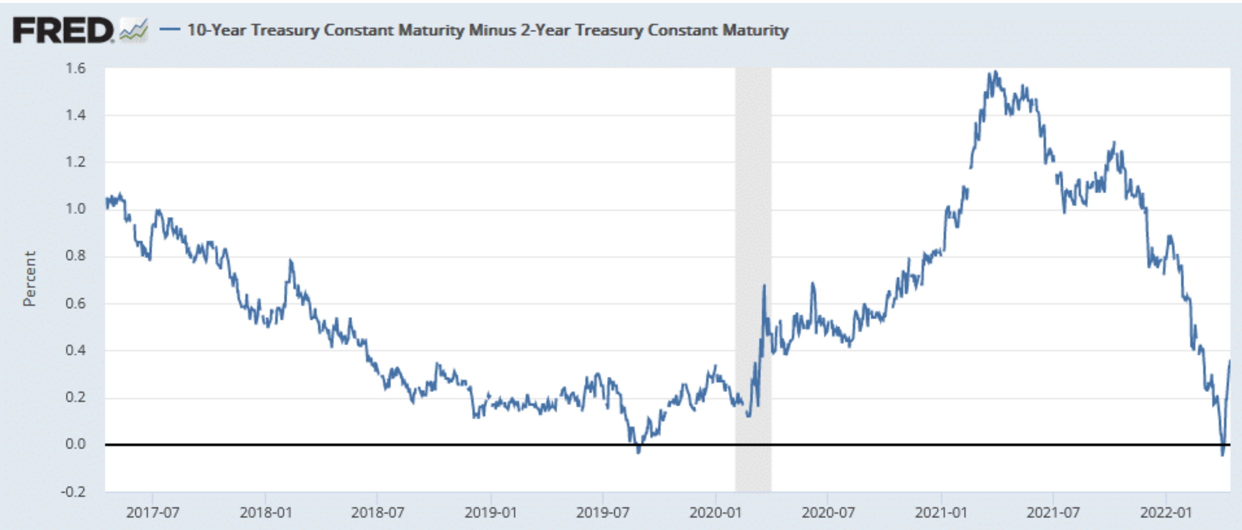
Uninverted Yield Curve- Are We Out Of The Woods?

Many economists have warned that an inverted yield curve will lead to a recession. The same characters are changing their tune. They now tell us not to worry because the yield curve has become uninverted. They are now selling us on a *"soft landing."* The graph below shows the yield curve inverted briefly in August 2019 before uninverting and leading to recession.

Similarly, the yield curve inverted in late March 2022 and quickly uninverted. In just two weeks, the curve went from a 5bps inversion to being uninverted by 38bps. While the sharp steepening elicits hopes of a soft landing, the reality is that yield curve inversions are not the signal of a pending recession. It is the steepening yield curve from inversion to an uninverted state that is the more timely warning of a pending recession. Either this time is different, or a recession is approaching.



What To Watch Today

Economy

- 8:30 a.m. ET: **Housing starts**, March (1.740 million expected, 1.769 million in February)
- 8:30 a.m. ET: **Housing starts, month-over-month**, March (-1.6% expected, 6.8% in February)
- 8:30 a.m. ET: **Building permits**, March (1.820 million expected, 1.859 million in February, upwardly revised to 1.865 million)
- 8:30 a.m. ET: **Building permits, month-over-month**, March (-2.4% expected, -1.9% in February)

Earnings

Pre-market

- **Fifth Third Bancorp.**&#2013266080;(FITB) to report adjusted earnings of $0.70 on revenue of $1.94 billion
- **Johnson & Johnson**&#2013266080;(JNJ) to report adjusted earnings of $2.60 on revenue of $23.68 billion
- **Citizens Financial Group**&#2013266080;(CFG) to report adjusted earnings of $0.92 on revenue of $1.63 billion
- **Halliburton**&#2013266080;(HAL) to report adjusted earnings of $0.35 on revenue of $4.20 billion
- **Truist Financial Corp.**&#2013266080;(TFC) to report adjusted earnings of $1.02 on revenue of $5.46 billion
- **Hasbro**&#2013266080;(HAS) to report adjusted earnings of $0.64 on revenue of $1.15 billion
- **Lockheed Martin**&#2013266080;(LMT) to report adjusted earnings of $6.21 on revenue of $15.55 billion

