

# ***The world economy in recession***

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## **Abstract**

**A global recession is a prolonged period of economic decline around the world. A global recession involves more or less synchronized recessions in many national economies, as trade relations and international financial systems transmit economic shocks and the impact of the recession from one country to another. Macroeconomic indicators must decline for a significant period of time to be classified as a recession. A global recession marks an extended period of economic decline in numerous national economies, interconnected through international trade relations and financial systems. Understanding the concept of a global recession is vital because it can significantly affect the world economy. It is essential to note that the definition of a global recession does not come with an officially specified duration. Understanding global recessions is essential because they can affect various aspects of economies, especially international trade and financial markets. By analyzing historical examples of global recessions, policy makers, investors and businesses can make more informed decisions regarding risk management, economic policies and investment strategies.**

**Keywords: GDP per capita, macroeconomic indicators, international trade, financial markets, economic policies, investment strategies.**

## **Introduction**

New disruptions in energy supply are weighing on growth and fueling inflation, particularly in Europe where activity could fall by a further 1.25 percentage points and inflation rise by 1.5 percentage points, so many countries could be stuck in recession during 2023. Although much less dependent on imported energy than Europe, the US is also sliding into crisis as the central bank raises interest rates to curb inflation.

Increasing concerns about global market stability with all equity markets returning to recent lows, last week's US interest rate hike, combined with the Italian election and geopolitical fears across Europe sent the dollar higher, falling below 0, 97 against the euro, crude oil below \$85 a barrel, container shipping costs from China to the West are in free fall.

There is no doubt that volatility in commodity markets will continue. Few commodities are immune to the global recession, and processors are uncertain about consumer demand and fear prices will remain high for too long.

## **1. Criteria for Recession Recognition**

The first step in assessing the occurrence of a global recession is to assess macroeconomic indicators such as gross domestic product per capita (GDP), trade, capital flows, industrial

production, oil consumption, unemployment rate, investment per capita resident and per capita consumption. The IMF uses purchasing power parity (PPP) to calculate the aggregate output of countries instead of exchange rates because of the complexity involved in managing different currencies around the world:

While some definitions specify a minimum length of time for a recession, the IMF does not set a fixed duration for global downturns. This is because individual economies may recover at different rates, making it more complex to define a global recession based on a specific time frame.

The extent and severity of the impact of a global recession on a country depends on several factors, including trade relations with other nations and the sophistication of financial systems. The interconnectedness of economies through trade and financial linkages can facilitate the transmission of economic shocks from one region to another, leading to contagion effects that contribute to a global recession.

A notable example of a global recession was the Great Recession of 2008, which involved an economic downturn that affected many countries around the world. During this period, global trade fell by over 15% between 2008 and 2009. The effects vary among nations: while the United States, with limited trade relations relative to its domestic economy, saw a large stock market correction and a significant increase in unemployment, countries such as Germany, which have extensive manufacturing sectors and global trade relations, experienced significant negative impacts regardless of their domestic economic strength.

The effects of the Great Recession persisted for many years in various forms, with some economies recovering more quickly than others. Understanding the nature and implications of global recessions is critical because they can have lasting effects on individual economies and the world economy as a whole.

US interest rates are now at their highest level since 2008, and the market is already expecting a further 75 basis point rate hike at the next meeting, with speculation that they could be around 4.5 percent by the end of the year.

At one point the markets were in turmoil; a rise in interest rates seemed to be a "bullish" signal for markets and commodities and that the economy could withstand this rise in interest rates, which would be a signal that economies are healthy. Speculators viewed commodity purchases as a hedge against further inflation, but that view quickly changed to fear of a recession due to the expected further rise in interest rates to correct what they assumed was only "transient inflation".

