3 Reasons Wall Street Is Worried About a Recession

Description

Recession worries are rearing their heads once again. After a brutal Friday that saw the Dow shed 2.59% of its value, investors are fretting about the dreaded “R” word — and the date on which it will go from word to reality.

For several years, the majority of economists (about 71%) have predicted a recession no later than 2021. That year is fast approaching, so naturally, many investors and analysts are beginning to worry. The following are the three main reasons why their fears may be justified.

Inverted yield curves

An inverted yield curve occurs when the yields on long-term bonds drop below those on short-term bonds. This tends to indicate a lack of investor confidence in the future and has predicted nine out of the last 10 recessions. Just recently, the yield on 10-year U.S. government bonds fell below those on two-year bonds. This is a pronounced yield curve inversion that has “bear” written all over it.

An unprecedentedly long expansion

The most recent economic expansion in the U.S. has been unprecedentedly long, with 10 full years of uninterrupted GDP growth. Although the stock market has seen its downturns in these past years — notably, the late 2018 correction — the economy has been doing extremely well.

The problem is that the economy doing so well for so long indicates a recession is overdue. Economic downturns are to be expected every once in a while, and the fact that we haven’t seen one in so long suggests that we may be ripe for one. Nobody can tell when the next recession or slowdown will occur, but each year that passes without one defies the odds a little more than the last.

Global trade tensions at all-time highs

A final factor that has some worrying about a coming recession is the ongoing trade war. The U.S.-China trade war is a topic for its own article, but suffice it to say, it has been raging long and hard with no end in sight.

Trade tensions between the U.S. and China could easily catch Canada in the cross-hairs. For example, a slowdown in either country brought on by reduced trade could hurt Canadian exports. Another example would be one of the previously mentioned countries slapping tariffs on Canada in retaliation for it trading with the other.

Financial stocks could be hit hard

If a North American recession were to occur, then financials would be one of the sectors hit the hardest. In the 2007/2008 recession, many bank stocks fell 50% or more, and a repeat of that is not impossible.

Consider **Canadian Imperial Bank of Commerce**. In the first quarter of 2008, the company posted a net loss of $1.4 billion on losses from credit derivatives and declining interest income. Such earnings downturns are common for banks during recessions, as investments start to decline in value and borrowers begin defaulting. In the event of a new Canadian recession, CIBC would be hit particularly hard, since it's one of the most domestically focused Canadian banks. However, if a U.S. recession occurred and didn't spill over, CIBC would be less impacted than other banks, owing to its minimal U.S. operations.

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