Post-market

- **Netflix**&#2013266080;(NFLX) to report adjusted earnings of $2.91 on revenue of $7.95 billion
- **IBM**&#2013266080;(IBM) to report adjusted earnings of $1.41 on revenue of $13.81 billion
- **First Horizon Corp.**&#2013266080;(FHN) to report adjusted earnings of $0.35 on revenue of $705.69 million

Market Trading Update

The last of the tax day selling occurred Monday as a lot of retail traders got their tax bills and realized they had to sell stuff to pay the tab from the last year. With the markets still flirting with support, oversold, and with sentiment very negative, we still expect to see a bounce starting as soon as tomorrow.

A rally back to the previous recent peak would not be out of the question and could happen fairly quickly given the underweighting of investors with respect to equity exposure.

More On The Uninverting Of The Yield Curve

The quad-panel chart below shows the 4-previous periods where 50% of 10-different yield curves are inverted. I have drawn a horizontal red dashed line from the first point where 50% of the 10-yield curves tracked became inverted. I have also denoted the point you should have sold and the subsequent low. You will note there are previous periods historically where the yield curve inverted, uninverted, and then inverted again.

inverted yield curve, Inverted Yield Curve History Should Worry Bulls

In every case, the market did rally a bit after the initial reversion. However, had you reduced your equity-related risk, not only did you bypass a lot of market volatility *(which would have led to investor mistakes)* but ended up better off than those trying to *?ride it out.?*

In 2019, the yield curve inverted again leading to a 35% correction and recession in 2020.

That?s just history

Currently, only 10% of the 10-spreads we track are inverted. **As such, there is no reason to become overly defensive just yet. But you should be at least paying attention.**

inverted yield curve, Inverted Yield Curve History Should Worry Bulls

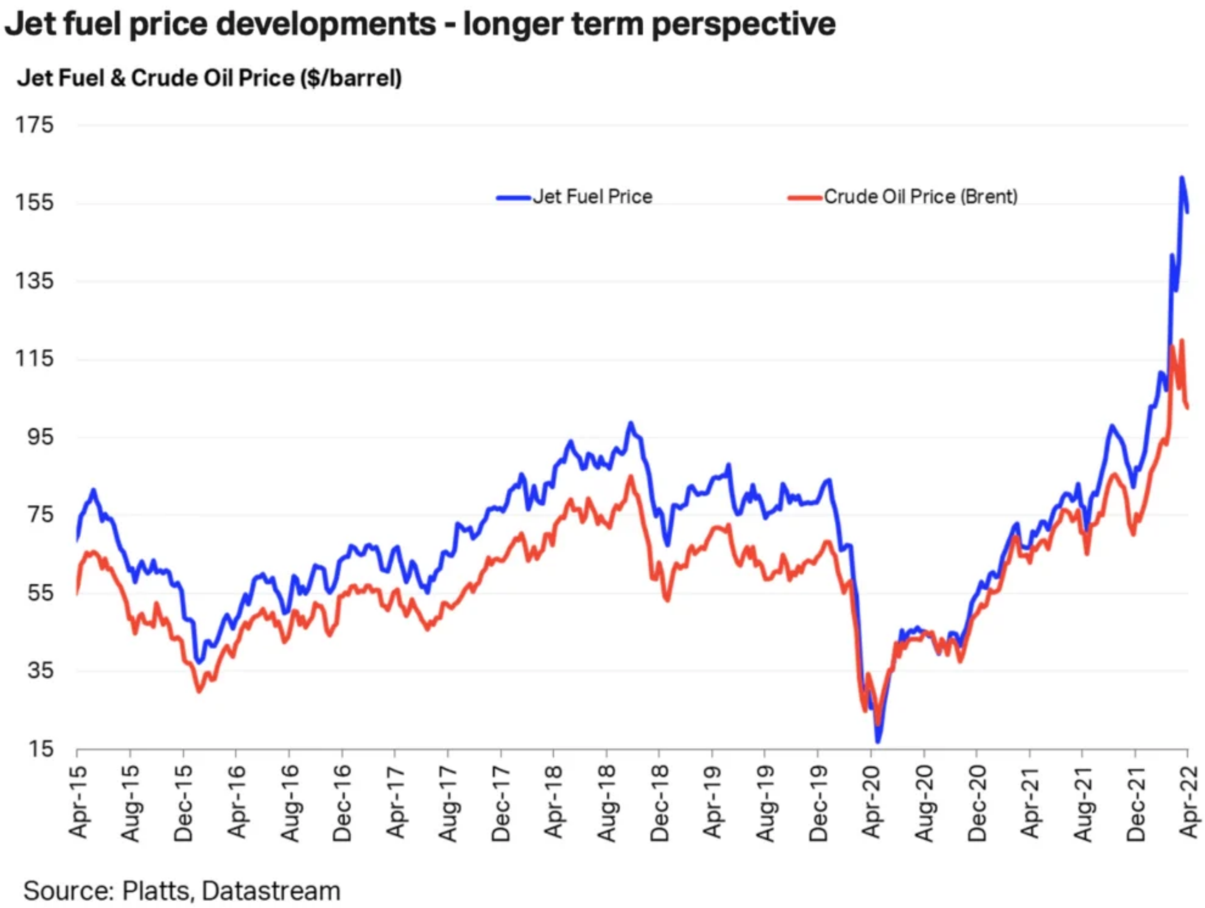
While the media is already rife with headlines about ignoring the inverted yield curve warning, history suggests it is unwise. **As the Fed hikes rates, more curves will invert.**

