Flash Economics

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Could there be a recession in the United States in the future?

A recession can be triggered:

- by a significant tightening of monetary policy; but the Federal Reserve has become very cautious, the rise in short-term interest rates has remained well below that of inflation in recent inflationary episodes;
- by a financial or real estate crisis causing the prices of given financial assets or real estate to collapse; today, the valuation of equities is high, but not excessive; the types of mortgage loans (subprimes) that caused the 2008 crisis no longer exist;
- by a serious health or geopolitical crisis, which is always possible.

It therefore seems to us that a recession due to restrictive monetary policy or falling asset prices has become much less likely than in the past in the United States.

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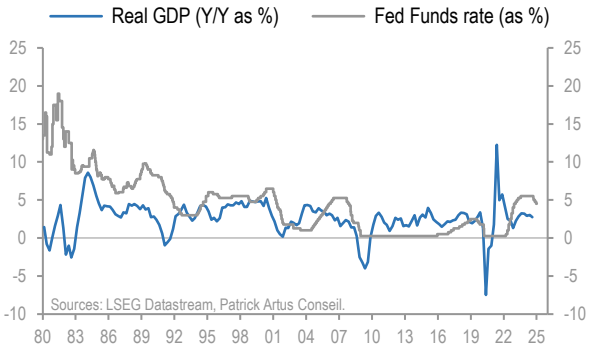
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What developments could trigger a recession?

If we look at **past recessions in the United States**, we see that they have **three possible causes**:

- a **significant tightening of monetary policy** (during the recessions of 1980-1982 and 1990, **Chart 1**);

Chart 1
United States: Real GDP and Fed Funds rate



- a **financial** (**2001-2002**) or **real estate** (**2008**) **crisis**, with a sharp drop in asset prices (real estate prices in 2007-2008, **Chart 2**) or equity prices (2001-2002, **Chart 3**), triggered by **excessive debt and rising interest rates**;

Chart 2
United States : residential real estate prices (1980.Q1 = 100)

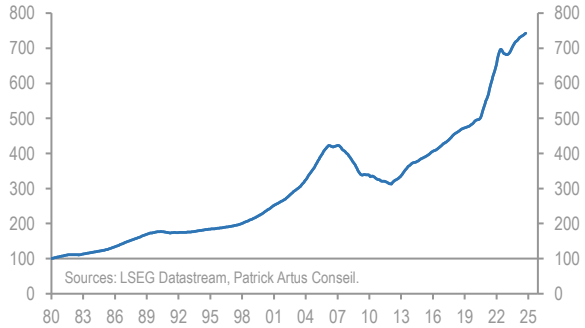
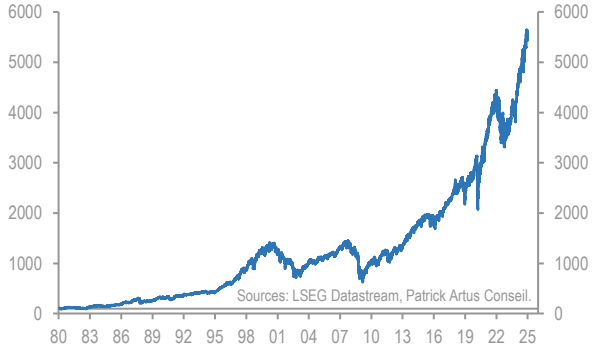
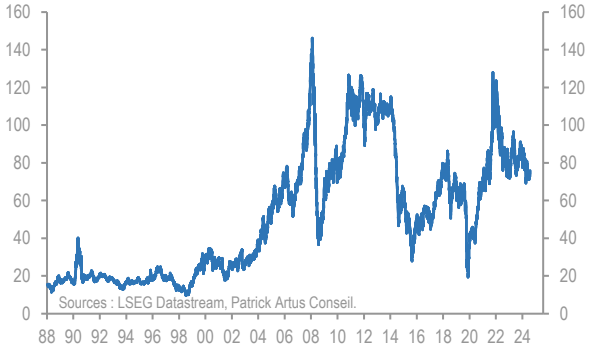


Chart 3
United States : S&P (01.01.1980 = 100)



- **a health crisis** (such as the Covid crisis in 2020) **or a geopolitical crisis** (leading, for example, to a sharp rise in the price of oil, as in 1980-1982 and 2007, **Chart 4**).

Chart 4
Oil price (Brent, $/bbl)

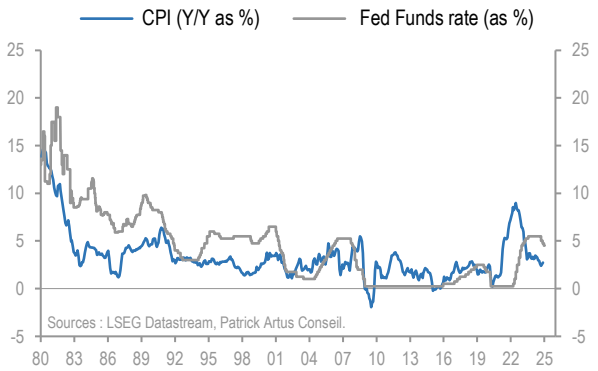


A crisis caused by a restrictive monetary policy, or a financial or real estate crisis, is highly unlikely today

1. **The Federal Reserve has become much more cautious and wants to avoid a violent downturn in activity due to excessive tightening of monetary policy**.

