

*Bill Watkins*

*September 2009*

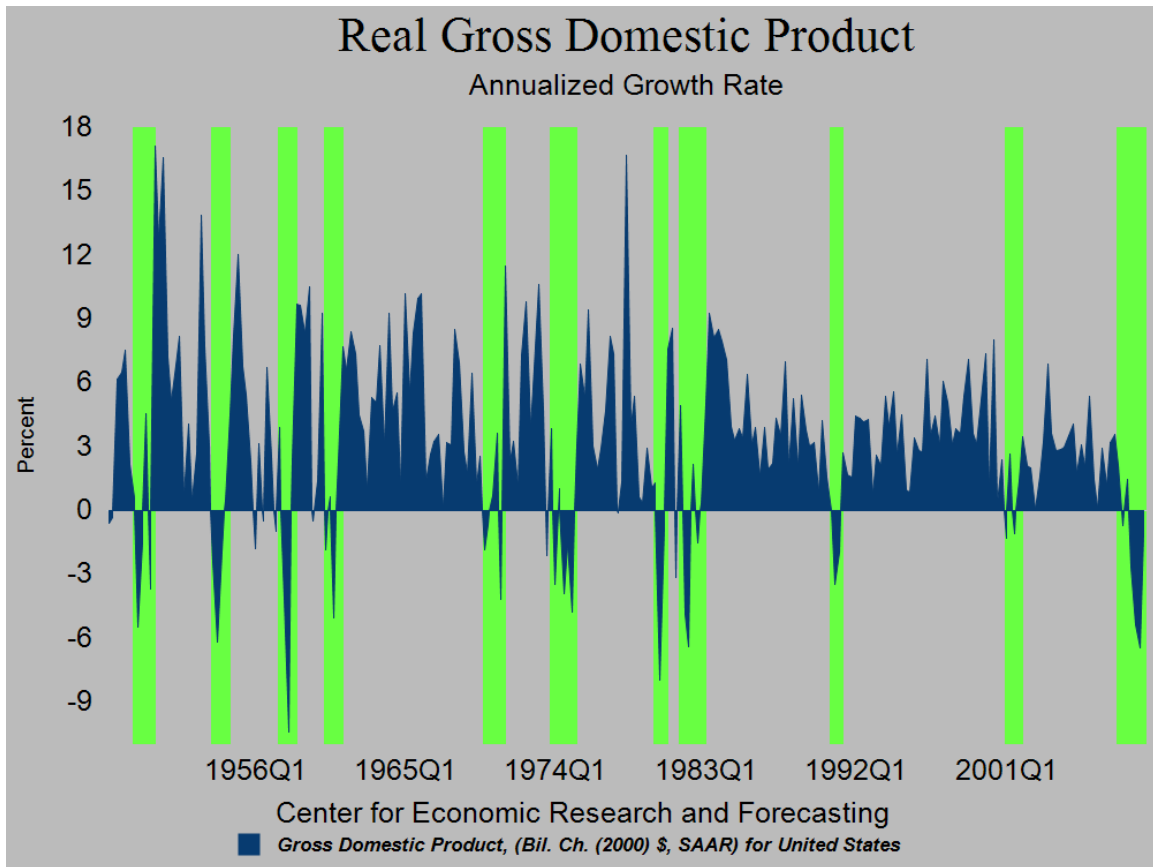
A few weeks ago real gross domestic product (GDP) data were released for Germany and France. Both came in at a positive 0.3 percent. Some headlines claimed that these country's recessions were therefore over. Not necessarily.

In the first place, the numbers for Germany and France are extremely small, probably within a standard error of zero. It wouldn't take much for the inevitable revisions to turn those small positive numbers to negative numbers. There goes the end of those recessions.