More importantly, with economic growth slowing rapidly, inflation running at the highest levels since 1980, and consumers tapped, recession risk is likely higher than analysts realize.

While using the *?yield curve?* as a *?market timing?* tool is unwise, it is just as foolish to dismiss the message entirely.

Airline Stocks Flying Against Stiff Headwinds

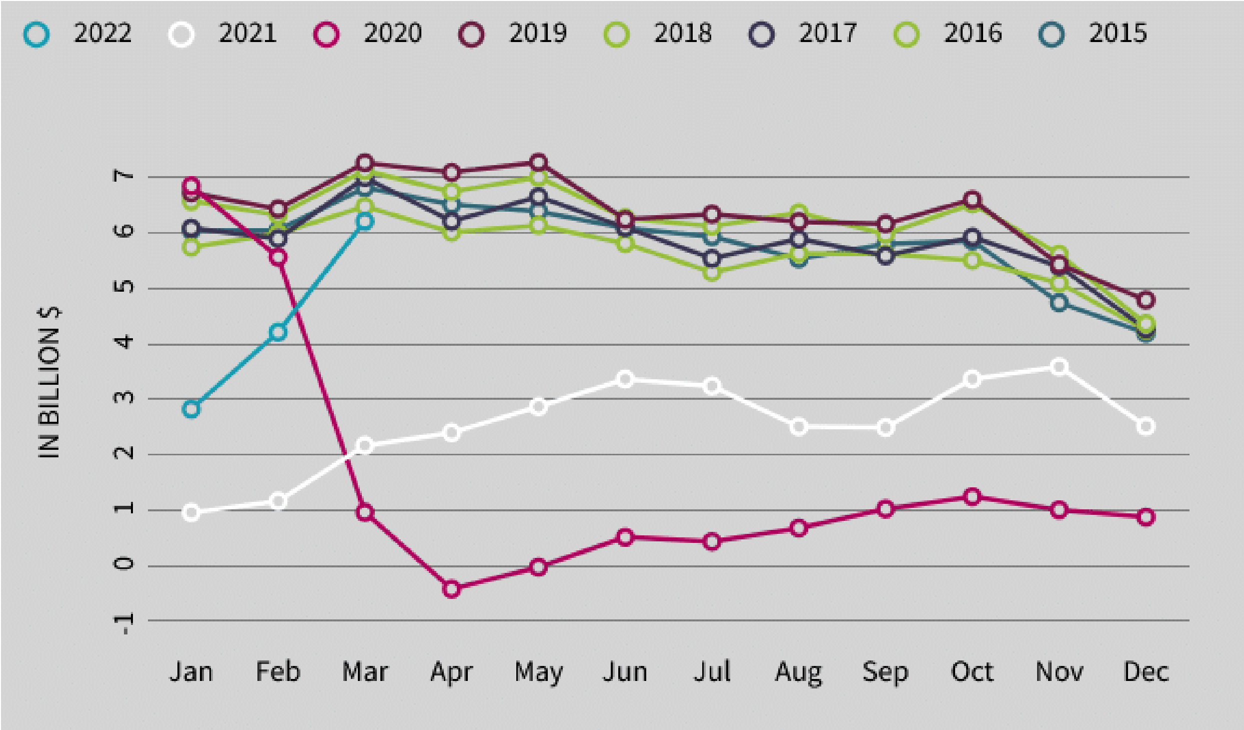
The graph below, courtesy of [Banking on the Market,] shows that the jet fuel price has risen significantly more than crude oil. Author Ayesha Tariq notes that jet fuel comprises about 20-30% of operating costs for many airlines. Further, most airlines do not hedge their fuel costs.



