

## State of Play

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21 April 2022

**As the International Monetary Fund (IMF) downgrades their global growth forecasts, does this mean recession is a possibility?¹ The cost-of-living and the Ukraine crises appear to have already started to slow the economy given the evidence from last week's data leading to a lack of market direction. Our Investment Specialist, Simon Durling, shares his thoughts in this week's State of Play.**

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### Slowing global growth

The IMF has said this week in their latest Global Economic Growth Forecast¹: 'The war in Ukraine has triggered a costly humanitarian crisis that demands a peaceful resolution. At the same time, economic damage from the conflict will contribute to a significant slowdown in global growth in 2022 and add to inflation. Fuel and food prices have increased rapidly, hitting vulnerable populations in low-income countries hardest. Global growth is projected to slow from an estimated 6.1% in 2021 to 3.6% in 2022 and 2023. This is 0.8% and 0.2% lower for 2022 and 2023 than projected in January'. Their report identifies the significant impact the conflict will have on the wider economy and the knock-on effect on commodity and energy prices. These dramatic increases are likely to cool demand, and therefore slowing economic activity in the process. The UK is predicted to be the lowest growth of the G7 nations next year in the revised numbers. The next question on investor's minds may be whether this will lead to a recession?

## Risk of recession

Importantly let's be clear, technically, a recession is described as two consecutive quarters of contraction as measured by economic output known as Gross Domestic Product (GDP).<sup>2</sup> GDP measures if and how much the economy is growing at a certain point in time, typically over one month, a quarter or one year. The UK Government website provides an excellent description of how this is calculated: 'GDP measures the total value of all of the goods made, and services provided, during a specific period of time. Goods are things such as your new washing machine, or the milk that you buy. Services include the haircut from your hairdresser, or repairs done by your plumber. It's only final goods and services that are sold to you and me that matter for GDP though. So, if some tyres roll off a production line and are sold to a car manufacturer, the value of the tyres isn't included in GDP, it is reflected in the value of the car. The amount you pay, or the market value of that good or service, is what's important as these are added together to get GDP.'<sup>2</sup> Their site goes on to explain that 'there's more than one way of measuring GDP. Just imagine trying to add together the value of everything made in the UK – that's no easy feat, which is why there is more than one way of measuring GDP.

GDP is calculated in three ways, adding up:

- all the money spent on goods and services, minus the value of imports (money spent on goods and services produced outside the UK), plus exports (money spent on UK goods and services in other countries)
- the money earned through wages and profits
- the value of goods and services produced

These are known as the expenditure, income, and output measures of GDP, respectively. All three different methods of calculating GDP should, in theory, give the same number.<sup>2</sup>

The latest UK GDP data released last week by the Office for National Statistics for February 2022 showed that the economy has slowed significantly since January.<sup>3</sup> However it is too early to tell whether this will lead to a widespread reduction in economic output. Certainly, investors are likely to be very sensitive to new evidence. For example, take this week's report from Kantar, a data insights and consulting company, which reported that 1.51m subscription video on demand (SVoD) services were cancelled by households in the first quarter of 2022.<sup>4</sup> They cited that the main reason for cancellation in their research was due to the cost-of-living crisis. The proportion of consumers planning to cancel SVoD services with the primary reason stating 'wanting to save money' has risen to its highest level ever at 38%, up from 29% in last quarter of last year.<sup>4</sup>

The risk of recession will in many respects depend on whether central banks continue with the interest rate rises they have recently signposted as they try to tackle rising prices. Clearly, if inflation cools economic activity and

consumer spending without further interest rate rises, then any additional interest rate increases risk tipping the balance and may lead to a contraction within the economic cycle.

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## The economic cycle

**Learn more**  
Tune in or read about the Principles of Investing [here](#).

The global and local economy travel through a natural economic cycle defined by different phases. These four stages are expansion, peak, contraction, and trough.<sup>5</sup> It can be very important for investors, particularly professional investors, like fund managers, to understand and identify in which phase of the economic cycle we have reached. They achieve this by assessing several factors including consumer spending, interest rates, total employment, and GDP. Importantly each economic cycle is different in length and has varied greatly over history.<sup>6</sup> The most recent economic cycle that concluded with the recession triggered by the global pandemic was the longest expansion ever recorded from just after the financial crisis in 2008 until COVID-19 forced the world into lockdowns, triggering a sharp downturn.<sup>6</sup> In the current, much shorter cycle, my own observations are that we are already towards the end of the expansion phase as economic activity cools and the risk of potential recession looms.

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## Market update

According to Refinitiv, of the 49 companies in the S&P 500 that have reported earnings so far in 2022, 79.6% reported above analyst expectations compared to a long-term average of 66%.<sup>7</sup> At the time of writing US stock markets were rising against a backdrop of concerns about a combination of rising yields, with US 10-year rates close to 3%, and signs last week that the yield curve has inverted, where short-term rates were higher than long-term rates, which can indicate a potential future recession.<sup>8</sup> The US market appears to be an outlier as European markets fell due to ongoing concerns about the Ukraine crisis and the impact of rising prices which is expected to get worse before it eases later in the year.<sup>8</sup>

**Find out more!**

Listen [here](#) to our latest Market Views from our Head of Systematic Research for TAA and Alpha, Stefano Amato, as he shares his thoughts on recent volatility within investment markets.

Note: Data as at 19 April 2022.

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<sup>1</sup> International Monetary Fund, 19/04/2022

<sup>2</sup> UK Government, 26/07/2017

<sup>3</sup> Office for National Statistics, 31/03/2022

<sup>4</sup> Kantar, 19/04/2022

<sup>5</sup> Investopedia, 3/02/2022

<sup>6</sup> Forbes, 21/01/2020

<sup>7</sup> Refinitiv, 20/04/2022

<sup>8</sup> Investing.com, 19/04/2022

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