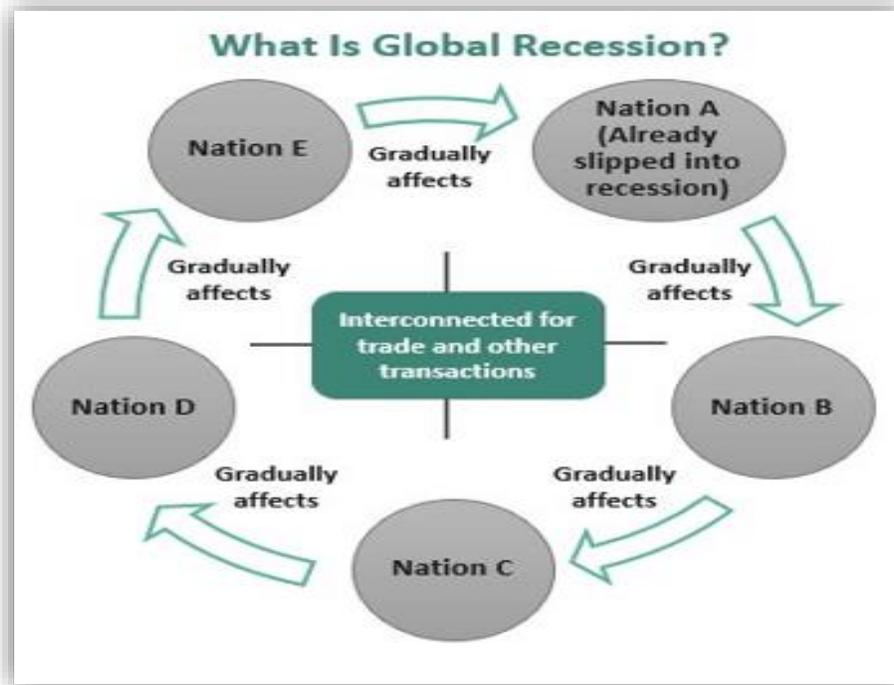
Central banks are now fully aware that they must first hurt the economy to actually fix it. The Fed is trying to tighten its monetary policy quickly and intensively to bring inflation under control, and they expect inflation to fall to 2 percent in 2025.

By comparison, Paul Volcker, the chairman of the US Federal Reserve in the 1980s, in order to fight inflation that was around 13 percent, raised interest rates to over 20 percent, only to reduce them to three percent in the next two years in order to revive the economy. Therefore, it is not surprising that the relationship between the euro and the dollar is at its lowest level in the last 20 years. More than the strength of the dollar itself, it is likely that the political, energy, military and economic crisis in the EU is pushing the euro into the abyss.

What does the European Central Bank say about all this? They expect that inflation may continue to rise in the short term, despite rising interest rates, and that they should rise further. A recession alone will not be enough to quell rising prices. The market expects that by spring interest rates could be above 2.5 percent (currently 0.75 percent).

## 2. Characteristics of the recession

Global recession refers to the economic slowdown observed in various nations around the world. While a recession affects one country at a time, its prolongation seriously affects other economies associated with the affected one. Such events lead to an increase in the unemployment rate and an increase in the price and consumption of goods, such as oil, investments per capita, etc. As countries recover from recession, they are becoming more efficient than ever:<sup>1</sup>



The growth of the world economy is slowing down more than expected, and the energy crisis and inflation increase the risk of recession in large economies, especially in Europe, the Organization for Economic Cooperation and Development (OECD) warned.

The world economy will grow by three percent this year, in line with previous estimates, but activity slowed in the second half of the year, the OECD said, forecasting a growth rate of 2.2 percent for 2023, which is 0.6 percentage points lower than what they calculated in June.

World GDP this year will be \$2.8 trillion lower than the OECD forecast published last December, before the Russian-Ukrainian war, expressed in terms of purchasing power parity and prices from 2023.

"The global economy weakened after Russia's unprovoked, unjustified and illegal war of aggression against Ukraine." GDP growth has stalled in many countries, and economic indicators signal a prolonged slowdown," said OECD Secretary General Matthias Cormann.

<sup>1</sup> WallStreetMojo, (2024), Global Recession - Meaning, Examples, Causes, <https://www.wallstreetmojo.com/global-re>.

The forecasts are especially pessimistic for Europe, which is most directly exposed to the consequences of the Russian war in Ukraine. The OECD predicts that economic growth in the euro zone will slow from this year's 3.1 percent to just 0.3 percent in 2023, meaning that the 19 countries in the area of application of the common European currency will spend at least part of the year in recession, with two consecutive quarters of declining activity. In June, the OECD forecast activity growth of 1.6 percent for the euro area in 2023.

