A Recession is Not Inevitable

by Michael Curtis

Don't know why, there's no sun up in the sky, stormy weather, keeps raining all the time, amidst signs of gloom and misery everywhere. Yet the music goes around and around, and the notes come out well. In 2019 the note blown by many so-called experts, in what appears "group think," is that an economic recession will have started by 2020, not only in the U.S. but one that is global, caused, among other things, by trade wars and weak growth in China and the EU, and fear of a continuing trade war between the United States and China. This note goes round and has influenced American public opinion. About 60% of Americans say they expect a recession next year, though paradoxically almost the same number view the economy positively.

Prediction, however, should not be seen as certainty or inevitability. A research paper by the IMF of March 2018 suggests that experts have a poor record in predicting recessions. Of 153 recessions in 63 countries, 1992-2014, only five were predicted by a consensus of private sector economists in the preceding year.

An economic recession, a general decline in economic activity, can be defined in general as a significant decline in spending and in economic activity lasting more than a few months, visible by changes and declines in a number of indicators: real GDP of at least 1.5%, real income, credit availability, rise in unemployment to level of at least 6%, building loans, more building closures and business failures, industrial production, and retail sales. In the UK, a recession is officially viewed as negative economic growth for two consecutive quarters.

It is axiomatic that the free market system is characterized by periods of recession, changes in consumer demand and business activity, and is not always self-correcting, even by stimulation of lower taxes, spending on social programs, and ignoring budget deficits. The economic system is cyclical, with fluctuations of recession, depression, recovery, expansion, depending on many factors such as energy crises, wars, world events, and extent of government intervention. The term “recession,” coined around 1930, is distinguishable from “depression,” which is longer lasting and more severe. Historically, the U.S. has experienced a number of them, especially after the very severe one in 1937-38.

Are the pessimists correct and is the U.S. due to experience a recession? The economy has positive indicators. It has shown a fast growing GDP and averaged 156,000 new jobs, above average, over the past 3 months and increased wage growth in 2017 and 2018. Administration tax reform and deregulation have been a spur. Unemployment is at 3.7%, a 50 year low. Labor force participation rate is 63.2% with the various sectors, non-farm 151 million, services 130 million, goods 21 million, and agriculture 2.4 million. The U.S. economic recovery is the longest period of expansion ever recorded.

Unemployment of black Americans fell 0.5% to 5.5%, an historic low, and the rate for Hispanics fell to 4.2%. Workers 25-54 old working or seeking work increased to 82.6% in August.

Average hourly earnings increased by 0.4%, and the length of the average workweek also increased. The unemployment rate depends on educational level: for those with a university degree it is 2.1, while of those with only or less than high school education it is 5.4%.

But there are signs of weakness. The job growth slowed to its weakest pace in 3 months in the month of August 2019 despite a boost from temporary hiring for 25,000 census workers. The private sector in August added only 96,000 jobs. Non-farm payrolls rose by 130,000, short of expectations of 158,000. Mining and logging sectors lost jobs , and manufacturing increased only 3,000. Demand for U.S. goods fell, due in part to U.S. protectionism. Slower growth means less job creation and slower wage gains. Differences are apparent. The service economy is larger and growing, as in education, health services, professional services, but the manufacturing sector made only small gains, or lost jobs as with mining and logging. The trade war affects this, tariffs are only on goods and that is manufacturing. Manufacturing sector exports a larger share of their products than other sectors and are dependent on suppliers overseas.

Elsewhere, there as a world wide economic decline. To deal with this, China’s central bank released a large sum to spur the economy, and the Bank of Russia cut its key interest rate. In similar fashion, the U.S. Federal Reserve for fiscal stimulus also cut 6 percentage points.

Undoubtedly, world manufacturing and investment has slowed with four months of contraction, though service sectors are resilient and predictions are that the world economy will grow by 3.2%. There are inherent complexities in the issue. Recession may result from different factors. Declining unemployment and increasing wages are welcome, but higher pay leads companies to raise prices and this leads to inflation. The result may be higher costs for borrowing for business and consumers, and higher mortgage rates. Federal tax cuts and increased spending may increase rates.

A number of factors affect the possibility of recession. Tariffs are likely to raise prices for consumers and businesses. This is the danger of the considerable tariffs threatened or imposed by President Donald Trump on Chinese goods and retaliation by China. Another problem is the higher energy prices which have contributed to every recession since World War II, partly the result of the antagonism between Saudi Arabia and Iran which threaten increase in gas and oil prices. A third problem is the issue of the limit of the national debt, connected with the amount of defense spending, that could lower the U.S. credit rating and impact economic confidence.

Rising rates force consumers and business who take on adjustable rate loans pay more each month and reduce other spending. In the U.S. higher rates are troublesome for consumers with credit card debt and big auto loans. Higher rates slowed home and auto sales because of higher interest cost on these expenses.

Not surprisingly in the U.S. differences on the economic policy of President Trump are apparent among citizens, men and women, and the political parties. A Washington Post-ABC poll conducted in early September 2019 indicates that about two-thirds of men say the economy is good or excellent, but that less than half of women do so. There are sharp differences over costs being increased because of tariffs. More than 80% of Democrats are concerned that the trade dispute will raise prices on items they will buy but only 30% are similarly concerned.

Yet the poll also shows the concern about price increased among some Republicans, whites without college degrees, those living in rural areas, and white evangelical Protestants.

Opinions about possibility of recession may change with various factors: retirements of the baby boomer generations, agreement or continuation of the tariff conflict between the U.S. and China, the growth of the Chinese economy, the decline in the trade surplus of $34 billion by China over the U.S., changes in productivity rates, increases in wages and in corporate profits, tariffs on steel and aluminum imports, the growing amount of debt, the increase in automat production and services that have been enhanced by artificial intelligence, and immigration factors.

The economic world is unfair, even if one does not accept the argument and the implication of the analysis by the French economist Thomas Pikettyn that the return on capital is likely to grow faster than the economy itself, and that the return on capital is larger than that on income. Levels of inequality will remain in the U.S. and in the world, but this does not suggest that an economic recession is likely, let alone inevitable.