

Yields Retreat as Recession Chatter Rises

The Atlanta Fed's GDPNow model has turned sharply lower in recent days, and is now showing a -2.1% second quarter reading. With the basic textbook definition of a recession being two consecutive quarters of negative growth and the first quarter GDP checking in at -1.6%, the reality of recession is starting to sink in. The majority of economists still don't expect a broad contraction within the next 12 months. The most recent forecast from *Bloomberg Analytics* puts the odds at 38%, but the incoming data is raising eyebrows.

Just three weeks ago, Fed officials laid out a very aggressive tightening path which included another 200 basis points of hikes between now and year end. But since then, a majority of economic releases seem to be signaling significantly slower growth and some moderation in price pressure. Last Friday, the ISM factory survey indicated U.S. purchasing managers' outlook had dimmed in June. Although still signaling expansion (any index number above 50), the overall manufacturing index slipped from 56.1 to 53.0, *the lowest reading in two years*.

There were several key sub-indexes in contraction territory including the new orders index, which fell from 55.1 to 49.2, and the employment index, which dropped from 49.6 to 47.3. In all fairness, the weak factory employment outlook has more to do with difficulty finding workers than diminished intent to hire, and the softening in new orders is related to the huge backlog of previous orders that weren't being filled.

There was some good news buried in the survey. The current production index crept up from 54.2 to 54.9, and the orders backlog index was whittled down from 58.7 to 53.2. At the same time, the supplier delivery index plunged from 65.7 to 57.3 as some purchasing managers pointed to an easing of supply chain delays.

The prices paid index fell from 82.2 to 78.5, still extremely elevated but moving lower. Any decrease in inflation at this point is welcome. On a related note, AAA reported the nationwide average for a gallon of gasoline was \$4.80 this morning, down from a record peak of \$5.02 three weeks ago.

Although just a survey, the ISM index has historically mirrored the broad economy. When the headline composite index drops to a two-year low, it adds to the narrative that recession is on the horizon and begs the question – *does the Fed really need to double the overnight funds rate over the next six months?* The market isn't so sure anymore.

In just over a week, the 10-year Treasury note yield has dropped from 3.20% to 2.83%, while the two-year has shed 30 bps and is now yielding 2.81%.

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Market Indications as of 10:12 A.M. Central Time

DOW	Down -704 to 30,393 (HIGH: 36,800)
NASDAQ	Down -123 to 11,005 (HIGH: 16,057)
S&P 500	Down -74 to 3,752 (HIGH: 4,797)
1-Yr T-bill	current yield 2.72%; opening yield 2.68%
2-Yr T-note	current yield 2.81%; opening yield 2.91%
3-Yr T-note	current yield 2.81%; opening yield 2.91%
5-Yr T-note	current yield 2.81%; opening yield 2.91%
10-Yr T-note	current yield 2.82%; opening yield 2.93%
30-Yr T-bond	current yield 3.06%; opening yield 3.15%

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