TEVIS INVESTMENT MANAGEMENT

What is “the economy”?

The economy is everyone’s favorite talking point, especially in an election year. And it seems sometimes that the more often the term is used, the less we know what it actually refers to. So let’s take a moment to consider what “the economy” actually is.

The shortest answer is gross domestic product (GDP), which refers to the total value of goods and services we produce. The government (via the Commerce Department) tracks this output and releases a report each quarter. The report is revised in subsequent months as more data becomes available (which is why you may see several, potentially different, numbers reported for the same period).

However, you can’t tell much about how well the average American is doing by looking at what the country collectively produces. And so experts lean heavily on other metrics—the *economic indicators* you hear about so often on the news.

Economic indicators

One of the most important indicators for experts (and regular Americans) is the unemployment rate. While there are multiple measurements for jobs, this looks specifically at the number of people who want to work but can’t find jobs.

The unemployment rate offers insights into how both companies AND regular folks are doing. Are employers able (and willing) to hire? And do Americans have jobs and income to pay for the goods and services that support the economy?

Other metrics include the consumer price index (CPI) which tracks inflation, trade numbers around what we’re importing and exporting, consumer sentiment, and more. Experts also track specific sectors of the economy, including agriculture, manufacturing, retail, and so on. Some of these, like retail and manufacturing, are watched more closely than others since they can have ripple effects.

The stock market can be thought of as an economic indicator, too. While you may have heard the refrain "the stock market is not the economy," the two are related. Corporations not only produce goods and services, they also hire smaller businesses and provide employment. And the stock market can provide some insight into how these companies are doing.

One catch, however, is that stock prices can be influenced by more factors than just the underlying health of the company.

Growth and recession

While we tend to focus on how the economy is doing in the short term (for good reason!), one important consideration: In the long term, the economy expands. As the human population grows, so too do the goods and services we create. Advancements in trade and technology increase our productivity, and we expand production. But this type of expansion happens in cycles, and growth is periodically offset by recessions.

Historically, a recession occurred when GDP shrank for at least two quarters, but as we've seen, there are so many more factors to consider when taking a big picture look at the economy. Because of that, the National Bureau of Economic Research (NBER, or the people who officially declare a recession) updated their criteria. Now, the NBER says:

> *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.*

A depression is an enhanced recession. There is no specific criteria that moves a recession into depression territory, but experts look for markers like economic decline of more than 10% or unemployment above 20%. (Both occurred during the Great Depression.)

The global economy

You may have noticed that the economy (and stock market) here moves thanks to events a half a world away. For instance, war in the Middle East might drive up the price of oil, which in turn drives up gas prices here and affects how consumers spend or save.

These days, everything is connected. But while there is technically a world economy that uses the international exchange of goods and services, as valued by different currencies, to track how the globe is doing…it's about as complicated as it sounds.

Generally, when people refer to the global economy, they're simply referring to economies across the globe. A global recession occurs when multiple economies across the world experience the same type of slowdown. Because countries trade heavily with each other nowadays, this is more likely than not.

Personal economy

One of the most common refrains I hear when people talk about the economy is: “I just don’t see it.” Often, the numbers we hear on the news don’t translate to what we experience in our daily lives.

Take the record bull market that ended in 2020; it started in 2009, long before jobs and the overall economy bounced back from the Great Recession. Or consider the dot-come bubble bursting. That triggered a brief recession, but retail sales that year remained strong.

That’s not to say headlines aren’t helpful. If there’s risk of a recession, we may want to pay more attention to our spending and cut back on unnecessary expenditures to pad the emergency fund. But what’s more important is having a plan to meet your personal goals. We build financial plans to account for ups and downs in both the economy and the market. And we pay attention to the minutia so you can focus on living your life well in the meantime.

Questions on your plan or the current state of the economy? Let’s discuss at our next meeting.