

# **The Application of the Sahm Rule to Determine the Likelihood of a Recession in 2025**

**David M. Savino**  
**Ohio Northern University**

*Over the decades a significant issue has been the degree to which expert analysts and economists have the ability to accurately predict the onset of a recession. The studies done to track trends and the early indicators of potential recessions have had mixed results that vary as much as the experts' opinions. However, one measure of predicting recessions has its supporters and proponents. The measure known as Claudia Sahm developed the Sahm Rule. This study is a twofold analysis of the Sahm Rule and its instrumentality in the analysis and predictions for the year 2025.*

*Keyword: Sahm Rule, recession, 2025, economic prediction power, consumer confidence*

## **INTRODUCTION**

Despite the dire predictions of a recession that would be an economic reality during 2023, the actual results achieved showed a resilient economy and significant positive indicators that have continued well into late 2024. With the election of 2024 just completed, many believe that there may be some signs of economic concerns as 2025 begins. However, the overall key indicators for the future seem to point to continued growth, lower employment, and a steady decline in inflation. With consumer confidence still strong and consistent, the actions of the Federal Reserve in late 2024 may have just achieved what was hoped for in terms of a soft landing and continued growth not only throughout 2025 but even for several economic quarters that could easily stretch into 2026. In recent decades, especially since the 1990s, the reality of longer sustained growth periods without recession seems to be a constant. Since the Great Recession 15 years ago, the economy has grown steadily and consistently except for the major disruptions of the COVID-19 pandemic. As we all know this period of adjustment was not driven by economic events but rather the unusual phenomenon of a health crisis that required strict economic measures and employment reductions due to the need to control the spread of the virus through enforced protocols such as social distancing. Now that we are about five years beyond the beginnings of the pandemic, the economy has recorded consistent growth patterns and positive economic indicators that could continue for several more years, well into 2026, marking more than a decade of prosperity sans the COVID-19 pandemic.

But on what basis do these projections seem to be offered by economists and even politicians? Discussing and analyzing the reasons for such optimism may be valuable. Several key indicators are tracked regularly by experts to assess the current economic situation along with potential predictors for changes soon. Macroeconomic metrics that are tracked over time include the unemployment rate, vacancy rate, the inverted yield curve, monthly job creation, the inflation rate, the Gross Domestic Product (GDP), stock price fluctuations, consumer confidence and spending and interest rates (Daly et al., 2012; Barlevy et al.

2024; Michaillet and Saez, 2024, US Bank, 2024). Based on these and other factors, calling for a recession to occur anytime shortly is always a challenge, especially in light of the disruptive effect of the pandemic and the associated period of recovery since 2021. With the help of the use of the Sahm Rule and other economic elements, the status of the economy over the year 2024 has shown several positive signs thus far which are expected to continue. For example, the U.S. economy grew at a rate of 2.8 % during the third quarter along with very positive Employment Situation Reports for August, September, and October (Moore, 2024).

### WHAT IS THE SAHM RULE?

The Sahm Rule was originally a chapter written by Claudia Sahm as part of a Brookings Institution’s report on the use of fiscal policy to stabilize the economy during times of recession (*Shambaugh et al., 2019*). In its applications, the Sahm Rule has indicated, with a high degree of accuracy, that recessions generally begin when the three-month moving average of the employment rate is at least a half percentage point higher than the twelve-month low (*Meredith, 2024*). The Sahm Rule was first published in the *Federal Reserve Economic Data (FRED)* report by the Federal Reserve Bank of St. Louis and is retroactively calculated to evaluate performance from past recessions (*FRED, 2019*). Typically, the rule uses the national data series of the monthly employment reports the Bureau of Labor Statistics released on the first Friday of each month (*Schneider, 2019*). The Sahm Rule has been a highly tested and robust tool with high reliability in identifying economic downturns (*Wiseman and Rugabur, 2024*). The accuracy of the Sahm Rule over the years is uncanny in its ability to track and predict recessions in its basic and simple calculation (*Ward, 2024*). As seen in Table 1 below, there have been eleven recorded recessions since 1950 (*Rasure and Courage, 2024*).

**TABLE 1  
RECESSIONS SINCE 1950**



Source: Rasure and Courage (2024). *Investopedia*.

