The Daily Dish

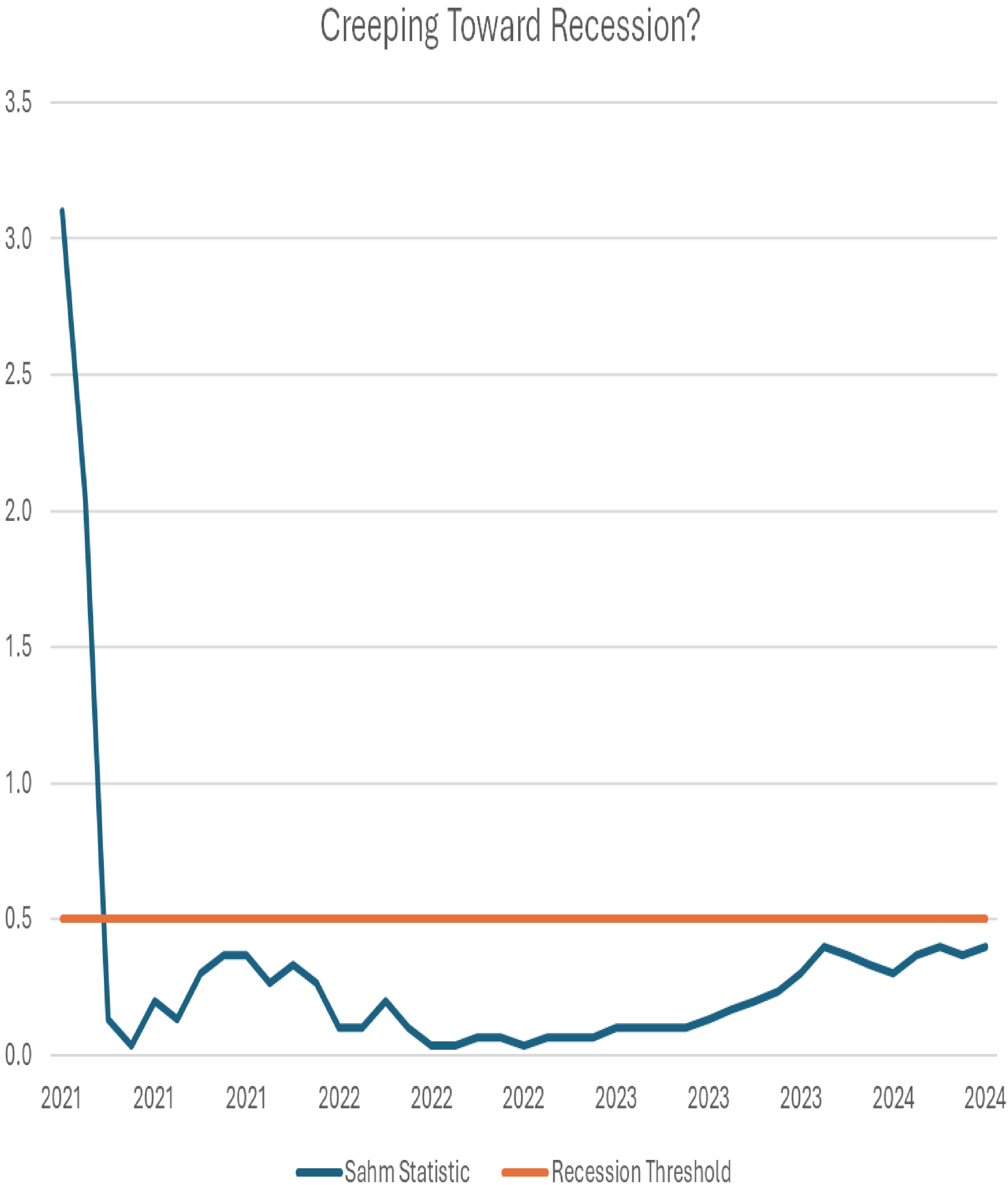
Sahm Evidence on Recession Risks

DOUGLAS HOLTZ-EAKIN | JUNE 21, 2024

A while back Eakinomics took a look at the Sahm Rule and recession risks. The Sahm Rule compares the three-month moving average of the unemployment rate with the low over the previous 12 months.?If the difference is more than 0.5 – one-half a percentage point – the economy is entering a recession.

It seems a useful time to check in on the Sahm Rule. There have been several relatively weak economic reports over the past two months. Is the labor market telling us something as well?

The graph shows the Sahm statistic – three-month moving average minus low rate in previous 12 months – versus the 0.5 threshold. The last time Eakinomics wrote on the rule, the statistic had reached 0.4, and it is at that level again. Indeed, if the next employment report features another 4.0 percent unemployment rate, it would rise to 0.5.



But stepping back, it seems the larger lesson is that the labor market has been under continuous and substantial stress since the final quarter of 2023. This has caught the attention of Claudia Sahm, inventor of the rule, who argued in this recent CNBC interview: “My baseline is not recession. But it’s a real risk, and I do not understand why the Fed is pushing that risk. I’m not sure what they’re waiting for.”

These data reinforce Eakinomics’ view that the Fed is well-positioned to cut rates. If the economy holds up, it will be able to cut pre-emptively after the election. But if conditions on the ground deteriorate materially, it can cut prior to the election without fear of being accused of trying to tip the electoral balance.