

By Thomas Wash

The business cycle has a major impact on financial markets; equity bear markets usually accompany recessions. The intention of this report is to keep our readers apprised of the potential for a recession, updated on a monthly basis. Although it isn't the final word on our views about recession, it is part of our process in signaling the potential for a downturn.

November 6, 2026

The US economy expanded further in September, largely driven by AI, though pockets of concern remain. Our proprietary *Confluence Diffusion Index* slipped back into contraction territory after a brief, one-month stint above the expansion threshold. Because the previous rise was short-lived, this reversal does not necessarily signal an impending downturn; rather, it suggests that even though overall growth remains strong, it may be increasingly concentrated.

Financial Markets

Financial conditions tightened significantly as expectations grew that massive AI infrastructure spending could compete with government borrowing for capital. Longer-dated Treasurys bore the brunt of the selloff, pushing the 10-year yield to a multi-decade high. This upward movement was also fueled by concerns that heavy AI investment would accelerate economic growth enough to rekindle inflation, reinforcing expectations of further Federal Reserve rate hikes. Additionally, heavy equity and corporate bond issuance from major tech firms has intensified market tightness by absorbing liquidity and competing directly with other assets.

Goods Production & Sentiment

Goods manufacturing continues to gain momentum, even as business and consumer sentiment remains mixed. The ongoing AI buildout has sparked a surge in construction activity, boosting manufacturing production. Outside of tech spending, however, signs of sluggishness persist — most notably in the housing sector, where home-building has slowed. Economic surveys show ongoing concern over rising costs for both suppliers and consumers.

Labor Market

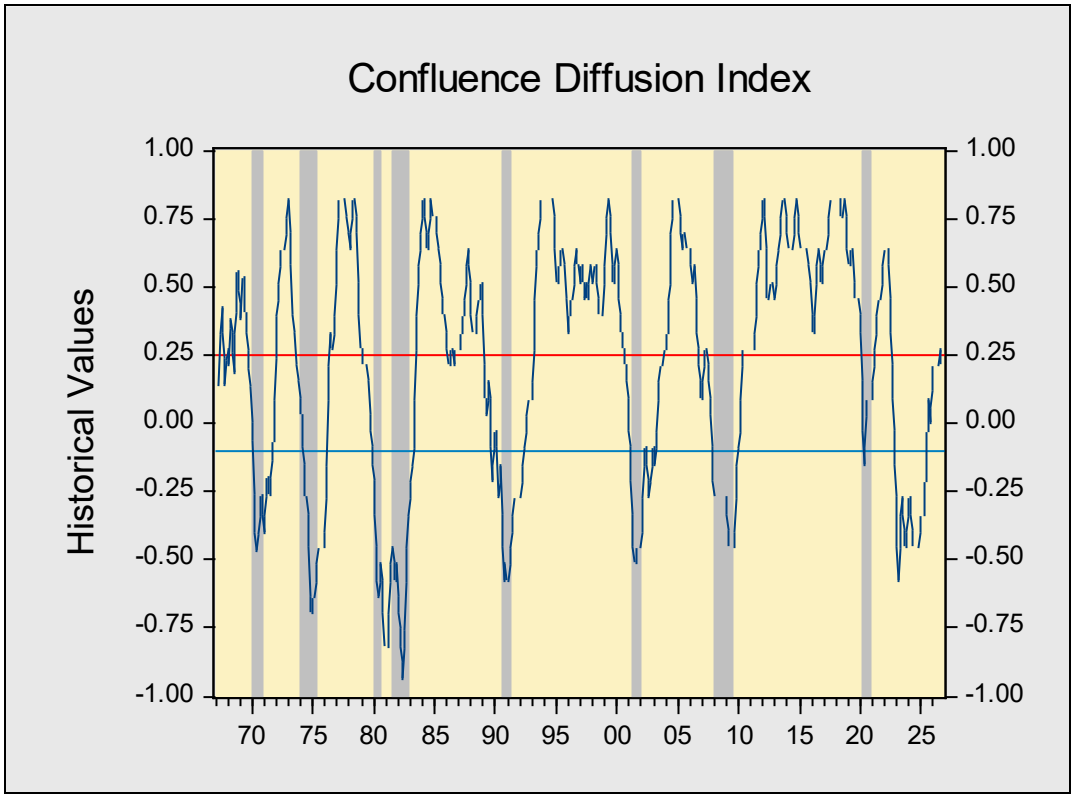
The labor market has weakened slightly from the previous month but remains solid. The economy added 29,000 jobs last month, driven by strong growth in construction and healthcare services. Unemployment ticked up to 4.2%, slightly above the previous month's rate, but still at a level consistent with economic expansion. Initial jobless claims remain well below historical averages, indicating that firms are holding on to their existing workforce.

