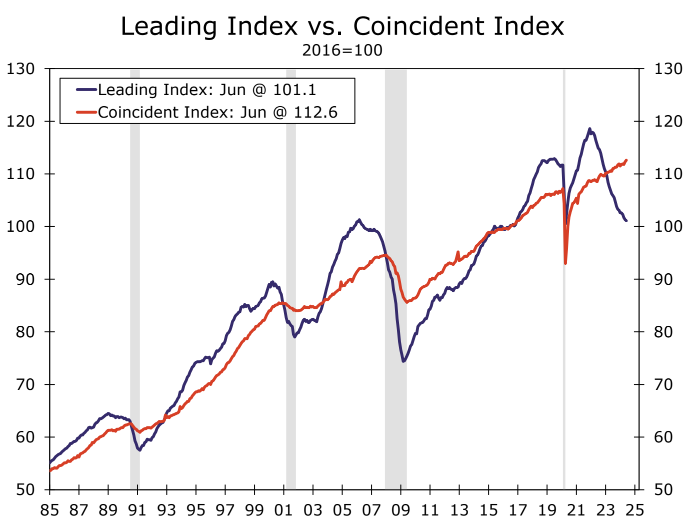
Economic Indicator — July 18, 2024

# Widening Gap Between Leading Indicators and Coincident Index


## Summary

Since the Leading Economic Index first slipped into negative territory in early 2022, economic growth has been steady and recession has been avoided. This is evident in the gap between the Leading Index and the Coincident Index. In fact, the spread has seldom been larger. We explore how in prior cycles that has marked a late-cycle turning point for the better.


Source: The Conference Board and Wells Fargo Economics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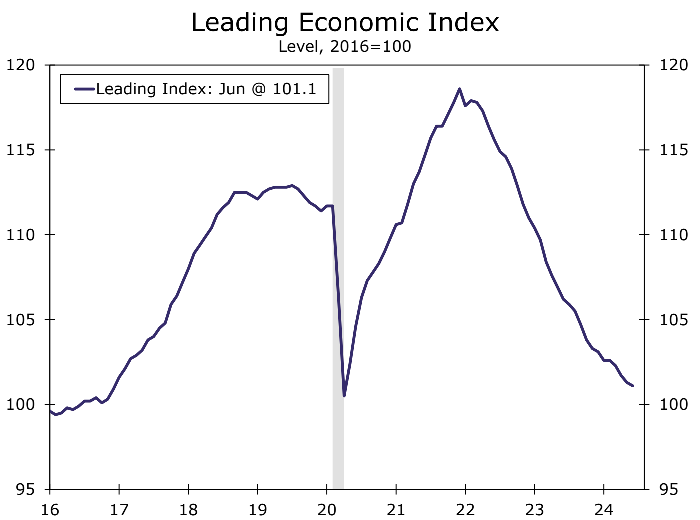
## Approaching the Cycle Low... Really?

The 0.2% decline in the Leading Economic Index is a slightly "less bad" outcome than what had been expected. This bellwether for the broader economy remains under pressure from depressed manufacturing orders, sour consumer sentiment and an uptick in initial claims for unemployment. At 101.1 in June, the LEI is only slightly above the reading of 100.5 it notched in May 2020 during its low point of the pandemic recession (chart). Is the outlook for the economy foretold by the LEI really as bad now as it was at its low point during the pandemic recession?

The spread between the Coincident Index and the Leading Index, a measure of how the economy is currently performing compared to how the LEI expects it to perform in the near future, is now sitting at 11.5, the widest it has been since 2008 (chart). While the LEI has been ever-declining over the past two and a half years, the Coincident Index, meanwhile, has been steadily climbing since it emerged from the pandemic recession. Wider spreads between the two measures indicate that the outlook for the economy is a larger degree more depressed than where it currently stands. Judging from prior cycles, when this gap is at its widest, the economy is often exiting recession and actually poised for decent growth. Note how that was the case in the early 1990s recession, the 2001 downturn and coming out of the recession caused by the financial crisis.



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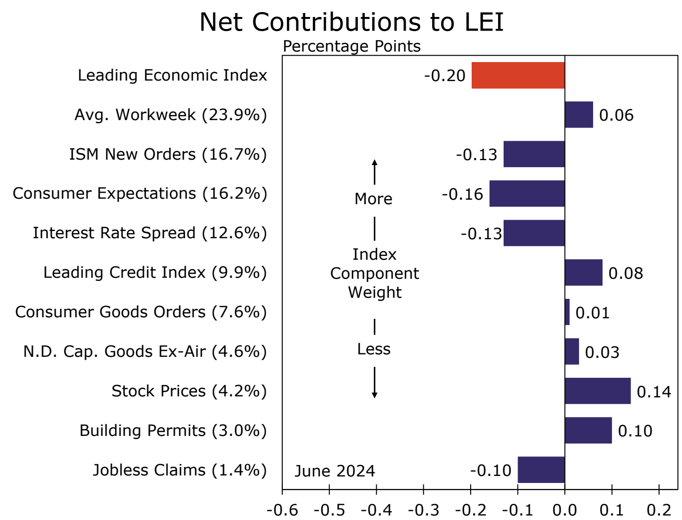

Source: The Conference Board and Wells Fargo Economics

## Negatives Outweighed the Positives

While the Leading Index plumbs closer to a cycle low, a factor that is offsetting the various drags is the still-buoyant stock market. In fact, stock prices were the largest positive contributor in June, adding a net contribution of 0.14 percentage points (chart). A rebound in residential construction activity also helped as building permits added a net contribution of 0.10 points to the headline.

Elsewhere, the index was bogged down by downbeat consumer expectations, ISM new orders that were still in contraction and the yield curve, all of which exerted drags on the headline. Initial weekly jobless claims also ticked up during the month. A rise in claims is a negative for the LEI and claims subtracted 0.10 percentage points this month. Other components turned a page from their negative contributions over the last two years, as consumer goods orders have now positively contributed to the index for five consecutive months. Similarly, the Leading Credit Index has positively contributed to the index in five out of six months year-to-date.

At present, the LEI is still an indicator that cried wolf. The index has continued to signal that a recession is on the horizon, even as the prospect for a soft landing has risen considerably and as inflation pressures gradually fade. The LEI is not alone in its warning, with the yield curve past its two-year anniversary of being inverted earlier this month. The widened gap between the LEI and the Coincident index offers hope that recession can be avoided altogether for the foreseeable future.

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