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October 03, 2019

"Markets are flashing deep red as investors worry about the health of the economy"
- CNN Business

"S&P and Dow Slide as Evidence of Global Slowdown Mounts"
- The New York Times

"Stocks Drop on Worries About Growth"
- The Wall Street Journal

The markets hit turbulence this week, with the Dow dropping almost 500 points on Wednesday, October 2.[1] Since recent reports have stoked new fears of a coming recession, I decided to write down my thoughts about what's happening and why.

For over a year now, economists have fretted about the possibility of a recession. The amount of evidence for one has waxed and waned, as good news and bad have jockeyed for attention. But recently, the signs in *favor* of a coming recession have started to light up in neon.

Before we get into that, though, it's useful to remember what a recession actually *is* – and what it isn't. Since the media tends to report every bit of news with breathless urgency, it's easy to let the *word* "recession" transform into a scary, supernatural bogeyman come to gobble up our economy. But what is a recession, really?

Economists define a recession in different ways, but here's the simplest way to look at it:

A recession is a significant decline in economic activity over an extended period of time.[2]

Let's break that down with a little Recession 101.

When economists refer to **economic activity**, they usually mean a country's **gross domestic product,** or GDP. This is a measure of the value of all goods and services a country produces every year. When a nation produces less, or when the value of what it produces drops, so too does the GDP. With that drop often comes a drop in employment, wages, corporate profits – and stock prices. As a result, consumers tend to spend less, which means less business is being done, which means less economic activity is happening. In other words, everything tends to *slow down*. Spending, lending, selling, making, building, investing. If this goes on for too long – usually at least two consecutive quarters – we're in a recession. Make sense?

The tricky thing about recessions is that it's almost impossible to know when they'll occur until we're already in one. After all, GDP is a measure of what *has* been produced, not what *will* be produced. That's why we tend to get a lot of false alarms when it looks like a recession may happen – and little warning when one *does* happen.

So. That's what a recession is. But why are experts worried about one now?

First, it has been a *long* time since the last recession. In fact, it's been over a decade! Since then, we've enjoyed one of the longest bull markets in history. Since the economy tends to move in cycles – a period of growth, followed by a period of stagnation, followed by a decline, rinse and repeat – many analysts have felt we're long overdue for the next one.

More important is the preponderance of data that suggests the economy is already slowing down. For example, on Tuesday, October 1, a new report showed that American manufacturing had slowed down for the second month in a row, dropping to its lowest level since 2009.[1] Other reports suggest the economy is adding far fewer jobs than in previous years. Combined with volatility in bonds, trade war uncertainty, and slower growth across the globe, and you can see why the horizon looks stormy.

That said, we've heard these tunes before. While parts of the economy *are* slowing, that doesn't guarantee a recession is coming next month, next quarter, or even next year. Consumer spending – perhaps the single biggest driver of the economy – has remained strong all year, and the unemployment rate remains very low.

When it comes to fears of a recession, none of these signs are catastrophic on their own. All these smaller issues just seem to be piling up on top of each other, enough to make everyone sit up and take notice. Here's how I look at it. Imagine you've had a very nice, reliable car for a long time. It's been strong, steady, and always gets you where you want to go.

Recently, though, you've noticed that the miles on your car are starting to show a bit. Your odometer is now over 100,000, a reminder that you've had your car for a *long* time. Furthermore, little problems are starting to pop up. That check engine light keeps coming on, even though you've had a mechanic look at it. The engine makes a funny noise whenever you turn the ignition, and is it just you, or are your brakes less responsive than usual?

None of these problems, on their own, would make you think your car is anything less than reliable. But put them all together…

That's where we're at with the economy. We may yet be able to wring a few more family trips out of it – but it's also time to start preparing for when it inevitably breaks down.

The effects of a recession

For the sake of discussion, though, let's say a recession *is* going to happen soon. What does that mean? How long do recessions last? And how bad do they get?

Every recession is different, but it's important to remember that we're not talking about another Great Depression here, or even another 2008-2009. If a recession happens, it doesn't mean everything will collapse. And if it happens, it certainly won't catch anyone unawares. Remember, experts have been stressing about this for a while.

Most recessions also tend to be mild in the grand scheme of things. Since 1940, the average recession has lasted just under eleven months, with the shortest being six months and the longest, eighteen.[3] On the other hand, make no mistake: Recessions can cause real economic pain for people. A slower economy means less spending, which means less profits, which means lower stock prices, which means lower wages, and worst of all, lower employment. And sometimes, even when a recession is technically over and the markets recover, it can take much longer for employment to get back to normal.

So, if a recession *is* coming, what should we do to prepare?

Great question! I love the word "prepare." You know what the definition is, right?

Prepare
verb
To make someone ready or able to do ***or deal with something.***[4]

So, how do we make ourselves ready to deal with a possible recession?

First, even the wealthiest of people should always have enough in emergency savings to cover at least six months' worth of expenses. This is also a good time to prioritize paying off short-term, high interest debts and evaluating your career security. If you need help with *any* of these things, please let me know.

Second, we need to remember that even though a recession will have an impact on the markets *in the short term*, we must always treat your portfolio for what it is: a long-term investment in your long-term future. That means we must not start making panicked decisions because we're afraid of short-term losses.

That said, if you are nearing the horizon on some of your long-term goals – like retirement, starting a business, building a house, whatever – then it may be prudent to start thinking more conservatively with your investments. After all, no one wants to get knocked off track right before the finish line. With 2019 winding down, it's time for us to have a complete review of your portfolio *and* your goals so we can update your financial plan as appropriate.

In other words, if a storm *is* coming, let's determine whether you can weather it, or whether it's time to "batten down the hatches."

Here's what I want you to do. If you have *any* questions or concerns about the markets, the economy, or a possible recession, please let me know! I want to address them, so that you'll continue to feel confident about working towards your goals.

In the meantime, please be on the lookout for a call from my office. My assistant will be reaching out to schedule a review with you.

It's impossible to know whether a recession is coming or not. There are signs for, and there are signs against. But regardless of when the next recession hits, let's remember that it's *not* a scary bogeyman. It's a slowdown in the economy – and it's not uncommon. Most importantly, let's remember that when it comes to the future, prediction is futile…but planning is not.

Have a great October!

Sincerely,

Bob Elliott

Robert G. Elliott, CFP
Vice President

[1] "U.S. Stocks Drop on Worries About Growth," *The Wall Street Journal,* October 2, 2019. https://www.wsj.com/articles/global-stocks-fall-amid-rising-fears-of-economic-slowdown-11570004904

[2] "Recession," *Investopedia.com,* May 6, 2019. https://www.investopedia.com/terms/r/recession.asp

[3] "List of recessions in the United States," *Wikipedia.org,* https://en.wikipedia.org/wiki/List_of_recessions_in_the_United_States#Great_Depression_onward

[4] "Definition of prepare," *Lexico*, https://www.lexico.com/en/definition/prepare