The rule is judged by economists and investors to be highly effective and accurate. In fact, in the 75 years since 1950, it has only had two mild false positives in the years 1959 and 1969 where recessions did occur but not within the specific periods predicted (*Dorn, 2024; Wiseman and Rugabur, 2024*). As seen in Table 2 below, specific Sahm Rule alerts have coincided with associated recessions based on the U.S.

unemployment rate, as indicated by the dates when the Sahm rule was triggered and the actual recession time.

**TABLE 2  
HISTORICAL ACCURACY OF THE SAHM RULE**

Sahm >0.50...	Sahm	U-rate %	Recession starts...	
Nov 1953	0.63	3.50%	Jul 1953	4 months prior
Oct 1957	0.50	4.50%	Aug 1957	2 months prior
Nov 1959	0.60	5.80%	Apr 1960	5 months prior
Mar 1970	0.77	4.40%	Dec 1969	3 months prior
Jul 1974	0.60	5.50%	Nov 1973	8 months prior
Feb 1980	0.53	6.30%	Jan 1980	1 month prior
Nov 1981	0.60	8.30%	Jul 1981	4 months prior
Oct 1990	0.53	5.90%	Jul 1990	3 months prior
Jun 2001	0.50	4.50%	Mar 2001	3 months prior
Feb 2008	0.53	4.90%	Dec 2007	2 months prior
Apr 2020	4.00	14.80%	Feb 2020	2 months prior
Aug 2024	0.40	4.10%	-	-

Source: Goldstein (2024). Marketwatch.

The important thing to remember with the Sahm Rule is that it is just one economic indicator that should be considered among a series of economic data and indicators. For example, the Sahm Rule has been criticized for relying too much upon a single economic variable, which may delay recessions and reduce accuracy in predicting their severity. Thus, prompting some experts over the years to call for tools and indicators that may more effectively integrate multiple economic variables for a more comprehensive assessment of economic conditions (Estrella & Mishkin, 1995). However, regardless of any cautions, the Sahm Rule remains a very valuable tool for economists and policymakers for early detection of economic downturns.

## OTHER KEY TOOLS AND INDICATORS

In the days and months before a recession occurs there are signs of economic slowdowns and downturns in various key indicators. In addition to economic factors, recessions are often triggered by natural disasters, healthcare emergencies, financial upsets, supply chain disruptions, political unrest, and regional outbreaks of war (TD Investing, 2024). Here are a few of the other key economic indicators;

### Yield Curve

Yield curves can be used effectively to forecast a recession or recovery. Over the years, many studies have been conducted to assess the predictive power of the slope of the Treasury yield curve to determine the likelihood of recessions (Kessel, 1965; Harvey, 1989). The research has shown empirical probabilities using statistical models where the yield curve becomes negative or an inversion where short-maturity rates exceed long-maturity rates before each recession since the 1970s (Benzoni et al., 2018). Adding the yield curve spread to the use of equity volatility adds significant prediction ability to foresee the chance of a recession occurring compared to the yield spread in isolation (Hansen, 2024).

### Inflation

A marked and steady increase in inflation can be a concern in times of potential recessions because it tends to dampen consumer confidence, consumption, and buying power. Since the household sector accounts for the largest majority of spending in an economy, any sign of increases in inflation can cause the potential for economic slowdowns. Since the COVID-19 pandemic, economies throughout the world

have faced the fact of rising inflation. This has caused the Federal Reserve to substantially tighten monetary policy beginning in early 2022. Such a shift in policy by the Fed was expected to try to reduce inflation but it also raised concerns about slowing the economy into a recession thus the possibility of dual negative effects on households (Schwartzman 2023). In light of this, the Fed hopes to contain inflation and encourage growth without causing a recession by over-tightening monetary policy. Attempts by the Federal Reserve to engineer a soft landing while controlling high inflation can come at the risk of job losses through economic slowdowns and uneasiness, where unemployment erodes earnings and economic well-being through job losses (Bengali and Duzhak, 2024).

