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WEALTH MANAGEMENT

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Monthly Insight

Is It a Recession? Or Is the Economy Just in a Bad Mood?

When was the last time you “woke up on the wrong side of the bed”? Maybe things were not going smoothly at work; maybe the kids were particularly demanding; maybe you burned your toast. Whatever it was, something got your day started on the wrong foot, and you just couldn’t seem to get back on track.

These days, many investors are worried that the economy is in a similar sour mood. With inflation running higher than it has in decades and the Fed raising interest rates, the questions on many minds are "Are we headed for a recession? Are we in one already?" Naturally, thoughts then turn quickly to what to do next: Should we change our investment strategy? What can we do to protect our portfolios? Is the market headed for a tailspin?

Though it is not clear that our current economic situation meets the definition of a recession (and by the way, there is no single definition, as we'll discuss in a moment), the negative business and economic climate associated with recessions is certainly something that bears better understanding. Especially now, with analysts and investors watching the Fed's efforts to tame inflation without provoking a recession, the topic is on many minds. It might be useful to think about what we know about recessions—and what we don't know.

1. There is no single definition.

Like a bad mood, we all have a pretty good idea of what a recession feels like: negative economic growth, high unemployment, disappointing retail sales, and other indicators. One commonly used definition is "two or more quarters of negative growth in gross domestic product (GDP)." Since the first quarter of 2022 evidenced negative GDP growth of 1.6%, some might say we are "halfway" to a recession.

But on the other hand, the US experienced a sharp recession in March and April 2020, coinciding with the onset of the COVID-19 pandemic. Economic activity didn't just contract, it came to a dead stop. Unemployment soared to over 10%. US stock markets lost over 30% of their value. By any measure, the economy was in dire straits. And yet, that recession lasted just two months—well short of the minimum six months of economic contraction required by the "classic" definition. In fact, it was the shortest recession in history.

What this means is that recessions come in all shapes and sizes and can be caused by a variety of factors, either singly or in combination. For the Great Recession beginning in 2008, the precipitating cause was the financial crisis brought on by the collapse of the market for certain mortgage-backed securities. In 2020, it was a worldwide pandemic. If we see a recession this year or next, the causes may well lie with higher inflation, combined with persistent supply-chain problems and the world oil shortage caused by the war in Ukraine. The only thing we know is that it will be different.

2. You never know how long it will last.

Just as there is no universal agreement on how to define a recession, there is no set length of time for a recession to run its course. Also like a bad mood, we won't know a recession is over until after the fact. For example, the National Bureau of Economic Research (NBER, the organization that keeps track of economic cycles in the US) declared in July 2020 that the COVID recession was over—three months after it was already concluded.

Going back to 1857, the average length of a recession is a little less than 17.5 months. By the way, that includes a couple of major outliers: the recession of 1873 lasted 65 months, and the Great Depression ran for 43 months. Since World War II, recessions have averaged slightly less than a year (for which we can probably thank the establishment of the Federal Deposit Insurance Corporation).

And we should also consider the flipside: the average length of business expansions. They tend to run much longer than recessions, averaging four to five years in length. The longest business expansion on record, according to the NBER, was just over 10.5 years, ending in February 2020. Does that date sound familiar?

3. They're a normal part of the cycle.

Just as you can't be "up" all the time, the economy can't expand indefinitely. As much as we would prefer it to be otherwise, recessions are part of the natural economic cycle. They may not be anyone's favorite tool for cooling off an overheated economy, but recessions sometimes are needed to help rein in runaway spending, earning, and pricing for companies, consumers, and creditors alike.

For example, in our current climate, we may enter into a recession as a byproduct of the interest rate increases aimed at warding off rising inflation, amidst the backdrop of lingering COVID-19 supply side issues and global economic sanctions against Russia. If we can avoid a recession (the much-desired "soft landing" that the Fed hopes to engineer), all the better. But if it's going to take a modest recession to reduce inflation, that may be the medicine the economy needs for the long haul.

4. You can't always control the circumstances, but you can control your response.

When you're in a bad mood, even if it's caused by something that's not your fault, you still have a choice: you can either pass your negative disposition on to everyone you meet, or you can "act better than you feel" and wait until the blues dissipate. The same principle holds for dealing with a recession. You can't control the US economy or the monetary policy of the Fed. But you can control your reactions to the market movements that inevitably accompany talk of a recession. There are several constructive steps you can take, even during a recession, to maximize your financial resources while maintaining your long-term financial plan.

- Retirees, review your "draw-down" strategy. All sources of funds are not created equal, and by strategizing properly, you can minimize the rate at which you deplete the assets you'll need for future growth.
- Notice the opportunities. They're out there, even in a recession. In fact, this may be the time to look past today's risks, channel your

"inner Warren Buffett," and retain an appropriate amount of market exposure in pursuit of your long-term financial goals.
- Stay disciplined. Panic selling in response to negative economic news or market downturns is not a recipe for long-term financial success.
- Review your budget. Cut back on spending where possible, and consider building up a little extra cushion in your emergency fund. This will also help you avoid the temptation to react emotionally to temporary situations.

Perhaps the most constructive step you can take, if you're concerned about the effects of a possible recession on your portfolio, is to have a long talk with a qualified, fiduciary financial advisor. Getting the perspective of a professional with experience and access to the latest market and economic research can go a long way toward helping you avoid making decisions that could undermine your long-term financial success. At Empyrion Wealth Management, we know our clients depend on solid, evidence-based guidance, delivered with their best interests foremost. To get a complimentary "second opinion" on your financial or investing plan, please click here.

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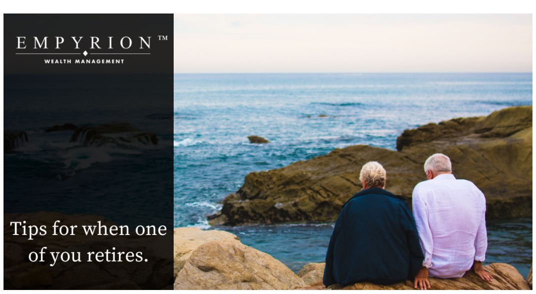
SOCIAL MEDIA DIGEST

In case you missed them, here is a roundup of my latest posts on social media:

At Empyrion, our clients receive full-

spectrum #financialplanning and #investment advice driven by proven research, rigorously tested by some of the most respected minds in academia. We focus our recommendations on the unique needs of each client, developing strategies that are in line with their circumstances, future goals and current or anticipated challenges. Download our informed investor whitepaper.

Kids need access to quality information about #personalfinance in order to have the best chance of becoming financially independent adults. And there has never been a more crucial time than the present for parents and other concerned adults to make sure they get the financial education they need. Read more. #wealthmanagement



When only one of you retires, things can feel off balance, but it's important for couples to communicate expectations and plans for things like household duties and finances. Whether you are planning to retire together or at different times, Empyrion Wealth Management is committed to helping thriving retirees create smooth transitions and well-funded retirement lifestyles. #retirementplanning #wealthmanagement

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"We understand that every person we serve has distinct values and ambitions, and they each need their own plan for wealth management."