The German economy, depending on the import of Russian gas, will see a decline in activity by 0.7 percent next year, OECD calculated. At the beginning of the summer, they forecast a growth of the largest European economy of 1.7 percent. In the group of the four largest economies of the Eurozone, the activity should grow the strongest in Spain, by 1.6 percent.

The forecast for the USA in the next year has also been significantly reduced, from 1.2 to 0.5 percent. This year, the largest European economy should grow by 1.5 percent, which is a whole percentage point weaker than the summer forecasts.

And China's economy is set to grow this year much weaker than previously expected, by just 3.2 percent, due to strict measures to combat Covid-19. In 2023, activity is set to accelerate to 4.7 percent.

They confirmed the forecast of 6.9 percent growth of the Indian economy this year. In the next year, they forecast a slowdown, with a forecasted growth rate of 5.7 percent.

The war in Ukraine has significantly increased energy and food prices, further intensifying inflationary pressures at a time of continued strong growth in the cost of living worldwide.

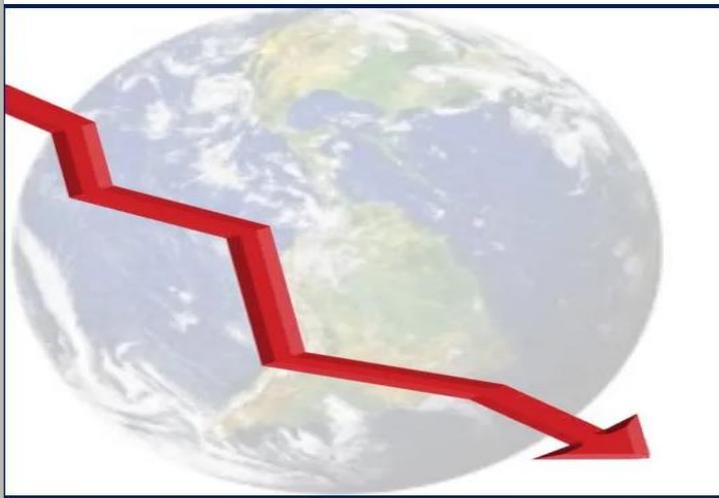
### **3. Impact of the recession on the economy**

A global recession is a recession that spans the entire world. It is a period of global economic decline. According to the IMF, macroeconomic indicators that point to a global recession include a decline in oil consumption, capital flows, trade, industrial production and rising unemployment. In other words, a decline in global output must coincide with a weakening of those indicators for there to be a global recession:<sup>2</sup>

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<sup>2</sup> Market Business News, (2024), Global recession – definition and meaning - Market Business News, <https://marketbusinessnews.com › financial-glossary>.

# What is a Global Recession?



*Economic slowdown*

*Falling oil  
consumption*

*Declining capital flows*

*Weakening industrial  
production*

*Rising unemployment*

*Slowdown in GDP per  
capita growth or  
contraction*

***A Global Recession is a sustained economic downturn  
that affects several countries across the world.***

New energy supply disruptions will weigh on growth and boost inflation, particularly in Europe where activity could fall by a further 1.25 percentage points and inflation rise by 1.5 percentage points, so many countries could be stuck in recession through 2023. Although much less dependent on imported energy than Europe, the US is also sliding into crisis as the central bank raises interest rates to curb inflation.

Aggressive tightening of monetary policy could push the economy into a deeper recession, economists there fear.

Technically, the US economy is already in recession, given that it has been falling on a quarterly basis for the last two quarters, but for now this recession is "shallow".

Even at the cost of a sharp slowdown in economic growth. Thus, the Fed cut its estimate for growth this year to just 0.2 percent, while previously estimating that the economy would grow by 1.7 percent. In the coming years, the average growth could be 1.8 percent.

Despite the significantly deteriorating outlook for major economies, the OECD believes central banks must raise interest rates further, forecasting they will exceed four percent in 2023 in most countries in the group.

Many governments are allocating more and more money to help households and businesses, but that help should go to those who need it most and must be temporary to reduce spending and further increase debt, they say.

Germany, which is one of the largest economies in the world, has now officially slipped into recession.

