**Economic Recession**

Student Full Name

Institutional Affiliation

Course Full Title

Instructor Full Name

Due date

**Introduction**

Recession can be defined depending on Shiskin’s rules of thumb, or the National Bureau of Economic Research (NBER) definition. They both consider recession to be a result of the decline in a country's economic activity for a given period and measured in GDP (Rodeck, 2022). It results to drop in consumer spending and turn result in cutbacks in production, manufacturing, and job, which prompts income loss that spreads from one sector to another and across the country, hurting sales and leading to more decreased production. Rodeck (2022) states that recession can be predicted by checking on indicators such as rising unemployment, sudden stock market decline, drop in Leading Economic Index, decrease in consumer confidence, and the inverted yield curve. This paper explores what recession is, why it happens, its consequences, and its impact on the economy and businesses.

**Recession and Why It Appears**

World Economic Forum (2022) defines recession as two successive quarters of decreasing gross domestic product. NBER recognizes recession as an economic deterioration that lasts several months and affects the nation’s economy, real GDP, real income, employment rates, industrial production, and evident in wholesale-retail sales (Rodeck, 2022). NBER recognizes economic decline as an actual recession until 6-18 months after the recession starts (Tretina, 2022). According to Rodeck (2022), a recession is declared when a country’s economy experiences decreasing measures of manufacturing and income for an increased period, declining retail sales, increased unemployment, and negative GDP. As Tretina (2022) indicates, NBER declares recession after checking on consumer spending, industrial production/manufacturing, employment, and personal income.

There are numerous ways through which recession is likely to happen, including economic shocks, uncontrolled inflation, excessive deflation, asset bubbles, excessive debt, and technological change. A sudden economic shock, such as the outbreak of coronavirus, is a negative, unexpected, and external event that disrupts economic expansion creating financial damages, which may lead to economic decline and recession if the decline lasts for months (Rodeck, 2022). A recession also happens when a country takes on too much debt in a way that makes the cost of repaying the debt grows to a point where a nation cannot pay it back. Another cause of recession is asset bubbles. In essence, this is where investors become too confident during a sturdy economy, which puffs up the stock market, and panic selling can damage the market leading to recession when the bubble bursts.

Excessive inflation can also lead to recession where central banks increase interest rates to regulate inflation, but higher rates depress economic activity resulting in recession. High deflation can also cause recession due to a decline in wages which depresses prices making individuals and businesses halt spending hence undermining the economy and leading to recession. Technology change increases productivity and supports the economy, but industrial revolutions such as robots and AI make the entire profession obsolete, which triggers recession due to an increase in unemployment caused by new inventions (Rodeck, 2022). The classical model theory explains that changes in the real wage have two effects, the substitution effect, which induces more workers to work for long hours or enter the workforce, and the wealth effect which increases wealth and reduces the incentive to work (Knoop, 2015).

**Recession Consequences and Impact on Economy and Business**

Consequences of recession include health problems such as depressive and anxiety disorders, and economic crises such as financial crisis, housing crash, employment loss, and economic decline (Wallace et al., 2022; Guerra & Eboreime, 2021). Tretina (2022) indicates that recession leads to income stagnation as employer slashes employees' working hours or reduce the workforce, which highly impacts the middle and lower classes. Wallace et al. (2022) found that recession leads to income inequality where its aftershock erodes the income shares of middle, working, and poor classes have no effect on upper-middle-class households, and increase income share for upper-class households. Cutting back employees for companies to reduce expenses increases the percentage of the total unemployed labor force but actively seeking work (Tretina, 2022). Another consequence of the recession is cutting back on consumer spending, and production and manufacturing, which decreases exports and economic activity, leading to economic decline. Wallace et al. (2022) indicate that economic deterioration is the level of inflation-adjusted GDP per capita comparative to pre-recession highest levels. Guerra and Eboreime (2021) state that not only does recession lead to housing issues or displacement, resource losses, and financial losses, but it also leads to specific psychological problems such as anxiety, depression, and trauma-related disorders.

Technology, capital, and labor are the factors that determine real output in the classical model, and they affect aggregate supply (Wallace et al., 2022). Recession influences these factors leading to the decline of macroeconomic indicators such as gross domestic product, inflation, business profits, household income, capacity utilization, and investment spending. Classical theory assumes that market forces automatically operate in the private enterprise system and supply creates its demand (Wallace et al., 2022). Therefore, according to the theory, deficiencies in effective demand such as ones caused by recession including unemployment results in an economic downturn reduced profits, decreased product quality, declined stock prices and dividends, credit crunch, and reduced cash flows. One consequence of the recession is reduced consumer spending, which makes it difficult for businesses to generate sales and invest in new products (Tretina, 2022). Business creditors also introduce new measures such as lending requirements that make it difficult for businesses to access credit. Again, recession impact cash flows due to reduced consumer spending delayed supplier payments and difficulties for consumers and vendors to make timely payments. Reduced cash flow and business profits reciprocate in business financial statements leading to decreased dividends and stock prices.

**Conclusion**

A recession hurts households and individuals due to increased living costs, reduced working hours or job loss, and challenges getting a job; businesses also make less sales, and the nation's total economic output decreases. The business cycle can explain how recession happens where it explains that during an economic expansion, lenders make it less expensive and easier for people and industries to increase debts. Then irrational exuberance goes beyond asset prices, and as the development ages, debt loads and asset prices increase. Consequently, one of the phenomena disrupts the economic expansion leading to shock that makes debts too expensive to maintain, stock market crashes, and asset bubble bursts making the economy entered recession.

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