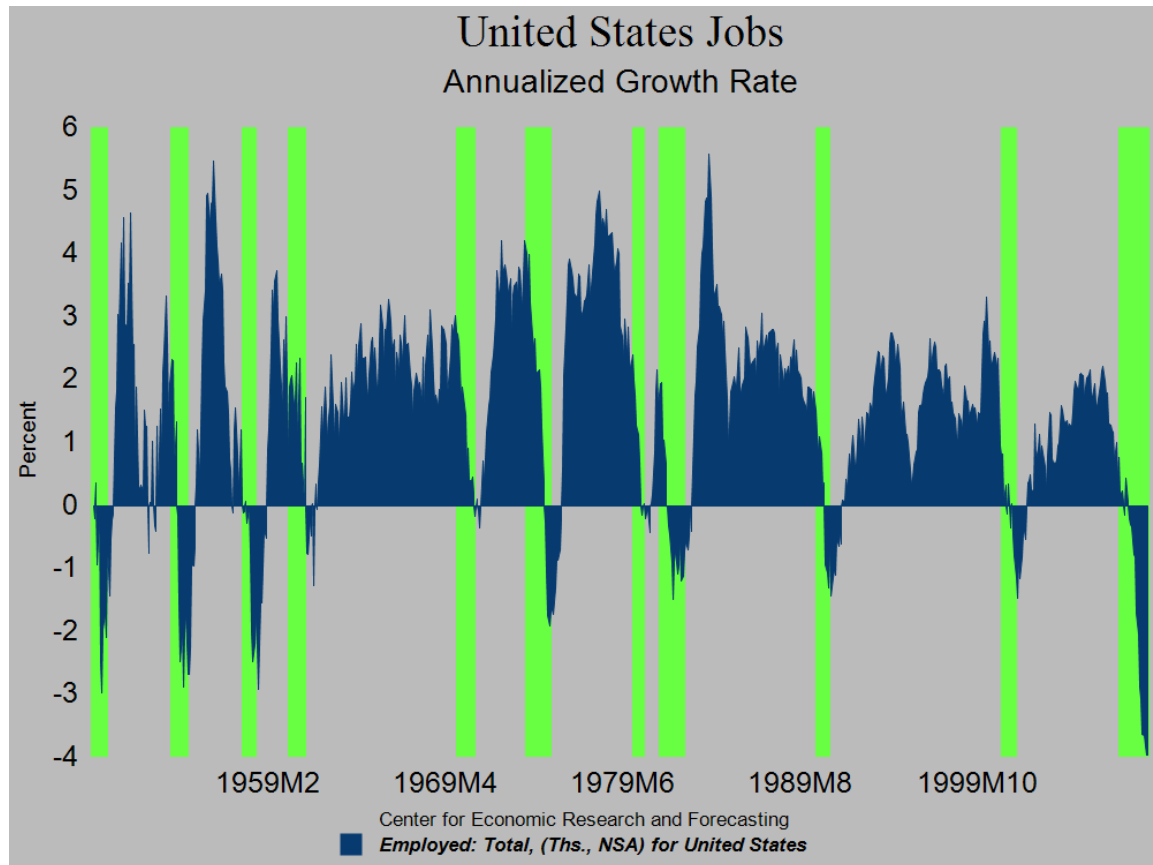
There are more problems with using one quarter of positive GDP growth, no matter how large, to declare the end of a recession.

I've placed a chart below that shows United States GDP data back to 1947's second quarter and shaded the recessions. Perhaps surprisingly, we've had periods of positive GDP growth in almost every recession, including the current recession, and some of those growth rates have been pretty high. Several recessions have had multiple quarters of positive GDP growth. A few have had multiple consecutive quarters of GDP growth. You could almost say that you need a period of sustained positive GDP growth to call the end of a recession, but the period between the early 1980's recessions could hardly be called sustained. I'd call them one recession.

It seems pretty clear to me that GDP data alone will not give you enough information to announce the end of a recession.



Maybe jobs data will help us. Here is a chart of the United States job data from January 1949 to present:



It is not immediately clear how these data will help us. It is hard to find patterns here. We've had recessions that were characterized by almost constant job losses. We've had recessions that had almost constant job gains, sometimes big job gains. In most, but not all, it looks as if job losses had peaked at the end of the recession. Indeed, no jobs were lost during the 1969-1970 or the 1960-1961 recessions. All job losses associated with these recessions occurred after the recessions were over!

Data revisions may be part of the problem. The people who call recessions, (National Bureau of Economic Research, NBER, a private non-profit organization), try to call recessions as quickly as possible; it is not real time, but it is close, usually within a year. Subsequent data revisions may mean that we are looking at data that is significantly different than the data they were looking at.

Another problem is that they refuse to give concrete definitions, preferring to look at a variety of indicators and using their judgment. In their words "...a recession is a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales."

That makes it difficult for an outsider to determine exactly what they are thinking. It leaves open the possibility of manipulation for political purposes. The NBER is presumably impartial, but the lack of a clear definition leaves them open to the charge.