Outlook & Risks

Growth was robust in the third quarter and should maintain momentum through the end of the year. Heavy investment in artificial intelligence has driven business fixed investment, providing significant support to the broader economy. Over the coming months, this spending is expected to broaden into other sectors, further bolstering expansion. Consumer spending remains resilient despite tighter credit conditions. While a recession does not appear imminent, we are monitoring a potential slowdown in AI spending as a pullback in the sector could present a key headwind to overall growth.

The Confluence Diffusion Index for October, which provides a composite view of the economy based on 11 benchmarks, remains in expansionary territory using September data. The index fell from +0.2727 to +0.2121, slipping below the contraction threshold. Despite this slight decline, the broader economy appears to be in solid shape, though underlying growth remains uneven. Currently, only four of the 11 benchmarks are in contraction territory.

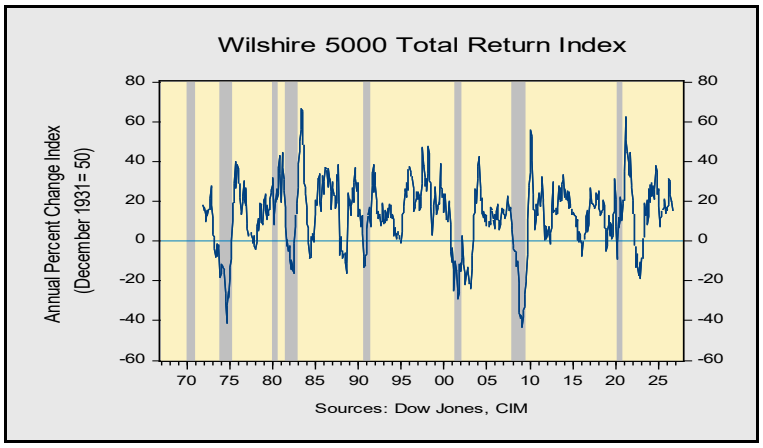
- Concerns about the economy overheating are pushing up yields.
- Sentiment remains low but spending continues.
- The labor market remains in "low hire, low fire" mode.



The chart above shows the Confluence Diffusion Index. It uses a three-month moving average of 11 leading indicators to track the state of the business cycle. The red line signals when the business cycle is headed toward a contraction, while the blue line signals when the business cycle is in recovery. The diffusion index currently provides about six months of lead time for a contraction and five months of lead time for recovery. Continue reading for an in-depth understanding of how the indicators are performing. At the end of the report, the *Glossary of Charts* describes each chart and its measures. A chart title listed in red indicates that the index is signaling recession.

Financial Markets

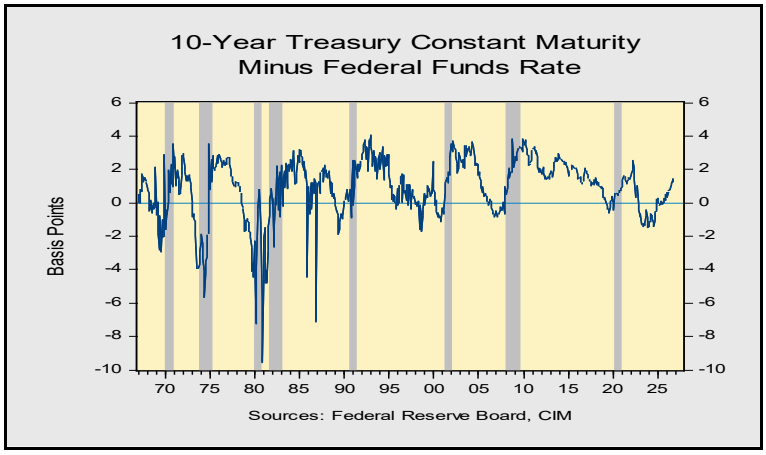
Wilshire 5000 Index



The Wilshire 5000 Total Return Index for September rose 15.1% from the prior year.