The latest official figures for Germany show negative growth for two consecutive quarters.

In Britain, the unemployment rate is the highest in more than a decade, and the largest British telephone company, BT, has cut 10,000 jobs.

The figures show that in the third quarter of this year, the German economy shrank by half a percent, which is more than expected.

Germany now has negative growth for the second consecutive quarter, which technically means the country is in recession.

For Europe's largest economy, the decline came as a shock.

Earlier this year, German politicians and business leaders predicted that the economy was strong enough to withstand any credit crunch that loomed.

But Germany is very dependent on its exports and the demand for it has fallen.

Even if you make the best cars and the best machine tools in the world, if there's a global recession, buyers can't afford them, and that's a major blow to manufacturers in Germany..

#### **4. Causes of the recession**

A recession is a significant decline in economic activity that lasts for months or even years. Experts declare a recession when a nation's economy experiences negative gross domestic product (GDP), rising levels of unemployment, falling retail sales, and declining measures of income and output over an extended period of time. Recessions are considered an inevitable part of the business cycle—or the regular cadence of expansion and contraction that occurs in a nation's economy:<sup>3</sup>

- During a recession, the economy struggles, people lose their jobs, companies make fewer sales, and the country's overall economic output declines. The point at which the economy officially falls into recession depends on a variety of factors.
- There is more than one way to start a recession, from a sudden economic shock to the consequences of runaway inflation. These phenomena are some of the main drivers of the recession:
  - ✓ Sudden Economic Shock: An economic shock is a sudden problem that creates serious financial damage. In the 1970s, OPEC cut off oil supplies to the US without warning, triggering a recession. The coronavirus outbreak, which has shut down economies around the world, is a more recent example of a sudden economic shock.
  - ✓ Excessive Debt: When individuals or businesses take on too much debt, debt servicing costs can rise to the point where they cannot pay their bills. Rising debt defaults and bankruptcies then turn the economy upside down. The housing bubble in the middle of the period leading up to the Great Recession is a prime example of excessive debt causing a recession.
  - ✓ Asset bubbles: when investment decisions are driven by emotion, poor economic performance is not far behind. Investors can become overly optimistic during a strong economy. The former chairman of Irrational Exuberance inflates bubbles in the stock market or real estate - and when the bubbles pop, panic selling can crash the market, causing a recession.

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<sup>3</sup> Forbes, (2024), Recession Definition: What Is A Recession? <https://www.forbes.com › advisor › investin>.

- ✓ Too much inflation: Inflation is a steady, upward trend in prices over time. Inflation in itself is not a bad thing, but excessive inflation is a dangerous phenomenon. Central banks control inflation by raising interest rates, and higher interest rates reduce economic activity. Runaway inflation was an ongoing problem in the United States in the 1970s. To break the cycle, the Federal Reserve quickly raised interest rates, causing a recession.
- ✓ Too much deflation: While uncured inflation can create a recession, deflation can be even worse. Deflation is when prices decrease over time, which causes wages to decrease, which further decreases prices. When the deflationary feedback loop gets out of hand, people and business stop spending, which undermines the economy. Central banks and economists have few tools to fix the underlying problems that cause deflation. Japan's struggles with deflation for most of the 1990s caused a severe recession.
- ✓ Technological change: New inventions increase productivity and help the economy in the long run, but there may be short-term adjustment periods to technological breakthroughs. In the 19th century, there were waves of labor-saving technological improvements. The Industrial Revolution made entire professions obsolete, causing recessions and hard times. Today, some economists worry that artificial intelligence and robots could trigger a recession by eliminating entire categories of jobs.

## 5. Impact of the recession on the economy

A recession means that there has been an economic contraction—or "negative growth"—of gross domestic product (GDP) for at least two consecutive quarters. To break it down, GDP is the total value of goods and services produced over a period of time. When it goes down - negative growth or economic contraction - it doesn't go well. And when it doesn't do well for six months, it counts as a recession:<sup>4</sup>

What happens during a recession?