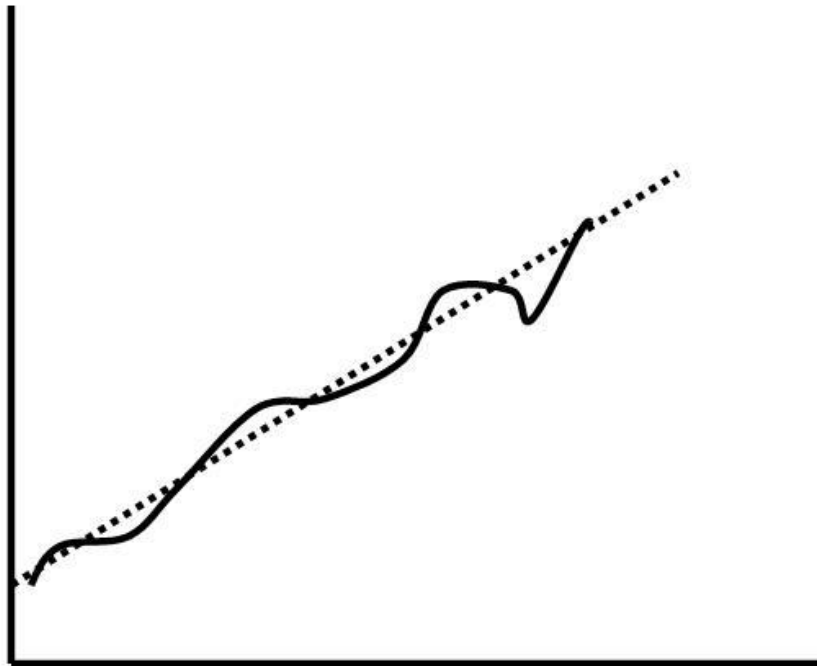
Their statement also doesn't rule out the possibility that the definition changes over time. After all, absent a rule, we are using people's judgment. A person's judgment may change over time, but here the people are changing all the time. It would be remarkable if the standard hasn't changed over time.

The recessions in the 1960s and the 2001 recession certainly look very different than the other recessions. Were they different recessions, or did the definition change? That could be an interesting research project, but it is beyond our scope. Each was pretty mild, in any event.

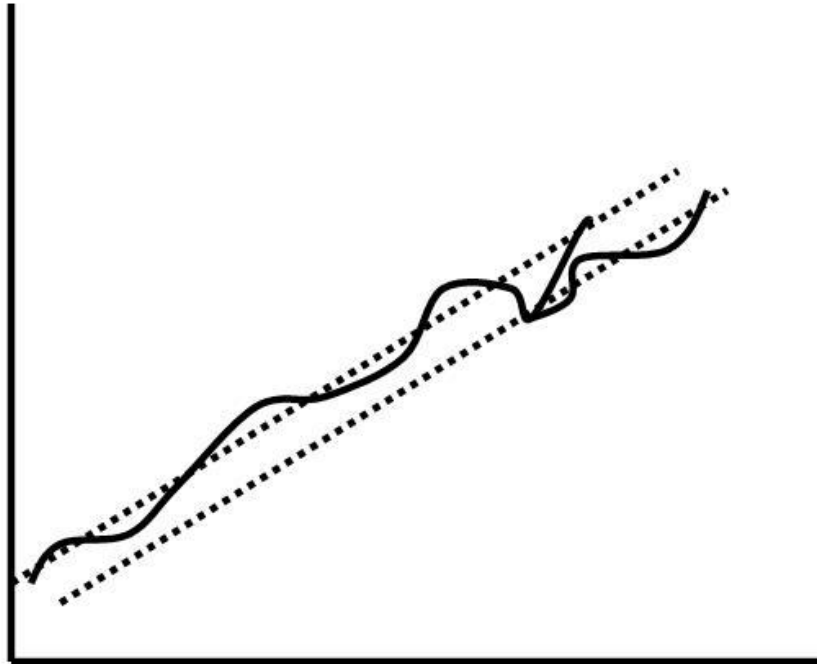
The current recession is not mild, and it looks to me as if calling the end of stronger recessions is easier. I'd say that the NBER will announce the recession is over when we have sustained economic growth and the rate of job losses has peaked.

There is something unsatisfactory about that definition. Job losses can continue in large numbers while the economy is in recovery according to the NBER. If you are the one losing a job, that makes no sense. That may be one reason that Richard Posner has proposed a different definition of a recession. He proposes that a recession is over "...when output rejoins the GDP trend line, that is, when it reaches the level it would have reached had the economy grown at its average rate of growth, rather than being depressed."

That would look something like this.



Unfortunately, that is not what happens. What happens is that the economy gets back to its original growth rate, but it may never get back to its previous growth line. It could look more like this:



Perhaps it would be more appropriate to say that the recession is over when output (Real GDP) has reached its pre-recession peak. Whatever the rule, I think we need one. The fact that we have to ask how we will know when the recession is over surely indicates a need for a standard definition.