

# ClearBridge

## Investments

## AOR Update: The Dominoes Are Falling

1 May 2023

### Key Takeaways

- ▶ The ClearBridge Recession Risk Dashboard saw three negative signal changes this month in Truck Shipments, Jobless Claims and Job Sentiment, pushing it deeper into red or recessionary territory and suggesting a significant downshift in the economy.
- ▶ As leading indicators of labor market health, a worsening of Job Sentiment and Jobless Claims suggests net job losses and a rising unemployment rate may emerge later in 2023. This, in turn, is likely to crimp consumption which is the backbone of U.S. economic growth.
- ▶ A sharp decline in truck freight volumes provides further evidence of an economic slowdown on top of supply chain normalisation, which appears to have largely played out.

### Stock Market Downplaying Macro Weakness, For Now

A better than feared start to earnings season coupled with lingering recession fears is causing a tug of war between the bulls and the bears. Consequently, U.S. equities were remarkably steady last month, with the S&P 500 Index trading in a narrow 2.5% range the entire month and closing up just 1.6%. Despite the rangebound market, April economic data was consistently weak, as evidenced by the US Citi Economic Surprise Index which declined from 57 to 22 during the month. Given this deterioration, it is unsurprising that the ClearBridge Recession Risk Dashboard saw three negative signal changes this month, with Truck Shipments and Jobless Claims worsening from green to yellow, and Job Sentiment worsening from yellow to red.

Exhibit 1: ClearBridge Recession Risk Dashboard

	Current	Deepening Red Signal			
	Apr. 30, 2023	Mar. 31, 2023	Dec. 31, 2022	Sept. 30, 2022	
Consumer	Housing Permits	✘	✘	●	●
	Job Sentiment	✘	●	●	↑
	Jobless Claims	●	↑	↑	↑
	Retail Sales	✘	✘	✘	✘
	Wage Growth	✘	✘	✘	✘
Business Activity	Commodities	✘	✘	✘	✘
	ISM New Orders	✘	✘	✘	✘
	Profit Margins	✘	✘	✘	●
	Truck Shipments	●	↑	↑	↑
Financial	Credit Spreads	✘	✘	✘	✘
	Money Supply	✘	✘	✘	✘
	Yield Curve	✘	✘	✘	●
<b>Overall Signal</b>	<b>✘</b>	<b>✘</b>	<b>✘</b>	<b>✘</b>	

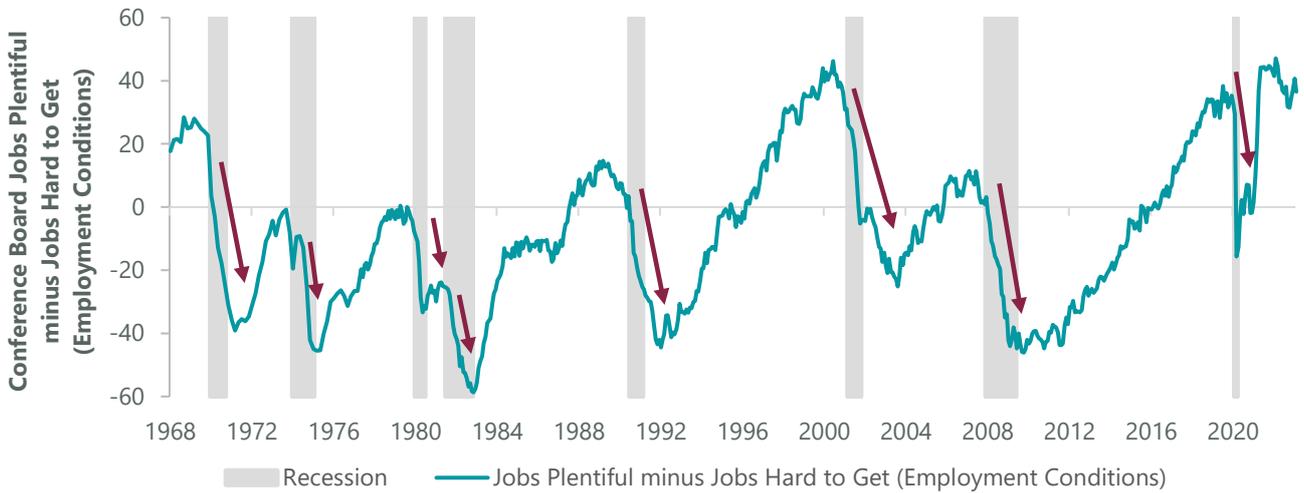
↑ Expansion      ● Caution      ✘ Recession

Source: ClearBridge Investments.

Two of these indicators – Job Sentiment and Jobless Claims – are leading indicators for the health of the labor market which has remained remarkably resilient. If history is a guide, net job losses and a rising unemployment rate should emerge later in 2023. Focusing first on Job Sentiment, individuals are reporting a

more challenging environment for finding work. The share of individuals responding that jobs are plentiful in the Conference Board Consumer Confidence Index® has fallen from 56.7% just over a year ago to 48.4% currently, while those responding that jobs are hard to get has risen but remains low. The difference between the two tends to presage slowdowns in consumption – individuals hold off on marginal purchases given less confidence in their ability to find work if needed – and has rolled over in recent months.

