Are We in a Recession or Not?

Presented by Christopher Phelps

The first estimate of national economic growth, the gross domestic product (GDP), came in this morning at an annualized, quarter-on-quarter growth rate of –0.9 percent. This is better than last quarter's number of –1.6 percent, but it is still the second quarter in a row of decline. By some definitions, this means we are now in a recession, and you can expect to see that all over the headlines in the next several days.

Recession Defined

But before you get too upset, you need to know a couple of things. First, the formal definition of a recession isn't that simple—and by that definition, we are not in a recession yet. Second, when you look at what caused those declines—in both quarters—they are not what drives a real recession, but are more in the nature of technical adjustments. So for two reasons, what we have here is more of a technical recession than a real one, if you even want to call it a recession.

A recession, to the average person, is when the economy shrinks. So far, so good. But what shows up to the average person when the economy shrinks are job losses, stores closing because people aren't shopping, and in general the kind of misery that affects the average person.

Slow Growth Is Still Growth

But when we look around, that is not what we see. Job growth remains strong, with millions of excess job openings available and voluntary quit rates still close to all-time highs. Consumer spending is still growing, albeit at a slower rate, and business investment was basically flat. Yes, inflation has hurt confidence, but for real things the economy continues to grow in ways we don't see in a recession.

Another way to understand that is to look at gross domestic income (GDI), the much-less-reported twin to GDP. GDP is purchases, and GDI is income. In theory, they have to be equal. They usually are quite close, but this year so far we have a discrepancy with GDP down while GDI is up. In the past, when this kind of gap has opened, GDP has often ended up being revised to match GDI, suggesting that might happen this time as well. Growth in income usually means growth overall.

And that is what we see on a longer-term basis. The quarter-on-quarter number, annualized, is what is reported, but the year-on-year number (i.e., where the economy is now compared with where it was a year ago) still shows growth. Slower growth, but still growth.

Why the Negative Numbers?

In both the first and second quarters, the negative numbers were due to adjustments in the aftermath of the pandemic, rather than real economic weakness. In the first quarter, exports dropped enough to take overall growth negative (but have since rebounded). In the second quarter, much of the weakness came from businesses continuing to cut their inventories, not because of sales declines, but because as the economy continues to recover from the pandemic, what people are buying has changed. Once that adjustment is completed, that too should reverse. In both cases, this is a post-pandemic adjustment, rather than something worse. As such, this looks more like a technical recession, at worst, than a real one.

Make no mistake, the data is showing a slowdown. Growth has slowed across the board and will likely continue to do so. We could be looking at a real recession sometime in the next year or so. But despite the numbers, we are not there yet.

Job growth is still strong, which doesn't happen in a recession. Businesses are still investing (ditto). National income is still growing (ditto). If this is a recession, it is better in many respects than many non-recessionary periods we have seen in the past decade.

The Bottom Line

Whatever we call it, it doesn't matter. The facts are the economy is in better condition than the headline numbers suggest. Despite inflation and everything else, the average person is still able to work and shop. And if that is as bad as this "recession" gets? We will be pretty lucky.

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