First Trust
Monday Morning OUTLOOK

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The Economy is Accelerating

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We've called it a "Plow Horse" economy, which was our metaphor invented to counter forecasters who said slow growth meant a recession was on its way. A Plow Horse is always slow, but that slowness hides underlying strength – it was never going to slip and fall. Now, the economy is accelerating.

Halfway through the fourth quarter, monthly data releases show real GDP growing at a 3%+ annual rate. If that holds, it would make for three consecutive quarters of growth at 3% or higher. Believe it or not, the last time that happened was 2004.

Last week saw retail sales, industrial production, and housing starts all come in better than expected for October, the latter two substantially better.

And while retail sales grew "just" 0.2% in October, that came on the back of a 1.9% surge in September. Overall sales, and those excluding volatile components like autos, gas and building materials, all signal a robust consumer.

Meanwhile factory output surged 1.3% in October, tying the second highest monthly gain since 2010. Production at factories is now up 2.5% from a year ago, and accelerating. By contrast, factory production was down 0.1% in the year ending October 2016 and unchanged in the year ending October 2015. The current revival is not due to the volatile auto sector, where output of motor vehicles is down 5.9% from a year ago while the production of auto parts is down 0.3%.

The last piece of last week's good economic news was on home building: housing starts surged after a storm-related lull in September. Single-family starts, which are more stable than multi-family starts - and add more per unit to GDP - tied the highest level since 2007. Housing completions hit the highest level since 2008.

As a result of all this data, the Atlanta Fed's "GDP Now" model says real GDP is growing at a 3.4% annual rate in Q4. The New York Fed's "Nowcast" says 3.8%.

Of course, if we get anything close to those numbers, some analysts will claim the fourth quarter is just a hurricane-related rebound. But the conventional wisdom has been way too bearish for years, and Q3 is likely to be revised up to a 3.4% growth rate from the original estimate of 3.0%. Put it all together, and things are looking up. It's no longer a Plow Horse economy. In fact, after years of smothering the growth potential of amazing new technologies, the government is finally getting out of the way.

The Obama and Bush regulatory State is being dismantled piece by piece, and spending growth has slowed relative to GDP. Tax cuts are moving through Congress. These positive developments have monetary velocity – the speed at which money moves through the economy – picking up. "Animal spirits" are stirring. We don't have a cute name for it, but growth is accelerating.

This reduction in the burden of government would be easier, and much more focused on growth, if Republicans had fixed the budget scorekeeping process when they first had the chance back in 2015, or even in the mid-1990s, after having gained control of both the House and Senate.

Instead, they took a cowardly pass. As a result, when assessing the "cost" of tax cuts, Congress still ignores the positive economic effects of tax cuts on growth. Oddly, while refusing to "score" better GDP growth, we understand the budget scorekeepers assume tax cuts lead to higher interest rates, which add to the cost of the tax cuts. In effect, the scorekeepers will use dynamic models to count the negative effects of tax cuts on the overall economy, but not the positive ones!

This kind of rigged scoring system is why the current tax proposals don't cut tax rates on dividends or capital gains, and why some of the tax cuts are temporary. It's also why the top tax rate on regular income for the highest earners is likely to end up near the current tax rate of 39.6%.

We were never satisfied with Plow Horse growth, but we always thought it showed the power of innovation. The power of new technology caused the economy to grow since 2009, despite the burden of big government.

Now with better policies, growth is on the rise. We haven't fixed enough problems to get 3% real growth in every quarter, and maybe not even as the average growth rate over time. That would probably take some major changes to entitlement spending programs. But the recent improvement is hard to miss and signals that entrepreneurship is alive and well in the United States.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
11-21 / 9:00 am	Existing Home Sales – Oct	5.400 Mil	**5.530 Mil**		5.390 Mil
11-22 / 7:30 am	Initial Claims – Nov 19	240K	**240K**		249K
7:30 am	Durable Goods – Oct	+0.4%	**+0.9%**		+2.0%
7:30 am	Durable Goods (Ex-Trans) – Oct	+0.5%	**+0.4%**		+0.7%
9:00 am	U. Mich Consumer Sentiment- Nov	98.0	**97.8**		97.8