Special Commentary — August 4, 2022

Checking Recession Claims

Summary

Initial jobless claims have been trending higher since early April in one of the clearest signs that labor market conditions have begun to deteriorate. While jobless claims have a successful track record foreshadowing recession, we find continuing claims to be a better check on whether the economy is already in one. The recent trend in continuing claims adds weight to the argument that the economy is not currently in recession. That said, the recent uptick bears some resemblance to the months that preceded prior recessions, suggesting that the start of a recession may not be far off.

Economist(s)

Sarah House
Senior Economist | Wells Fargo Economics
Sarah.House@wellsfargo.com | 704-410-3282

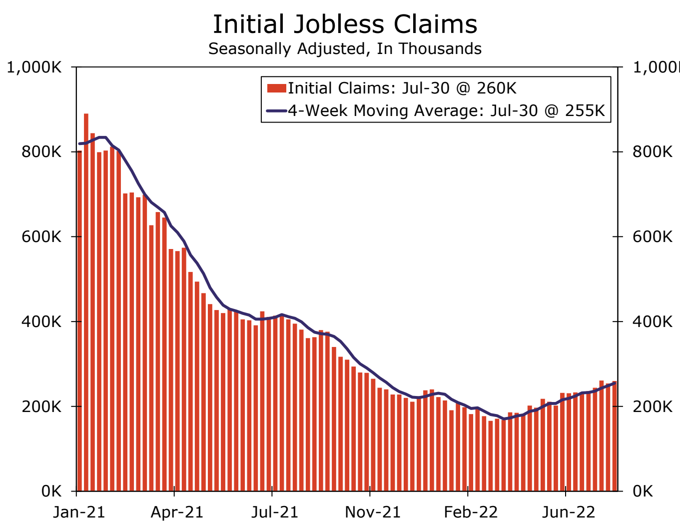
Michael Pugliese
Economist | Wells Fargo Economics
Michael.D.Pugliese@wellsfargo.com | 212-214-5058

Claim Check on Recession Timing

Back-to-back quarters of negative GDP growth have fueled the debate surrounding whether the U.S. economy is already in a recession. Labor market conditions currently offer the strongest evidence that the U.S. economy is not broadly contracting. Businesses are still struggling mightily to fill jobs, with half of independent businesses reporting at least one opening hard to fill. The unemployment rate, currently 3.6%, has held steady around its lowest point in 50 years for four consecutive months. Moreover, businesses have continued to add jobs at an impressive clip. In June, employers added 372K new jobs, little changed from job growth in April and May. This pace of hiring in June would have been the second-strongest month of job growth in the entirety of the previous expansion (excluding temporary Census hiring in May 2010).

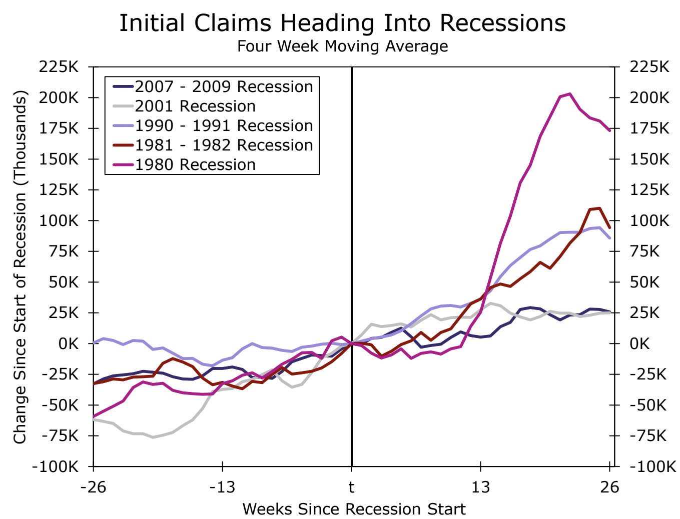
But the jobs market is not impervious to the slowdown in spending and investment already underway. Cracks have begun to show. Job openings fell for a third straight month in June, while postings in July slid further according to data from Indeed. Hiring plans among small businesses have also rolled over since last year. Perhaps most troubling, however, is that initial jobless claims are trending higher (Figure 1).

Figure 1



Source: U.S. Department of Labor and Wells Fargo Economics

Figure 2



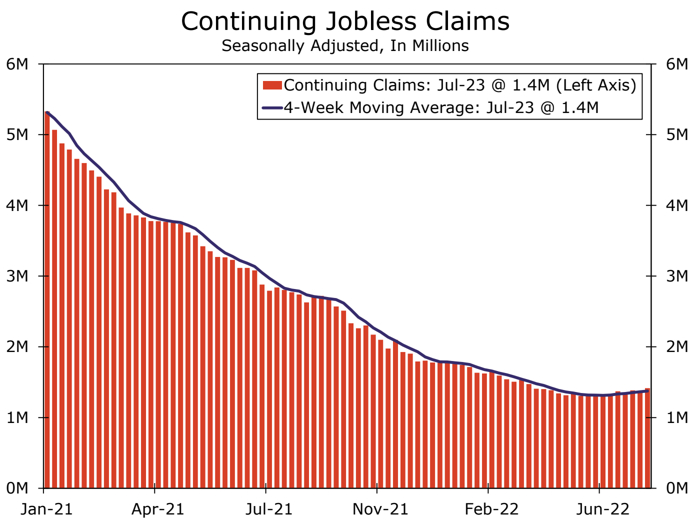
Source: U.S. Department of Labor and Wells Fargo Economics

