

US Macroeconomics

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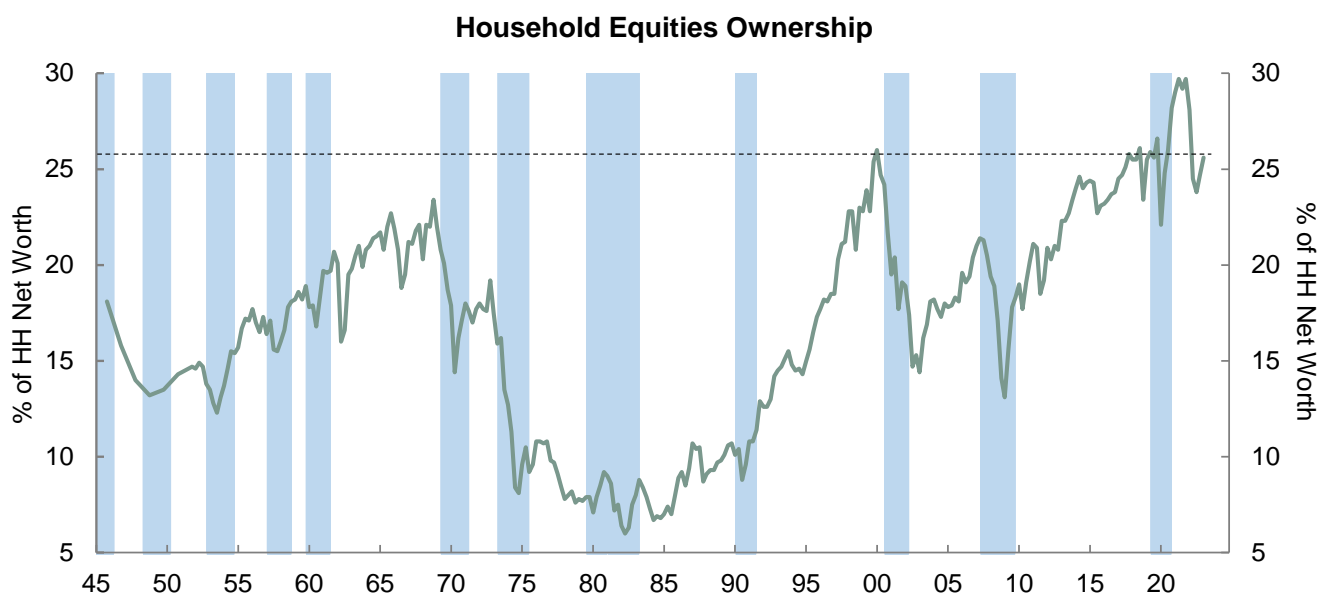
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Too Many Eggs in One Basket

Households appear unprepared for a potential correction in equities. Because investing is psychological, investors can become overextended in good times just to see conditions deteriorate and thus necessitate a deleveraging process.

This is important because, as shown below, **households' equities exposure is near the historical high point, with data going as far back as the 1940s.** Anticipating a quick economic bounce-back during the pandemic, households dramatically increased their equities exposure as a percentage of net worth from 22% in Q1 2020 to 30% in Q4 2021. This was a record, even topping tech bubble ebullience (26% in Q1 2000)! Only after an inflationary recession and galloping interest rates was exposure reduced to 26% in Q1 2023 — thus back to tech bubble levels. Historically, this is the 96th percentile, which seems imprudent given the present macro risks.

Households are particularly vulnerable not only because a recession could lead to substantial job and income losses, but also because a recession would lead to lower valuations, at a time when households are heavily invested at frothy valuations. As a result, **the hit to household wealth, and the associated wealth effects, could be particularly notable**, as every 1 dollar increase (decrease) in stock market wealth leads to more than 3 cents of increased (decreased) consumption. The risks of both lower valuations and increased unemployment are high considering that leading economic indicators are signaling recession, economic growth is low (or negative if looking at GDI), productivity is uninspiring, and interest rates are high (and rising) a factor restricting asset price growth.



Sources: Federal Reserve, NBER, Haver, SMBC Nikko

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