- During a recession, less money circulates: less money for workers from their employers, less money spent in stores and restaurants, and less money going to the government as payroll taxes to pay for things like benefits and public services.
- As employers look to save, people may find it harder to find work or get a raise. As businesses and shops close or downsize their workforce, people may lose their jobs.
- Getting a mortgage or loan during a recession will prove difficult as banks tighten their lending criteria.
- Recent discussions on the world economy and markets have been defined as a set of recurring questions. The first question was straightforward, ie is a recession looming? With authoritative growth forecasts such as those of the International Monetary Fund downgraded significantly, there is good reason for concern. However, the chances of a global recession are slim, although a major shock, such as a dramatic expansion of conflict

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<sup>4</sup> Franks, J., (2024), What is a recession, what causes it and what happens during an economic Sky News,<https://news.sky.com › story › what-is-a-recession-what-causes-it-and>.

or a sudden and significant disruption in a key market such as energy, could change this outlook. Some economies will certainly shrink.

- The second key question concerns the trajectory of inflation. The proximate cause of the recent price increases are supply chain bottlenecks and imbalances between supply and demand. The Ukrainian conflict has intensified upward pressure on energy, commodity and food prices. Some of this will be transient, although it will last longer than originally expected. But inflation is also driven by other trends, which won't disappear anytime soon. The population, which represents about 75 percent of the global economy, is aging, labor force participation is declining, and productivity growth is trending downward. Moreover, spare capacity in developing economies is lower than it used to be, and what there is remains unused. Add to that the coming policy-driven diversification of supply-demand linkages in response to a myriad of shocks, from the pandemic and climate change to geopolitical tensions and conflicts, and a prolonged period of supply-constrained growth with built-in inflationary pressures seems likely.
- The third recurring question is what's next for the technology sector and digital transformation? Quarantines and other public health measures have spurred the adoption of digital technologies to accelerate during the pandemic. But contrary to market expectations, this trend is likely to slow down as pandemic restrictions are lifted.

A recession can be caused by the collapse of any area of the economy and create a domino effect that begins to spread to other areas. A housing bubble can cripple banks, which then struggle to serve businesses and customers, many of whom will lose their homes and lead to a wider collapse. A prolonged oil crisis could drive up prices and shut down major industries, leading to job cuts that begin to force large numbers of people to tighten their belts. Lenders could be overly liberal with their lending when economic times are good, only to be left out of pocket when times get tough, saddling people with heavy debt at a time when they could be losing their jobs or taking a pay cut. The economy is a combination of many things - how many and what type of jobs are offered, the state of the housing and construction market, how production works, etc. - and they are all strongly interconnected, so if one fails, then the entire economy is under threat.<sup>5</sup>

- At a time of rising inflation, tightening monetary policies and falling growth projections, markets began to correct. Not surprisingly, growth stocks, whose value is derived from expected future cash flows and tend to be concentrated in the technology sector, fell particularly sharply. These market changes do not mean that the digital, energy and biomedical transformations underway are without substance or that they will not have long-lasting economic effects. Markets naturally tend to be more volatile than the underlying economic reality they are meant to reflect. Greater market volatility will have important short-term consequences, as venture and private capital funding, which plays a key role in supporting innovative companies with potentially high growth, is not isolated.
- The final question that seems to be preoccupying minds lately is whether the Ukrainian conflict, Europe's determination to reduce dependence on Russian energy sources and skyrocketing fossil fuel prices will hinder the transition to low carbon emissions. Fortunately, there are good reasons to think it might not happen, at least not in a permanent way. For starters, high fossil fuel prices create a strong incentive for countries and consumers to increase energy efficiency

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<sup>5</sup> IG, (2024), What is a Recession? Definition, <https://www.ig.com › za › trading-strategies>.

and invest in sustainable energy solutions. In this sense, they go some way towards offsetting the failure to establish an effective global carbon pricing scheme. High fossil fuel prices will have negative distributional effects within and across countries, similar to the impact of a regressive tax. But these effects can be mitigated, ideally through some form of income redistribution. What governments should not do is subsidize fossil fuels by regulating final prices below market levels, as this would weaken the incentive to pursue more sustainable options. There is a good argument for stabilizing energy prices to encourage investment in alternative solutions.