- Top-performing sectors: Information Technology, Communication Services, Health Care.
- Bottom-performing sectors: Materials, Financials, and Real Estate.
- Indicates recession when the level falls below zero.

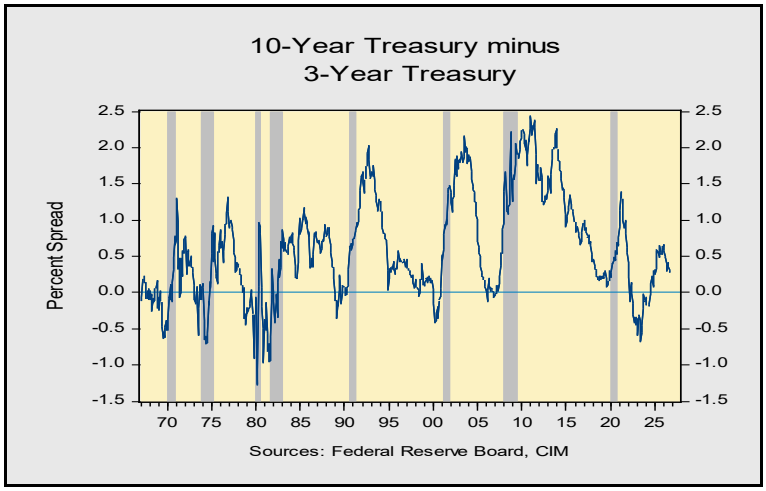
10-Year Treasury Constant Maturity Minus Federal Funds Rate



The financial spread, which is the 10-year Treasury yield minus the effective fed funds rate, increased from +1.12 to +1.41.

- The effective fed funds rate rose from 3.63% to 3.88%.
- The 10-year Treasury increased from 4.75% to 5.29%.
- Indicates recession when the level falls below zero.

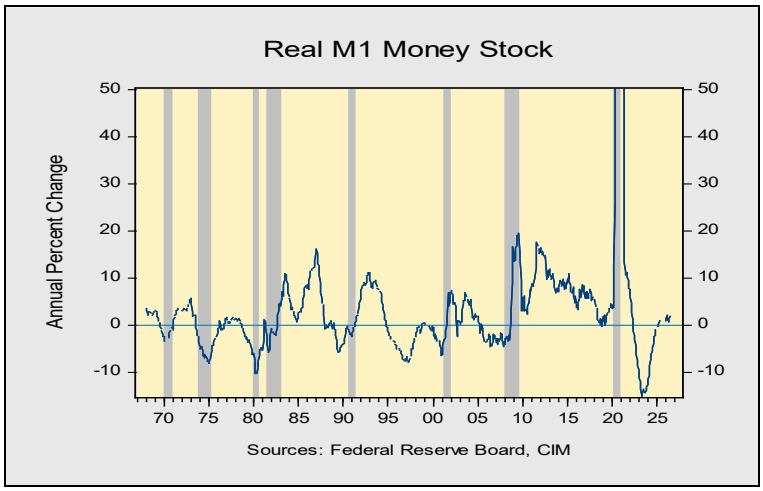
10-Year Treasury Minus Three-Year Treasury



The term spread between the 10-year yield and three-year yield fell from +0.35 to +0.29.

- The 10-year Treasury increased from 4.75% to 5.29%.
- The three-year Treasury yield increased from 4.40% to 5.20%.
- Indicates recession when the level falls below zero.

Real M1 Money Stock

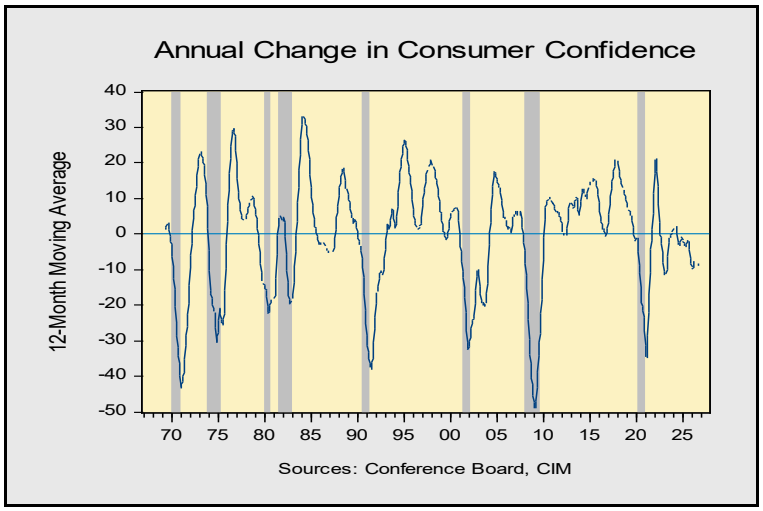


Real M1 money stock rose 2.5% from the prior year.