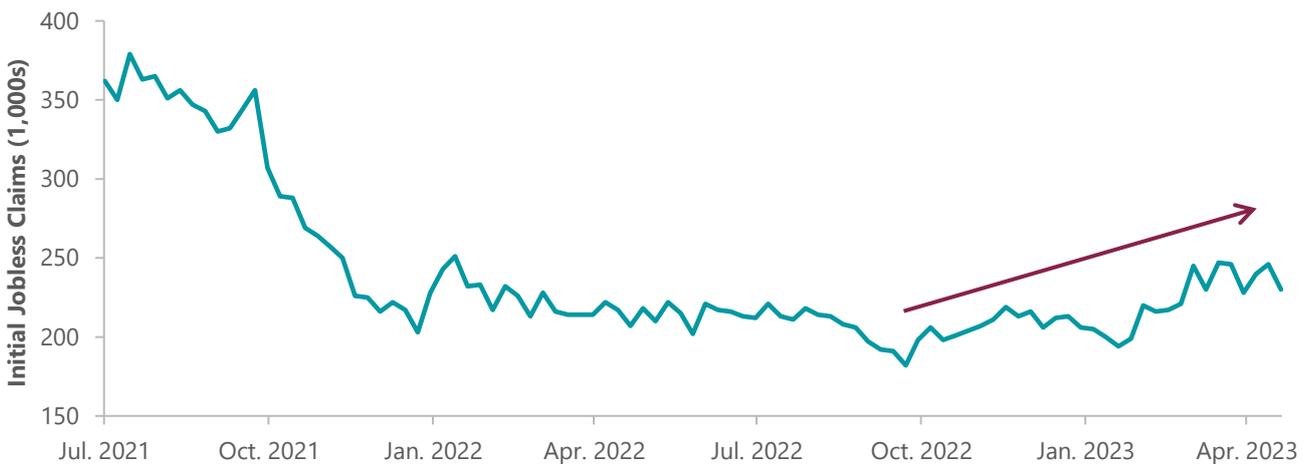
Exhibit 2: Job Sentiment Showing Fatigue



Data as of 31 March 2023, latest available as of 30 April 2023. Source: FactSet, Conference Board, National Bureau of Economic Research.

The second weakening labor market indicator is Jobless Claims, which has been drifting higher in 2023. In early April, the Bureau of Labor Statistics released updated seasonal adjustment factors for jobless claims that impacted the last several years. One impact of these changes was that jobless claims were stronger (lower) during the summer of 2022, but weaker (higher) in early 2023 than previously believed. Jobless claims have been choppy over the past two months – as is their nature and why we (and many) focus on their 4-week moving average – but have clearly risen into a higher range relative to what was seen in the second half of 2022. This step-up in claims is unsurprising as companies face margin pressure from reduced pricing power, coupled with stickier cost structures.

Exhibit 3: Jobless Claims a Canary in the Coalmine

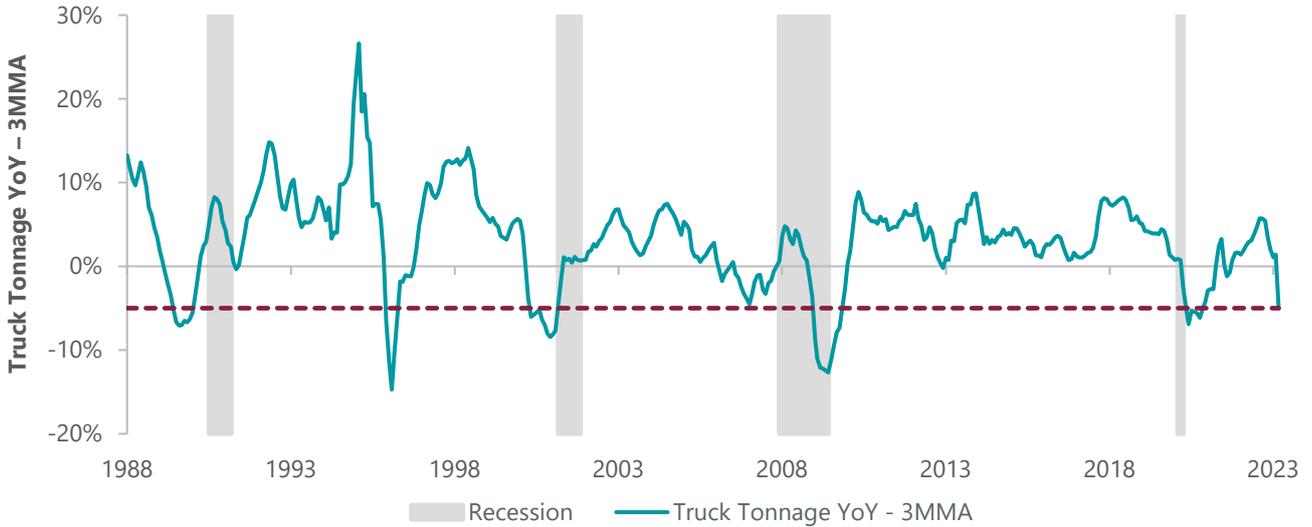


Data as of 21 April 2023. Source: Bloomberg, BLS.

