

Recessions following expansions: The instability of market economies

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Objectives

- To provide new facts about business cycles in the economy and challenge the common view that the economy is fundamentally stable
- Developing models that illustrate a necessary trade-off between severity and length of recessions
- Recommend structural policies to limit recessions, rather than responses to shocks

The conventional view in macroeconomics is based on the idea that the economy is fundamentally stable, with market forces acting to push it towards a smooth growth path. Business cycles are then caused exclusively by the arrival of random shocks, such as an increase in oil prices or higher tax rates.

Ademu's research challenges this view, and suggests the economy is fundamentally unstable and would go through booms and busts without shocks. We have come to this conclusion by using three elements: data, which shows a cycle of change in the economy around every 10 years; theory, in which expansion and recessions are linked - expansion sows the seeds of the next recession, and vice versa; and a quantitative model in which we analyse the data.

Based on our research, we have two recommendations: there should be a trade-off between the severity of a recession and its length by supporting weak sectors; understand that structural policies, such as better unemployment insurance, can limit fluctuations rather than responding to shocks.

Further reading

To read the full paper which accompanies this policy brief, see chapter five (pages 53-60) of the ADEMU e-book published by VoxEU.org:

www.voxeu.org/The-emu-after-the-crisis

You can see a short video summary of this topic by one of the authors at:

www.ademu-project.eu/ademu-explained-recessions-following-expansions-and-the-instability-of-market-economies-video-with-franck-portier/

A European Unemployment Insurance System

www.ademu-project.eu/policy-brief-a-european-unemployment-insurance-system

Macroeconomic stabilisation in heterogeneous societies

www.ademu-project.eu/macroeconomic-stabilisation-in-heterogeneous-societies

Reassessing tax policies and tax coordination: The case for a tax on automation

www.ademu-project.eu/reassessing-tax-policies-and-tax-coordination-the-case-for-a-tax-on-automation

Stimulus packages? Better be persistent!

www.ademu-project.eu/stimulus-packages-better-be-persistent

There are 38 working papers related to this topic. See the full list:

www.ademu-project.eu/ademu-working-papers-related-to-work-package-2

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