First Trust
Monday Morning OUTLOOK
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Dude, Don't Fret Q1 Drop in GDP

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When the GDP report comes out Thursday, look out, the Pouting Pundits of Pessimism will have a field day.

It was bad enough when the government's first report on real GDP growth for Q1 showed the slimmest of growth – a 0.1% annual pace. But, now, after adding up all the new data and revisions to old data, it is likely that government stats will show a shrinking economy – we expect a -0.4% annualized rate of growth.

Inventories will likely be revised significantly lower, but there should be other minor hits. All in all, it will be the first negative GDP report since the first quarter of 2011.

But regardless of which part of the GDP report accounts for the downward revision, the most important thing to remember is that the report is for the first quarter, the last days of which ended almost two months ago. It's a "rearview mirror" picture of the economy. The winter weather was awful, everyone knows it, and everyone knows that the economy in Q1 was weaker than in recent years.

Since then, more timely data show an economy that has quickly rebounded. The Institute for Supply Management Production Index fell to 48.2 in February (signaling contraction), but rebounded to 55.7 in April.

Job growth has picked back up, claims for unemployment insurance are down, and housing starts have bounced back. Meanwhile, consumer spending continues to grow and new orders for durable goods have gone up and beat consensus expectations for three months in a row. The fundamentals are bright for business investment, including loose monetary policy, high corporate profits, and an upward trend in capacity utilization. As a result, we still look for roughly 3% real GDP growth for the year ahead.

Some analysts fear that if we get one quarter of negative growth then somehow this raises the risk of getting another, and then maybe another, and then all of a sudden we find ourselves in a self-reinforcing downward recessionary spiral. Those analysts typically liken the economy to a motor, which, once stalled, is more likely to stall again.

But the economy isn't a motor, which without the right driver (usually the government, according to the theory) will end up idle. The economy is more like an eco-system, with constant change. And the big threats to this eco-system, the kinds of things that can consistently strangle its growth are not yet here.

The Federal Reserve is loose and likely to stay that way, the yield curve remains steep, tax rates are still low by historical standards, particularly on capital income, and engineers are finding ways around impediments to energy exploration. New technology in 3-D printing, the cloud, computers, software, healthcare, and other areas is still defeating government spending and regulation which threaten to slow growth every day.

In the last quarter of 2012, earlier in this much-maligned and supposedly fragile recovery, real GDP was originally reported as down slightly for the quarter. That drop in GDP was taken as proof that the "sugar high" recovery had come to an end. But the economy bounced back and grew 2.6% over the following four quarters. So, dude, don't fret the negative GDP report, and put in your earplugs. The naysayers will be wrong again.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
5-27 / 7:30 am	Durable Goods – Apr	-0.7%	**-2.0%**	+0.8%	+2.9%
7:30 am	Durable Goods (Ex-Trans) – Apr	0.0%	**-0.6%**	+0.1%	+2.4%
9:00 am	Consumer Confidence – May	83.0	**83.9**	83.0	82.3
5-29 / 7:30 am	Initial Claims May 25	317K	**323K**		326K
7:30 am	Q1 GDP Preliminary Report	-0.5%	**-0.4 %**		+0.1%
7:30 am	Q1 GDP Chain Price Index	1.3%	**1.4%**		1.3%
5-30 / 7:30 am	Personal Income – Apr	+0.3%	**+0.3%**		+0.5%
7:30 am	Personal Spending – Apr	+0.2%	**+0.2%**		+0.9%
8:45 am	Chicago PMI	60.8	**62.1**		63.0
8:55 am	U. Mich Consumer Sentiment- May	82.5	**82.0**		81.8