We can see that the highest level reached by the Fed Funds rate in the inflationary episode of 2021-2024 was 5.5%, while inflation reached 9% (**Chart 5**).

Chart 5
United States: Inflation and Fed Funds rate (as %)

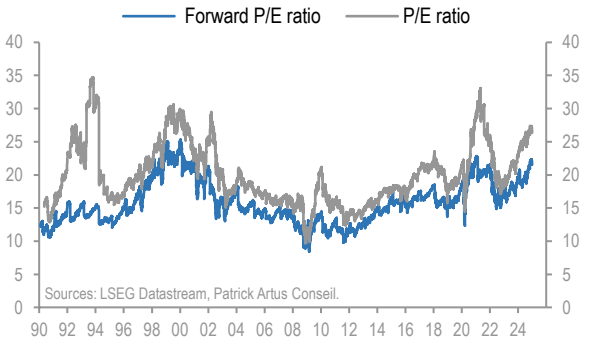


A recession due to a very restrictive monetary policy has therefore become highly unlikely.

2. **A financial crisis has also become highly unlikely.**

a. **Some investors are concerned about the current level of stock market valuations in the United States (Chart 6).**

Chart 6
S&P: P/E ratio and Forward P/E ratio

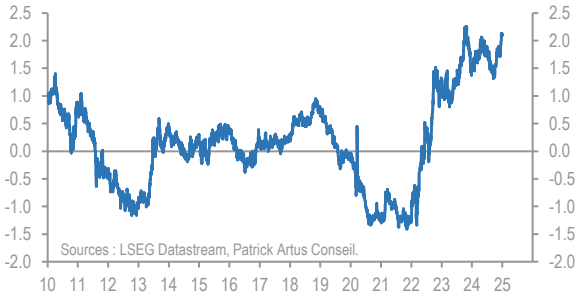


However, when we compare the P/E today and at the time of the dotcom bubble, we see that **stock market valuations are still lower today than they were during the dotcom bubble**. What's more, corporate profitability is strong (**Chart 7**) and long-term real interest rates are lower than potential volume growth (**Chart 8**).

Chart 7
Profits after tax and interest of non-financial corporations (as % of nominal GDP)



Chart 8
United States: Real interest rate on 10-year Treasuries (deflated by 10-year inflation-swap, as %)

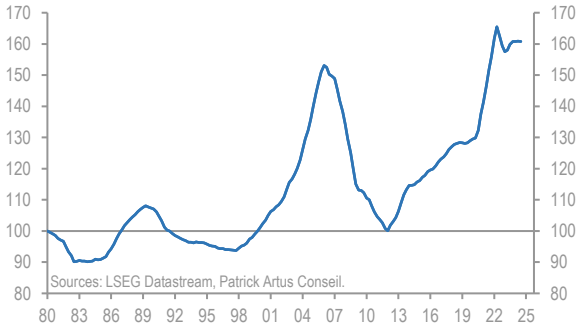


A sharp downward correction in US stock market indices is therefore unlikely.

b. Should we be concerned about the level of real estate prices?

Chart 9 shows **residential real estate prices in the US relative to the level of wages per capita**.

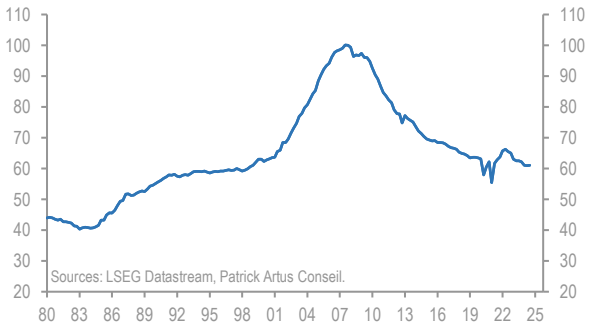
Chart 9
United States: Ratio between residential real estate prices and wage per worker (1980.Q1 = 100)



We observe that real estate prices have indeed been high since 2022.

Chart 10 shows the **rate of household mortgage indebtedness**, which is much lower than in 2007.

Chart 10
United States : Household's home mortgages (as % of disposable personal income)



Finally, since the 2008 crisis, securitisation of mortgages by private financial institutions (which accounted for just over 50% of total outstanding securitised mortgages) **has all but disappeared** (nowadays, only government agencies - Freddie Mac, Fannie Mae, Ginnie Mae - securitise mortgages).

All of which goes to show that **a financial crisis triggered by a drop in residential real estate prices has also become highly unlikely**.

Summary: only a health crisis or a serious geopolitical crisis could trigger a recession in the United States

In the United States today, we have indeed ruled out:

- a very restrictive monetary policy;
- the existence of significant stock market overvaluation;
- the risk of a sharp fall in real estate prices (particularly with the virtual disappearance of private securitisation of mortgages).

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