

Guess What? Growth is Back!

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The first quarter has come and gone and lots of data have been released. Still, there are pieces of data missing and these missing data points make forecasting GDP treacherous.

Nonetheless, the data we are confident about are consumer spending, business investment, and home building, which appear to have expanded at an annualized real rate of 3.8% in Q1 – the fastest combined pace of growth for these portions of GDP since 2010. In other words, the economy appears to be bouncing back from its weaker Q4. The plow horse economy is starting to trot – at least in the near term.

The other components of real GDP – the ones we are less confident about – such as inventories, government purchases, and trade should pull growth down. Putting it all together leaves us with a forecast of 3.1% annualized growth for real GDP in Q1.

To put this in perspective, just a few months ago, the consensus forecast for Q1 was 1.5 - 2%. The consensus was fretting about the payroll tax hike and the federal spending sequester. (We were forecasting 2.5% at the time.)

Now, the consensus is forecasting about 1.5% growth in Q2. You guessed it, they think the economy will be hit with a delayed response to the fiscal cliff. As usual, we are not as dour and are forecasting another 3% for Q2.

Let's be real – it's still not the 1980s and 1990s, when government was shrinking. But 3% is nothing to sneer at. Monetary policy is loose, housing is rapidly recovering, Corporate America has high profits and strong balance sheets, and entrepreneurs are innovating at a breakneck pace.

Here's our "add-em-up" calculation of real GDP growth in Q1, component by component.

Consumption: Sales of cars and light trucks were up at a 6.4% annual rate in Q1, while "real" (inflation-adjusted) retail sales ex-autos were up at a 1.8% rate. Services make up about 2/3 of personal consumption and they grew at about a 2% rate. So far, it looks like real personal consumption of goods and

services combined, grew at a 2.8% annual rate in Q1, contributing 2.0 points to the real GDP growth rate. (2.8 times the consumption share of GDP, which is 71%, equals 2.0.)

Business Investment: Business investment in equipment & software looks like it grew at a 6.7% annual rate in Q1 while commercial construction was unchanged. Combined, they grew at 5% pace, which should add 0.5 points to the real GDP growth rate. (5 times the business investment share of GDP, which is 10%, equals 0.5.)

Home Building: The housing rebound that started in late 2011 is clearly in full swing. Home building looks like it grew at a 23% annual rate in Q1, one of the fastest increases since the 1980s. This translates into 0.6 points for the real GDP growth rate. (23 times the home building share of GDP, which is 2.6%, equals 0.6.)

Government: Military spending shrank in Q1 (and was doing so even before the sequester) while public construction appears to have declined as well. On net, real government purchases shrank at about a 3.5% rate in Q1, which should subtract 0.7 percentage points from real GDP growth. (-3.5 times the government purchase share of GDP, which is 19%, equals -0.7).

Trade: At this point, the government has only reported trade data through February. On average, the "real" trade deficit in goods has grown compared to the Q4 average. As a result, we're forecasting that the trade sector subtracted 0.1 points from the real GDP growth rate.

Inventories: Inventory accumulation slowed substantially late last year, in part due to a drought in the farm sector. Very early figures for Q1 suggest a rebound. As a result, we're assuming inventories add 0.8 points to the real GDP growth rate in Q1.

Add-em-up and you get 3.1% real GDP growth for Q1, not the start of an economic boom, but far from the recession the pessimists have been warning us about the last few years.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-22 / 9:00 am	Existing Home Sales – Mar	5.000 Mil	5.050 Mil	4.920 Mil	4.980 Mil
4-23 / 9:00 am	New Home Sales - Mar	0.416 Mil	0.421 Mil		0.411 Mil
4-24 / 7:30 am	Durable Goods – Mar	-3.0%	-3.7%		+5.6%
7:30 am	Durable Goods (Ex-Trans) – Mar	+0.5%	+0.9%		-0.7%
4-25 / 7:30 am	Initial Claims Apr 20	350K	352K		352K
4-26 / 7:30 am	Q1 GDP Advance Report	3.1%	3.1%		0.4%
7:30 am	Q1 GDP Chain Price Index	1.4%	1.3%		1.0%
8:55 am	U. Mich Consumer Sentiment- Apr	73.5	72.7		72.3