- Headline CPI rose 3.7% from the prior year.
- M1 money stock rose 6.2% from the prior year.
- Indicates recession when the level falls below zero.

Goods Production & Sentiment

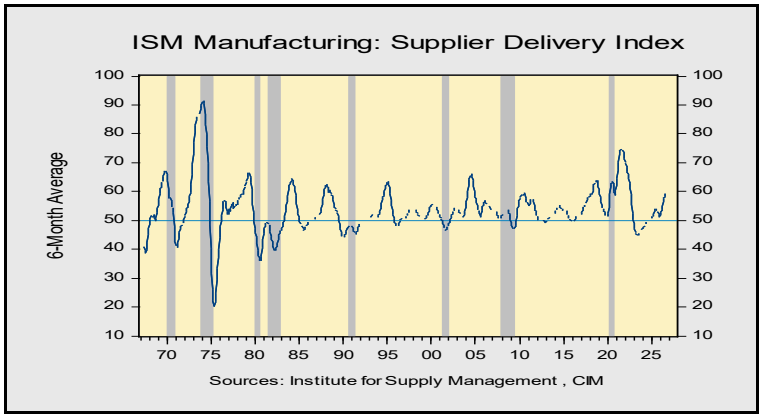
Consumer Confidence



In September, the 12-month moving average of the annual change in consumer confidence fell from -8.30 to -9.21.

- Consumer confidence came in at 81.9, down from 95.6 in September 2025.
- The sub-index for the current situation came in at 109.3, down from 127.5 last year.
- Meanwhile, the sub-index for future expectations decreased from 74.4 to 63.6 in the same period.
- Indicates recession when the level falls below zero.

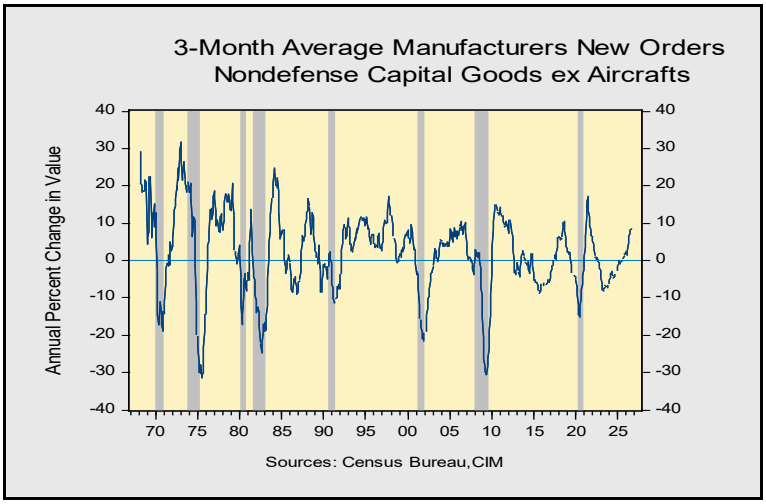
ISM Manufacturing: Supplier Delivery Index



The six-month moving average of the Supplier Delivery Index was unchanged at 59.3.

- The overall index fell from 54.6 to 54.5.
- The Supplier Delivery Index fell from 59.3 to 59.0.
- Indicates recession when the level falls below 50.

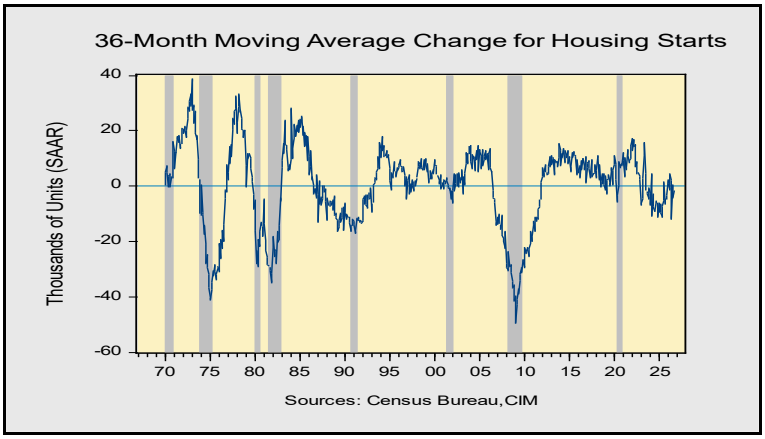
Three-Month Average Manufacturers' New Orders
Nondefense Capital Goods excluding Aircraft



The three-month moving average of the annual change in new orders for nondefense capital goods rose 9.1% from the prior year.