Soaring fuel prices will likely take a bite out of profits in the future, but Tariq also warns:

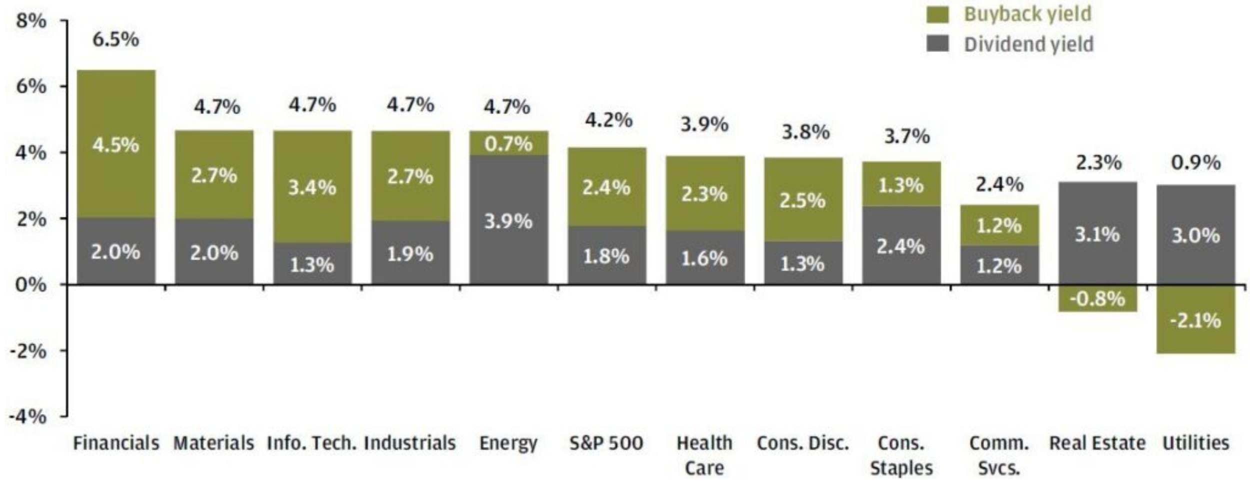
> "*And then there?s the cost of labor - the second biggest chunk of operating costs. We?ve been hearing about labor shortages for three* quarters now, *and the result has been* ***wage increases****. Finally, most of the airlines are structurally weaker. Airlines are notorious for never having enough cash and when the pandemic hit, most of them decided to drawn down on their standby credit lines, which tend be based off of floating rates. With* ***rates rising****, this is sure to hit their bottom line.*"

She notes that ticket sales are improving but bookings for premium seating and international travel, which are more profitable, are lagging. The following graph shows that total fares are now only $1billion away from pre-pandemic levels. Lastly, the third graph charts the ETF JETS, which holds the major airline stocks. As we show, it is still about 30% below pre-pandemic prices as investors seem to be cautious of the pitfalls noted above.