The increase in the number of individuals filing for first-time unemployment benefits bodes poorly for future consumption, particularly given that high earners make up a disproportionately large share of the rise in those filing for benefits today, which is uncommon. This suggests that generous severance packages granted at termination may be running out. It similarly bodes poorly for future economic growth if these workers are unable to find new employment, a prospect that appears more challenging given deteriorating Job Sentiment.

The labor market is not the only area of the economy showing strain. Seventy-two percent of total freight moved each year goes on trucks, and the American Trucking Association’s Truck Tonnage Index saw one of its worst monthly declines on record in April going back to the early 1970s. Supply chain pressures appear to have normalised at this point with the New York Fed’s Global Supply Chain Pressure Index dropping to -1 standard deviation from +3 just over a year ago. This, in turn, is contributing to the decline in freight volumes as bottlenecks have eased, inventories have been restocked and less “stuff” is moving through the economy overall, portending a further slowdown in activity.

Exhibit 4: Truck Tonnage Hits the Brakes



Data as of 31 March 2023. Source: ATA, NBER, and Bloomberg.

Taken together, these three dashboard signal changes support the notion that the U.S. economy experienced a substantial downshift in economic activity in March and April. The dashboard now has 10 red and two yellow underlying signals, along with an overall deep red or recessionary reading. Our base-case view for the last 10 months has been that a recession was the most likely outcome, although the timeframe was always uncertain and never imminent. While we still do not believe a recession has yet started, we are less confident than we were just two months ago given the dominoes falling (dashboard signal changes) and think the onset of a recession is likely within the next few quarters. Given this assessment, we continue to believe tilts toward defensive and high-quality equities will be rewarded in the coming months.

## About the Authors



### Jeffrey Schulze, CFA

Director, Head of Economic and Market Strategy

- 18 years of investment industry experience
- Joined ClearBridge Investments in 2014
- BS in Finance from Rutgers University



### Josh Jamner, CFA

Vice President, Investment Strategy Analyst

- 14 years of investment industry experience
- Joined ClearBridge Investments in 2017
- BA in Government from Colby College

## ClearBridge Investments ClearBridgeInvestments.com.au

### Important Information

While the information contained in this document has been prepared with all reasonable care, ClearBridge Investments Limited (ABN 84 119 339 052, AFSL No. 307727) and its related companies ("ClearBridge") accept no responsibility or liability for any errors, omissions or misstatements however caused. Any views expressed in this material are given as of the date of publication and such views are subject to change at any time.

This information is not personal advice. It has been prepared without taking account of individual objectives, financial situations or needs. Where an investment product is mentioned, potential investors should seek independent advice as to the suitability of the product to their investment needs. Reference to shares in a particular company, is not a recommendation to buy, sell or hold that stock. Investors should be aware that past performance is not indicative of future performance.

This information may contain forecasts, including in regard to targets, expected returns, PE ratios and dividend yields. Any such statements are based upon research undertaken by the ClearBridge investment team. This research incorporates ClearBridge's reasonable assumptions and beliefs concerning future developments and their potential effect but are subject to risks and uncertainties that may be beyond ClearBridge's control. Returns can be volatile, reflecting rises and falls in the value of underlying investments. Accordingly, ClearBridge does not provide any assurance or guarantee that future developments will be aligned with ClearBridge's expectations, and actual results may differ materially from those expected by ClearBridge at the time of writing.

The distribution of this document may be restricted in your jurisdiction. This document does not constitute an offer or solicitation in any jurisdiction in which to make such an offer or solicitation would be unlawful. It is your responsibility to ensure that any such product, security, service or investment outlined is available in your jurisdiction.

Issued and approved outside Canada and the United States of America by ClearBridge Investments Limited ("CIL"), registered office Level 13, 35 Clarence Street, Sydney, NSW 2000, Australia (ABN 84 119 339 052; AFSL 307 727).

In Canada and the United States of America, issued and approved by ClearBridge Investments (North America) Pty Ltd ("CINA"), registered office Level 13, 35 Clarence Street, Sydney, NSW 2000, Australia (ACN 138 069 191). Neither CIL nor CINA are registered as a dealer in any province in Canada. CIL and CINA are not offering the securities of any investment fund that may be described in the materials in Canada or the United States. This material has not been approved or verified by the SEC, OSC or the Autorité des marchés financiers.

ClearBridge is wholly, indirectly owned by Franklin Resources, Inc., and part of ClearBridge Investments, LLC.