### **Retail Sales and Consumer Spending**

An obvious indicator to watch for potential recessions is related to consumer confidence and retail sales. A decrease in retail sales can signal an economic contraction. Over the last 15 years, the data in the retail sales area has been mixed. While retail sales have remained strong throughout the period, except for the disruptions during the COVID-19 pandemic, store closures have accelerated, store openings have slowed, and shareholder-value destruction has been massive (Rugaber, 2024; Favaro et al., 2009).

### **Gross Domestic Product (GDP)**

Gross Domestic Product (GDP) tends to be a narrow measure of monitoring declines in the economy that signal the beginning of a recession. GDP is the value of all goods and services a country produces as measured in certain periods. When GDP declines for at least two quarters in a row, the economy is usually in a recession (Claessens and Kose, 2024).

### **Vacancy Rates and Housing**

Another assessment of the economy and the likelihood of a recession is to track the percentage of all available units in rental property such as hotels and apartments where a low vacancy rate is considered positive because there is a demand and thus more occupied units (Chen, 2020). While vacancy rates are positive, the current housing market holds both bad news and good news. The reality of the housing market is characterized by record-high home prices and climbing mortgage rates with some fears of a market bubble prime to pop as in 2008. However, this is of somewhat lower concern compared to earlier periods because of the record low supply of houses and the actions taken by the Fed to cut interest rates, and the fact that today's homeowners are on more secure ground with more positive expectations for 2025 (Rothstein and Basile, 2024).

## **CHANCES FOR A RECESSION IN 2025**

The July Employment Situation report from the BLS in early August was disappointing, to say the least. Employers added a mere 114,000 jobs, which was 35 percent below the expected level, along with an unemployment rate increase to 4.3 percent (Wiseman and Rugaber, 2024). Throughout the last few months of the 2024 Presidential election, the economy was a major concern which, among other things such as illegal immigration, may have cost Kamala Harris the election. It is important to note that the recorded 4.3 percent increase in unemployment crossed the Sahm Rule threshold indicating that a recession would likely occur soon while Claudia Sahm herself, as chief economist of New Century Advisors, said that a recession was not imminent (Wiseman and Rugaber, 2024). Despite triggering the Sahm Rule standards to call for a coming recession, the overall assessment by economists and experts is to wait and see what happens during the fourth quarter of 2024.

While there have been some concerns in some areas related to persistent inflation and continuous increases in consumer prices, the Stock Market has been consistently strong in setting new record highs into the 4th quarter, and wage values have grown. Some of the economic underachieving can be attributed to two severe hurricanes that disrupted the lives and the economic systems of a sizable portion of the southeast region of the United States. Despite Hurricanes Helene and Milton, job growth was strong in October due to the 250,000 jobs added in September and 125,000 in October (Jones, 2024). In addition, the

economy's resilience into the fall can also be explained by two recent interest rate cuts by the Federal Reserve's Open Market Committee helping to cool inflation and supporting a hoped-for soft landing.

Optimism for the near future as related to the US economy is largely based on the continuing strength of consumer spending since households benefited from higher incomes, lower taxes, and accumulated savings during the pandemic (Santerelli, 2024).

## CONCLUSION

Estimates of a recession occurring during 2025 vary in a range of probabilities from about 15 to 50 percent (Moore, 2024; Goldmansachs, 2024). Analysis of industry assessments and predictions for 2025 may be more optimistic for investors than for everyday consumers (Petro, 2024). Some predictions see a recession occurring from August 2025 to February 2026 (Santerelli, 2024). The strength of these predictions of a coming recession is based on a reported broad decline in the Consumer Confidence Survey index and concerns about high prices as expressed in a recent University of Michigan Consumer Sentiment Survey (Petro, 2024). In addition to the economic analysis, much attention must be paid to the current political environment. The recent election of Donald Trump to another term as President of the United States points to business optimism in terms of policies more conducive to less regulated business practices related to corporate taxes and more business opportunities for more investment coupled with increasing consumer confidence. There is now more of a belief that President Trump will positively impact family incomes and consumption, encouraging growth and minimizing the chances of a recession. The results of the recent election seem, to some degree, to be based on the differences between the touted positive macroeconomic results by the Democrats over the last 4 years versus the microeconomic effects of the economy emphasized by Republicans on households and the associated perceptions experienced by voters. Generally speaking, it appears that the economy will continue to grow but at a slow pace thus reducing the chance for a recession during 2025.

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