- In September, new orders were down 0.3% from the prior month and rose 8.5% from the previous year.
- Indicates recession when the level falls below zero.

36-Month Moving Average Change for Housing Starts

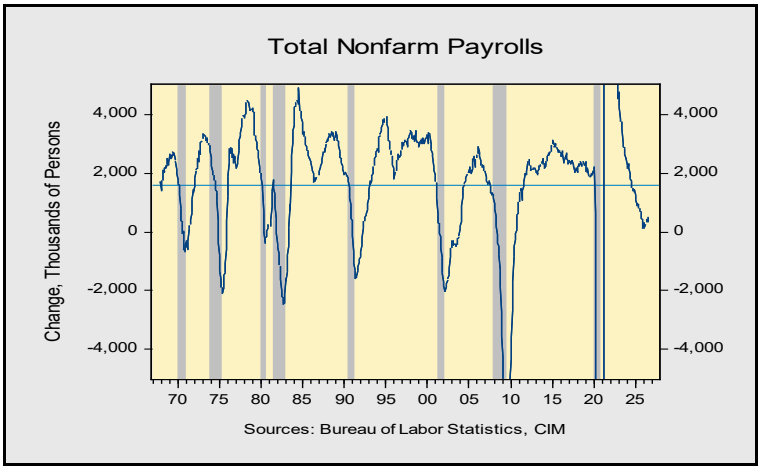


The 36-month moving average change for housing starts worsened from -0.9 to -4.1.

- Housing starts expanded at an annualized rate of 1,221k, below the previous month's revised pace of 1,288k.
- Single-family starts fell from 900k to 859k. Multi-family dwellings fell from 376k to 349k.
- Indicates recession when the level falls below zero.

Labor Market

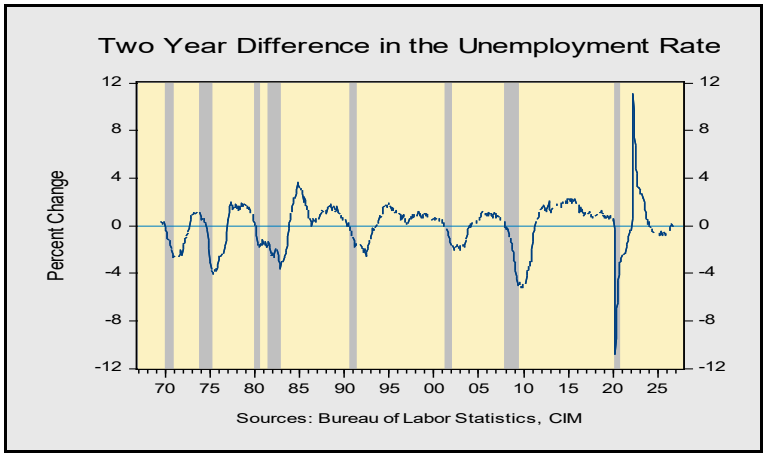
12-Month Sum of Nonfarm Payrolls



The 12-month moving sum decreased from a revised 543k to 496k.

- Nonfarm payrolls showed that the economy added 29k jobs in September.
- Service-Providing industries added 28k jobs. The Goods-Producing sector added 18k jobs from the previous month, while the Government sector lost 17k jobs.
- Indicates recession when the level falls below 1,500k.

