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INSIGHT

Is the U.S. Economy in a Recession?

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On July 28, 2022, the Bureau of Economic Analysis (BEA) published its advanced estimate for second quarter gross domestic product (GDP), which showed that real GDP fell by 0.9% after a 1.6% drop in the first quarter. This has many commentators concerned that the U.S. economy has reentered a recession. However, the National Bureau of Economic Research (NBER), an independent nonprofit organization, declares official recessions. If the economy is currently in a recession, it would likely be some time before the NBER made it official, because it first wants to make sure that the downturn is significant and long lasting.

In the meantime, economists and policymakers disagree about whether NBER will ultimately determine that the economy is currently in a recession. A commonly used unofficial rule of thumb for predicting recessions is two consecutive quarters of negative real GDP growth—a criteria now met. But the GDP data have not followed the pattern one would typically expect in a recession, and other indicators, such as employment, are still growing strongly. For background, see CRS In Focus IF10411, *Introduction to U.S. Economy: The Business Cycle and Growth*.

What Is a Recession?

Recessions are not determined by the federal government and are not defined in statute. NBER defines *recession* as a "significant decline in economic activity that is spread across the economy and that lasts more than a few months" and does not have a set numerical formula to define a recession. Instead, NBER evaluates three criteria—depth, diffusion, and duration—using a variety of monthly economic indicators including, but not limited to, income, employment, consumption, sales, and industrial production. (Notably, inflation is not a determinant of recessions.)

An outsized impact to one criteria can make up for a weaker impact to another. For example, NBER declared the United States to be in a recession from March to April 2020—less than two quarters—owing to the extreme drop in economic activity, despite the brevity of the contraction. Although NBER considers GDP growth in its quarterly business cycle dating, NBER cites several reasons for not using the two-quarter rule as a definition for recessions, including not relying on just one indicator, considering depth of declines in activity, using more frequent monthly data (so as to provide monthly dates for recessions), and accounting for discrepancies in output and income data—including in the first quarter, when output fell and income rose. In the meantime, one can observe how GDP and employment have performed so far.

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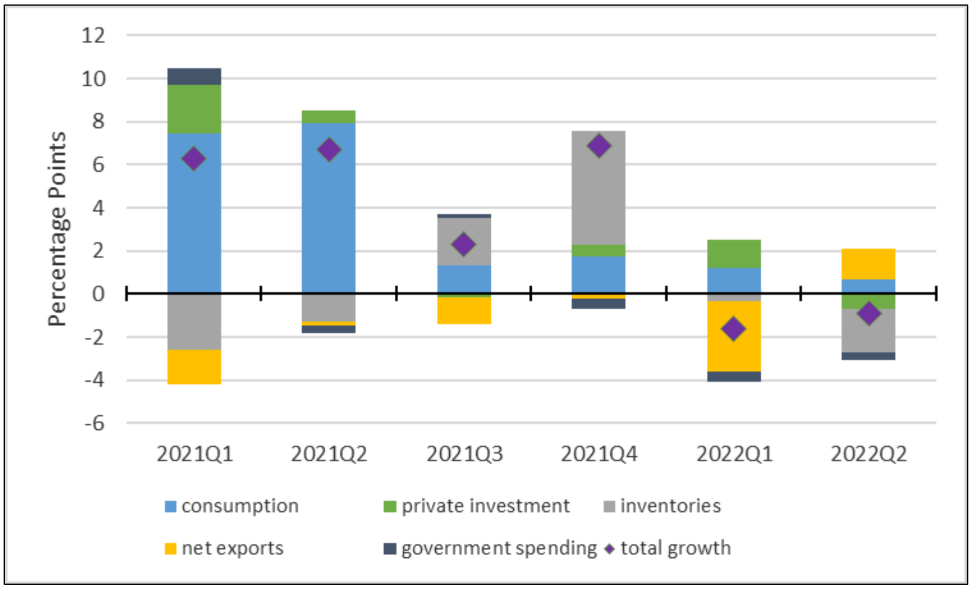
GDP in 2022

Parsing exactly what has happened with real GDP over the past two quarters is important in determining the likelihood that the economy is in a recession. It should be noted that the BEA's advanced estimate is based on incomplete data and will be subsequently revised, which may change the picture of the economy in 2022. In fact, the absolute average revision to past advanced estimates is larger than the second-quarter decline. Keeping that in mind, **Figure 1** shows the contributions to the percent change in real GDP. The growth rate during the initial recovery from the COVID-19 pandemic was relatively high but has sputtered in 2022. A significant portion of the decrease in real GDP in the first half of 2022 was a result of a drawdown of business inventories after an unusually large buildup in the second half of 2021. If the drawdown was a one-off, it would not necessarily be indicative of recessionary conditions.

Figure 1. Contributions to GDP Growth



Source: BEA.

A fall in net exports and government spending also contributed to the negative first quarter growth. The contribution of government spending was negative again in the second quarter, which is unlikely to be caused by cyclical factors. Personal consumption expenditure growth—one of the main metrics NBER considers—was positive in the first and second quarters, although it did slow in the second quarter. Personal consumption expenditures typically account for about two-thirds of GDP, and thus, a further slowdown could be problematic for future growth. Perhaps most meaningful is the 13.5% decrease in gross private domestic investment in the second quarter. It was led by a 14% drop in residential fixed investment, which could be another sign of a cooling housing market and which some economists consider to be another recession predictor.

Does the Labor Market Suggest Recession?

Despite negative GDP growth in 2022, most indicators suggest that the labor market is still strong. From March to June 2022, the unemployment rate has been 3.6%, relatively low by historical standards. The economy has added at least 350,000 jobs in each of the past 14 months. (However, the Current Population Survey shows employment declines in two of the past three months.) Average hourly earnings increased by 5.1% in the 12 months ending in June. It would be unprecedented to have a recession during such a strong labor market.

Another unofficial, rule-of-thumb recession predictor is called the "Sahm Rule." It finds that all recessions since 1945 have featured at least a 0.5 percentage point increase in the unemployment rate relative to its previous annual low point—something that has not occurred to this point. The two-quarters rule and the Sahm rule are not official indicators of recession, but the fact that they currently conflict shows that evidence of a recession is mixed at best.

Conclusion

According to NBER, the two indicators it most closely considers for dating recessions are real personal income less transfers and nonfarm payroll employment. The economy had strong job growth in the first half of 2022. Real personal income less transfers grew in April and May as well but fell in June, potentially pointing to a slowdown if this trend continues. Whether or not the economy eventually proves to be in an official recession, the picture provided by the data available at this point is mixed—output growth seems to be slowing while labor market growth remains robust. Nevertheless, efforts to reduce inflation may cause a further slowdown in the coming months.

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