Jobless claims are a tried-and-true favorite among economists for measuring stress in the labor market. Not only does weekly reporting make claims timely, but data are based on filings rather than surveys. As a result, claims data are not subject to multiple rounds of revisions the way nonfarm payrolls are. The prior week's data may be revised by a few thousand, and seasonal factors are updated annually. The adjustments, however, pale in comparison to payrolls, where revisions can sometimes paint a different picture from initial data. For example, payroll growth as reported on the eve of the 2007-2009 recession was cut by about half, from a gain of 115K to 55K after a year's worth of revisions. Had the payrolls data been this weak in real time, it would have been a more clear sign that hiring momentum was slowing acutely.

It is typical for initial jobless claims to trend higher months before the start of a recession (Figure 2), making the steady rise in claims since early April a worrisome signal for the economy's near-term growth path. Initial jobless claims edged back up to 260K in the final week of July, bringing the four-week average to its highest level since November.

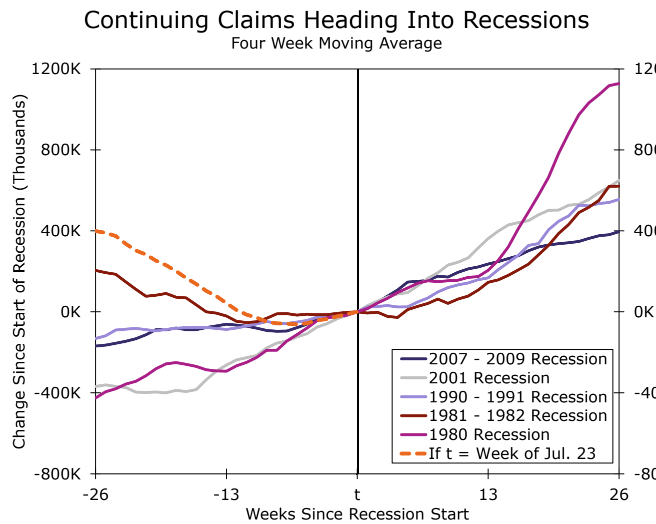
Continuing claims, which count workers' claims for *ongoing* unemployment, give clues to how quickly recently laid off workers are finding new employment. Through the week of July 23, continuing claims have started to edge up, but only slightly (Figure 3). In other words, recently laid off workers do not appear to be having too difficult a time finding new employment, offering evidence that despite some clear weakening, the labor market remains generally strong.

Figure 3



Source: U.S. Department of Labor and Wells Fargo Economics

Figure 4



Source: U.S. Department of Labor and Wells Fargo Economics

Continuing claims are more of a coincident indicator than a leading indicator of the business cycle. That makes continuing claims less effective at foreshadowing a recession, but useful in determining if the economy may already be in one. The path of continuing claims in recent months is not terribly different from the months preceding the prior recessions (Figure 4). While the potential for payrolls to be revised over the next few months or even year limit the conviction with which we can say whether the U.S. economy is in recession, continuing claims add weight to the argument that the recession clock has not started ticking. That said, continuing claims are starting to drift higher and, with the rise in initial claims, suggest the start of a recession might not be far off either.

Whether the U.S. economy may already be in a recession is likely to have minimal bearing on the course of Fed policy in the near term, however. With inflation still raging and FOMC members, including Chair Powell, acknowledging that an "over-tight" labor market is contributing to price pressures, we suspect the Fed will be undeterred by the recent slowing in activity both inside and outside the labor market, and it will push ahead with raising the fed funds rate to around 4% in the coming months.

Subscription Information

To subscribe please visit: www.wellsfargo.com/economicsemail

Via The Bloomberg Professional Services at WFRE

Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	704-410-3274	Jay.Bryson@wellsfargo.com
Mark Vitner	Senior Economist	704-410-3277	Mark.Vitner@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Shannon Seery	Economist	332-204-0693	Shannon.Seery@wellsfargo.com
Nicole Cervi	Economic Analyst	704-410-3059	Nicole.Cervi@wellsfargo.com
Jessica Guo	Economic Analyst	704-410-4405	Jessica.Guo@wellsfargo.com
Karl Vesely	Economic Analyst	704-410-2911	Karl.Vesely@wellsfargo.com
Patrick Barley	Economic Analyst	704-410-1232	Patrick.Barley@wellsfargo.com
Jeremiah Kohl	Economic Analyst	704-410-1437	Jeremiah.J.Kohl@wellsfargo.com
Coren Burton	Administrative Assistant	704-410-6010	Coren.Burton@wellsfargo.com

Required Disclosures