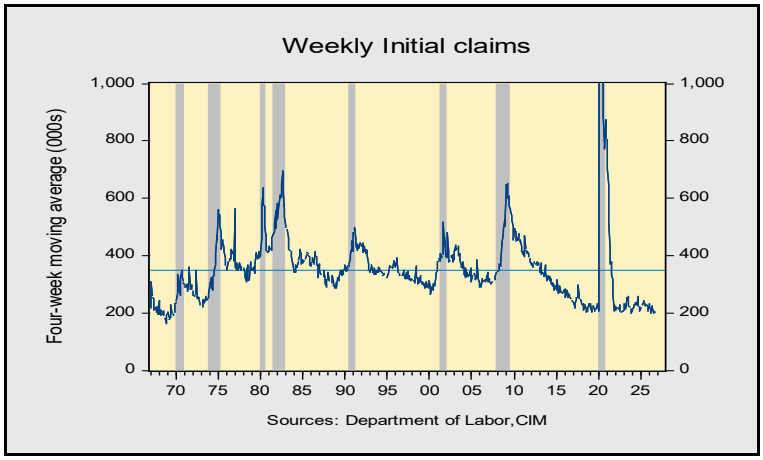
Two-Year Difference in the Unemployment Rate



The two-year difference in the unemployment rate fell from +0.1 to -0.1.

- The unemployment rate rose from 4.1% to 4.2%.
- The number of unemployed rose 1.1% from the prior month.
- Indicates recession when the level falls below zero.

Weekly Initial Claims



Average weekly claims for September were unchanged at 199k.

- Indicates recession when the level rises above 350k.

Thomas Wash, CBE
November 6, 2026

This report was prepared by Confluence Investment Management LLC and reflects the current opinions of the author. It is based on sources and data believed to be accurate and reliable. Opinions and forward-looking statements expressed are subject to change. This is not a solicitation or an offer to buy or sell any security.

Glossary of Charts

Consumer Confidence: The Consumer Confidence Index is an economic indicator that measures the level of consumer optimism about the overall state of the economy and consumers' personal financial situations. This chart shows the 12-month moving average of the annual change of the index.

Wilshire 5000 Index: This chart shows the annual change in the Wilshire 5000 Total Return Index, which is the broadest US equity index. The index contains 3,500 stocks and is designed to track the overall performance of the US stock market. It is an important indicator because steep equity pullbacks have often coincided with economic contractions.

Three-Month Average Manufacturers New Orders Nondefense Capital Goods excluding Aircraft: This chart shows the annual change in the value of core capital goods orders. This indicator gives insight into the amount of business investment spending. A positive report suggests that manufacturers are optimistic about future demand.

10-Year Treasury Constant Maturity Minus Federal Funds Rate: This chart shows the spread between the 10-year maturity and the fed funds rate. It reflects the market sentiment of the future state of the economy. Generally speaking, a negative spread suggests a contraction is likely to occur within 24 months.

36-Month Moving Average Change for Housing Starts: This chart shows the 36-month moving average of the annual change in housing starts. This is an important indicator because it provides a gauge of future construction activity. If housing starts are strong, it implies that builders are optimistic about future demand.

ISM Manufacturing (Six-Month Average): The ISM Manufacturing Index is a report that monitors employment, production, inventories, new orders, and supplier deliveries. This index specifically focuses on the six-month moving average of supplier deliveries section in ISM, which we believe is a good gauge of future levels of manufacturing activity. A reading above 50 signals that manufacturing activity is expected to expand, while a reading below 50 signals that manufacturing activity is expected to contract.

Total Nonfarm Payrolls: This chart shows the 12-month moving sum of total nonfarm payrolls. This report represents the total number of workers added to the workforce, excluding proprietors, private household employees, unpaid volunteers, farm employees and incorporated self-employed. It is a significant indicator of the strength of the labor market. A moving sum that exceeds 1,600 suggests the demand for labor is intense.

Real M1 Money Stock: The Real M1 Money Stock report measures the annual change in the money supply minus inflation. M1 is the measure of currency in circulation and represents the amount of money being held for transaction purposes, therefore it can act as a proxy for economic activity.

10-Year Treasury Minus Three-Year Treasury: This chart shows the spread between the 10-year and three-year Treasury and gauges investor sentiment. A widening spread suggests investors are optimistic about the state of the economy, whereas a negative spread suggests pessimism. This indicator is less sensitive than the financial spread as it is less affected by the Fed's decisions.

Two-Year Difference in the Unemployment Rate: The two-year difference in the unemployment rate measures the amount of slack in the labor market. When the difference of the two-year unemployment rate falls below zero, it indicates the labor market is becoming less tight.

Weekly Initial Claims: This chart shows the four-week moving average of initial jobless claims. A rising initial claims number means the demand for labor is weakening, likely due to a worsening business environment. If the four-week moving average rises above 350K, it signals the economy April be headed toward a contraction.