ASKING MY ECON PROF WHAT RECESSION IS.

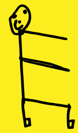
Artwork by Mr. Creasy

"GREGG" (2024), COURTESY CARBYNE GALLERY

Julian is a Professor of Economics at McGill University in Montreal.

This is Julian. 

And this is Emma.

Emma sat down with Julian to discuss what recession is and what it is not. 

E: So, let's cut right to the chase; what is recession?

J: That's one of the holy grail questions. I'll repeat what we both know, the technical mainstream economics definition. The technical definition, which I have to say, didn't strike me as right when I first learned it, is two quarters of negative economic growth or two months in which the economy is contracting rather than expanding. This is the dominant definition still in the news and mainstream orthodox economics.

I think that definition is far too narrow, and gives a misleading idea that there's somehow an automatic nature to the economy, that

“MBOYA” (2023)

it grows, and then there’s these kind of recessions that come every five years or longer. And this gives you the idea that they kind of automatically self-correct or if they don’t, that you have two quarters of negative growth and then the government can reduce interest rates or increase spending and get the economy back on track.

There’s a couple of problems with that definition. One is that it focuses too narrowly on a single number. So now when I think of two quarters of negative growth, or a contracting economy, I always thought it meant that fewer people are working or that the government is collecting less tax revenue.

But it could mean all sorts of things. It could mean that rising unemployment is going to trigger social problems. So the concentration on a single number is something to be concerned about.

For me, recession is something in which a small and growing part of the population is expecting a very terrible kind of stress, which is economic and financial stress. This means that suddenly in a country the size of the United States, if there’s a significant enough recession, it means millions of people are going to have trouble paying their bills.

E: To that point, how do we know we're in a recession? There's been a lot of speculation about that in American media as of late with terms like "Vibecession" cropping up on social media signaling a collective feeling of unease with the economy.

J: A very practical way to know just in general terms is using non-clinical language. Visibly you can see or hear about people who are losing their jobs. One interesting statistic in the States is that, two thirds of households live check to check, which is incredible. Or to use Elizabeth Warren's words, two thirds of households are one or two paychecks away from personal bankruptcy, or one or two medical problems away from personal bankruptcy. One indicator to know when you're in a recession, is the number of rising unemployment. For me, that would be more important than two quarters of negative GDP growth: if suddenly, there's a lot of involuntary unemployment. Another way would just be anecdotally, you're hearing around that people are losing their work and they're having trouble paying their bills. That's something that would be of concern.

For example, there's some talk of recession in Canada. I have a couple of things to note. One, central bankers, a lot of them, were saying that inflation in the wake of COVID was going to be temporary. And even before that, they were arguing that there wasn't going to be any inflation. They said it was going to be temporary when inflation started to accelerate. And then they said that actually, it's going to be more permanent, unless we increase interest rates and tighten policy.

At that time, warnings about recession started to come in the summer. For me, the last two years have seen a lot of talk in official circles about what's going on with the economy, inflation, and recession. It shows how little we know collectively about how the economy functions. Does it function in the midst of a crisis like COVID?

So I don't think we fully understand the complexity of a modern economy. When COVID struck and there was the shutdown, a lot of economists were telling politicians, “Don't worry, we'll just hit the reset button.” But it's not going to work like that. It's just way too complicated. It's like dropping your computer on the floor, and then it may not reset at all. And so there was a lot of errors and assumptions, before the

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financial crisis in the wake of the financial crisis, after the financial crisis, all the way up to COVID.

So I actually think the continual reliance and use of neoclassical economics, shows how little we know about how the economy functions, and how much we have to learn. This idea that we're predicting there's going to be a recession, despite the job numbers being continually strong, is a red flag for me. We're not even close to fully understanding the complexity of a modern day economy.

E: Then how do we explain the low unemployment rates?

J: So that's an important question. And it's a question that there's been a lot of misunderstanding about and I don't claim to fully know it myself. But when you look at the numbers in the United States, COVID was not just a lockdown of the economy in the wake of a pandemic, but it did change people's habits too. So we saw an increase in the rate of retirement, which was unexpected.

The idea that we hit a reset button and everything was going to go back to normal. That hasn't turned out to be true.

We've seen that some people have left the workforce, some people have taken retirement, all of which is greater than pre-COVID days. We see in Canada that the rate of retirement has definitely increased. So suddenly we find ourselves with a labor shortage. Some policymakers, not necessarily politicians... more so technocrats have been warning about a recession for a while. However, the jobs numbers are still strong in Canada, in the US and around lots of the West.

E: So, why is it that haven't we developed a system where we don't see recession?

J: Back in the early 2000s, there was this talk of a new golden era, there's going to be no more recession, it's going to be expansion.

We're heading into a new golden era, we've conquered inflation because there was no official inflation. Which doesn't mean there wasn't inflation, *there was lots of inflation.* But there was no officially measured inflation.

A few years later, the financial crisis kind of stripped down a lot of notions in economics. And it certainly killed the idea that we'd recession-proofed the economy. So why haven't economists developed?

This comes back to Robert Heilbroner and the way he approached economics. I think he's one of the greatest economic thinkers that's ever lived and something in his writings struck me, so I'll base my answer on his thinking and part of it on my own thinking. One of the reasons we haven't recession-proofed the economy is a reason that cuts both ways; it has a good side and a bad side. We've placed our fortunes in a market-oriented economy—a capitalist system—and the organizing principle of a capitalist system is the accumulation of capital. That's the whole point.

The organizing principle of medieval society in Europe was dynastic struggle. So the organizing principles of medieval Europe were control of the population through power and the threat of force. And the means of control was violence from the aristocracy and a kind of threat from the European church.

Beyond the power, the organizing principle of those societies was really the struggle for one dynasty over another between and within countries. There's a struggle within capitalism or the organizing principle of our system. Given that the organizing principle is the accumulation of capital, we've placed responsibility in economic stability in private markets. So it's this huge complicated orchestra of different sized companies and people across the world that are interacting, that are creating cycles. Because we have governments that step in and have macro policy, and during COVID we saw that the state stepped in and did the right thing, basically, the cycles in our economy are determined by the interaction of private agents: individuals, firms of all sizes. So it's hard to recession-proof that without moving to a more rigid kind of socialism, you'd have to really dampen the fires of capitalism.

You could create more stability, recession-proof, in the way that the Soviets did. But the whole system then becomes rigid, and it could collapse as their system did.