- Geopolitics also strengthens the drive for clean energy. Unlike fossil fuels, renewable sources do not create external dependencies to a large extent. Therefore, the green transition is a powerful mechanism for increasing resilience and reducing vulnerability by using energy reserves as a tool. After all, the green transition is a multi-decade process, whereby the energy mix gradually shifts from fossil fuels to clean alternatives. In the near future, economies, especially Europe, may turn to "dirty" energy, including coal, to meet their needs. But this does not necessarily mean that it will be disastrous for the energy transition, let alone for the global sustainability agenda.

## **6. Recession results**

The International Monetary Fund (IMF) has again cut its growth forecasts for the world economy, warning of the risks of high inflation and the war in Ukraine, which could push the world economy to the brink of recession.

Growth in the global economy will slow to 3.2 percent in 2022, the IMF said, cutting its April forecast to 3.6 percent, according to updated forecasts that include only major economies and large groups of economies.

They add that world GDP actually shrank in the second quarter due to declines in China and Russia.

The fund also cut its growth forecast for 2023 to 2.9 percent, down from an April estimate of 3.6 percent growth, citing the impact of tighter monetary policy.

"The outlook has worsened significantly since April. The world could soon be on the brink of a global recession, just two years after the last one," said the IMF's chief economist, Pierre-Olivier Guerinchas.

The fund said the latest updated forecasts are "extremely uncertain" and subject to downside risks from Russia's war in Ukraine, which causes energy and food prices to rise.

Under the alternative scenario, which includes a complete cutoff of Russian gas supplies to Europe by the end of the year and a further drop in Russian oil exports by 30 percent, the IMF predicts that global growth will then slow to 2.6 percent in 2022 and to 2 percent in 2023, with near-stagnation in Europe and the United States next year.

Global growth has fallen below two percent on only five occasions since 1970, the IMF said, including the first year of the Covid-19 pandemic in 2020.

The IMF now expects inflation in advanced economies to reach 6.6 percent in 2022, up from 5.7 percent in April, adding that it will remain elevated for longer than previously expected.

Furthermore, they now expect inflation in emerging markets and developing countries to reach 9.5 percent this year, up from a projected 8.7 percent in the April estimates.

"Inflation at current levels poses a clear risk to current and future macroeconomic stability, and its return to the levels set by central banks should be a top priority for policymakers," Gurrinchas said.

For the United States, the largest economy, the IMF reaffirmed its July 12 forecast that it expected growth of 2.3 percent in 2022 and an anemic 1.0 percent in 2023, having previously cut it twice since April due to slowing demand.

The IMF significantly cut its earlier estimate for China's growth in 2022 to 3.3 percent, from an April projection of 4.4 percent, citing the Covid-19 outbreak and widespread shutdowns in major cities that have curbed output and worsened disruptions in global supply chains.

The IMF also assessed that the worsening crisis in the Chinese real estate sector is affecting sales and investments in real estate. They say additional fiscal support from Beijing could improve growth prospects, but that a continued slowdown in China, driven by the wider spread of the virus and lockdowns, will result in strong spillovers.

The IMF cut its forecast for eurozone growth in 2022 to 2.6 percent from 2.8 percent in April, reflecting inflationary spillovers from the war in Ukraine.

However, forecasts were cut significantly for some countries with more war exposure, including Germany, where growth estimates for 2022 were cut to 1.2 percent, from 2.1 percent in the April forecast.

For the Russian economy, the IMF predicts a six percent decline in 2022 due to tightening Western financial and energy sanctions, and that it will shrink by a further 3.5 percent in 2023, according to updated forecasts.

They also estimate that the Ukrainian economy will shrink by about 45 percent because of the war, but such estimates are highly uncertain.

## **Conclusion**

Recessions cause standard monetary and fiscal effects—credit availability tightens and short-term interest rates tend to fall. As businesses try to cut costs, unemployment rates rise. This, in turn, reduces consumption rates, which causes inflation rates to decrease. Lower prices reduce corporate profits, which causes more job cuts and creates a vicious cycle of economic slowdown.

National governments often intervene to rescue key businesses facing potential failure or structurally important financial institutions such as large banks. Some companies with foresight and planning understand the implicit opportunity created by the lower cost of capital as interest rates and prices fall and are actually able to take advantage of a period of recession. A larger pool of unemployed workers allows employers to recruit more qualified candidates.

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