known as the worst recession since the Great Depression of 1930. Between 2008 and 2009, volumes dropped almost 15%, not regaining 2007 levels until 2014.

COULD IT BE WORSE?

There is little on the domestic side to suggest that. I know a housing economist who pointed out that there has been a minimal recovery of housing starts during this recovery: no overbuy, thus no underbuy is needed to make up. The downside risks are all on the global side. Three are easy to see:

1. There are still major sovereign debt problems in Europe that could spark a global banking crisis.
2. The saber-rattling in the Persian Gulf; $200/barrel oil would be a real problem. That's what would happen if a U.S./Iran tiff shut off the Straits of Hormuz through which pass 25% of the world's oil.
3. The slowly simmering animosity with China. China represents the first large scale challenge to the United States' dominance of world trade since we assumed that position in 1946. There is always the slim but terrifying possibility of open warfare. More likely is a flexing of China's financial muscle. We have already seen some of that in their devaluing of their currency this month. More importantly, they hold more than enough U.S. sovereign debt to cause a major debt funding challenge for our treasury if they dumped that debt. Revisionist economists contend that we can fund big deficits indefinitely. That breathtakingly naïve idea is dependent on a friendly China.

HOW ABOUT INDIRECT EFFECTS – THINGS NOT HAVING TO DO WITH VOLUMES AND PRICES?

Here are four likely outcomes:

1. The coincidence of recession and a presidential election usually means a change in the party occupying the White House: it happened in 1980, 1992, and 2008. Donald Trump is vulnerable enough without having to explain how his programs are no longer creating jobs. Whatever you say about his other policies, he is anti-regulation. A democratic administration would have a different view. Such a view would mean more regulation for trucking.
2. We know that the tremendous retail revolution has pushed some very visible brands to the brink of disappearance. A recession will accelerate the already high failure rate. Some of YOUR customers will disappear.
3. Of course, tractor and trailer sales will tank, especially after the misplaced euphoria of 2018. That means 2020 will be a great time to buy assets.
4. Finally, the march towards adequate driver pay will take a step back. That's what happened in 2008-2009. Some reduction in pay or benefits will likely occur (not as much as in 2009). That will lower costs but make the adaptation to the next expansion more difficult.

AND IF THERE IS NO RECESSION?

After having another laugh at my expense, consider these two things. The first has ample historical precedent. As in 2001, when the total economy just skated by recessionary territory, the freight economy still had a couple of tough years. Just as 2001-2002 was a freight recession, so 2019-2020 will very likely be one too. I put the probability at 80% on that. The other insight piggybacks off the same historical precedent. The lack of a consumer underbuys in 2001 lead to a major expansion of consumer debt in the Oughts. As a result, the eventual correction was much bigger than a normal one – the Great Recession of 2008-2009. Just as many economists in the early Ought's talked about the end of the business cycle, many are repeating that claim now. It seems to me that human nature sustains overbuying behavior until forced by painful realities to retrench. The grasshoppers of the ancient fable eventually get their comeuppance. Technology may be changing, but human nature ain't!

ABOUT THE AUTHOR

Joining Truckstop.com in June of 2017, Noël Perry is the rare economistic to specialize in transportation. Starting on a loading dock in 1968, he has followed his life's interest in senior research positions at Cummins Engine, CSX and Schneider National. He has been in private practice since 2008, working with clients in four modes and the shipper community. He is frequently quoted in the national logistics media and heard on the speaking circuit.

Noël holds degrees from the University of Pennsylvania and Harvard University and navigated KC-135's during the Vietnam War. He and his wife Ginny live in the historic iron mining village of Cornwall, PA. In his spare time Noël is a gardener, singer, golfer, WWII historian and is a member of the Society for American Baseball Research.