Utilities Are Lacking Dividends

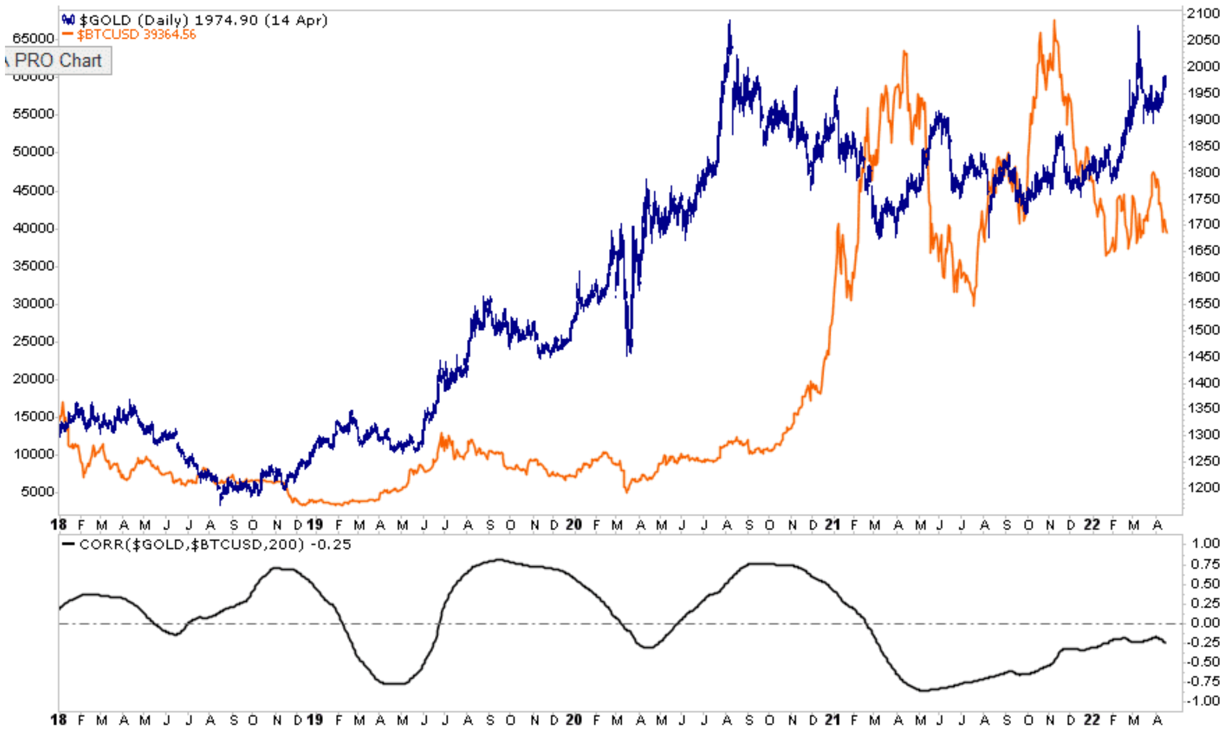
Investors are flocking to the utility sector for safety and higher dividends. The graph below shows that utilities have the third-highest dividend yield at 3%. However, the sector's total yield, including its buyback yield, ranks it at the bottom of the S&P 500 sectors. Utilities are actually net issuers of stocks along with REITS. All of the other sectors reduce shares in aggregate due to buybacks. Some dividend buyers may want to question their logic.



Gold or Bitcoin

War and inflation, what could be better for gold and bitcoin? It is widely believed that gold and bitcoin help preserve wealth in periods of war and or inflation. The graph below shows that narrative may not reflect reality. Since February 2021, when inflation started spiking, gold has risen about 25%. Over the same period, bitcoin is relatively flat. Similarly, since the Russian invasion of Ukraine, gold is about 10% higher while bitcoin is again flat.

Bitcoin surged with other risk assets in late 2020 and early 2021. However, when inflation became more pronounced, bitcoin fell. At that same time, gold started its ascent higher. The smaller graph below the prices shows that it was at that exact point when the correlation between gold and bitcoin was near negative 100%. Since then, the correlation has remained negative but much less so. Based on recent experience, bitcoin trades like the riskier segments of the stock market, while gold appears to trade as a function of real rates and geopolitics. To support the view on bitcoin trading like stocks, consider that the correlation between the NASDAQ (QQQ) and bitcoin has been 75% for the better part of the last year.



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