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Recessions

Is a recession really very likely? —NERVOUS ABOUT THE ECONOMY

On the one hand, we may be in a recession already. The conventional shorthand metric for recession is two consecutive quarters of contracting Gross Domestic Product (GDP). The first quarter of 2022 saw a 1.6% decline in GDP, and the early indications are that GDP was down in the second quarter also, perhaps as much as 2%.

On the other hand, that conventional shorthand is not conclusive. The National Bureau of Economic Research, the arbiter of the boundaries of recessions, uses many economic indicators in making its judgments, of which GDP is but one. The unemployment rate is another. Recessions are typically marked by sharp spikes in unemployment, but at the moment we are experiencing the opposite, a significant and prolonged labor shortage. On average, during recessions since World War II the unemployment rate has risen by 3.5 percentage points. So long as employment remains robust, recession should be merely a cloud on the horizon.

On yet another hand, the Federal Reserve is raising interest rates to bring inflation under control. Fed Chairman Powell has explicitly warned that rate increases will continue despite the risk of triggering a recession. That's the same stand that Paul Volcker took when he tamed the inflation of the 1970s and early 1980s, the last time sustained inflation was as high as it is now—and it did cause a recession then.

The stock market went into bear market territory in June, and bear markets are correlated with recessions. The great economist Paul Samuelson reportedly advised that the stock market had accurately predicted nine of the previous five recessions, implying that the market frequently overreacts. But Robert Bartley, editor of The Wall Street Journal, responded that in the other four the government got the message in time and changed course, averting the downturn.

Sorry I can't be more definitive. I will suggest that this may be a good time for prudence, for caution, given the many unusual uncertainties in the global economy. If you'd like to discuss how this might impact your investment portfolio, please arrange for an in-person consultation.

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