First Trust
Monday Morning OUTLOOK
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Rear-View Mirror Shows Ugly Q1

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We know Plow Horses don't have rearview mirrors, but economists do. So, let's not beat around the bush: the economy barely grew last quarter. Right now, we're forecasting that real GDP expanded at a 0.7% annual rate in Q1. That's a little below the consensus expected 1.0% growth rate, although above the 0.1% estimate by the Atlanta Fed's GDPNow Model.

Anytime a forecast for real GDP growth is so slow, it's well within the realm of possibility the economy actually shrank. That's exactly what happened a year ago. After a horrible winter, the consensus estimate was that real GDP grew at a 1.2% annual rate in the first quarter of 2014, while we were forecasting 0.5%. The first report showed growth of only 0.1%, which was later revised to *negative* growth and now the government says real GDP shrank at 2.1% rate in Q1-2014.

At that time, the weak data was interpreted by some as the leading edge of a new recession. The conventional wisdom, was that the weather surely played some role in holding down growth, but an outright contraction that bad couldn't possibly all be due to the weather. Of course, that was before the economy rebounded sharply in the middle two quarters of last year, growing at a 4.8% rate, thereby underscoring that it really was the weather all along.

In other words, don't get caught up in the angst about the first quarter, whether the number is slightly positive or even negative. Although the weather was not as bad this year as in 2014, this February was the coldest for the most Americans since 1979. In addition, we had prolonged West Coast port strikes that disrupted both trade and production pipelines. Meanwhile, the huge drop in oil prices appears to have curtailed production in the Oil Patch faster than consumers have translated their savings into purchases in other sectors.

But these issues are all temporary and, like last year, the economy will rebound. In the meantime, below is our "add-em-up" forecast for Q1 real GDP.

Consumption: Auto sales declined at a 3.6% annual rate in Q1 while "real" (inflation-adjusted) retail sales outside the auto sector were down at a 3.2% rate. But services make up more than 2/3 of personal consumption and those were up at about a 4.3% rate. So it looks like real personal consumption of goods and services, combined, grew at a 1.6% annual rate in Q4, contributing 1.1 points to the real GDP growth rate (1.6 times the consumption share of GDP, which is 68%, equals 1.1).

Business Investment: Business equipment investment looks like it declined at a 3% rate while commercial construction fell at a 10% pace. But R&D probably grew, so we estimate overall business investment shrank at a 3% rate, which should subtract 0.4 points from the real GDP growth rate (-3.0 times the 13% business investment share of GDP equals -0.4).

Home Building: Somehow home building continued to grow in Q1. Burned last year, maybe builders arranged to make sure they were doing inside work this winter. It looks to us like residential construction grew at a 3% rate, which should add 0.1 point to real GDP (3 times the home building share of GDP, which is 3%, equals 0.1).

Government: Falling outlays for national defense and less activity on public construction projects suggest real government purchases declined at a 1% rate in Q1, which would subtract 0.2 percentage points from real GDP growth (-1 times the government *purchase* share of GDP, which is 18%, equals -0.2).

Trade: At this point, the government only has trade data through February – and the end of the port strikes in late February make March data a wild card – but the data so far suggest the "real" trade deficit in goods has gotten a little bigger. As a result, we're forecasting that net exports are a drag of 0.2 points on the real GDP growth rate.

Inventories: At this point, we have even less information on inventories than we do on trade, but what we do have suggests companies piled up inventories at a slightly faster pace in Q1, adding 0.3 points to the growth rate of real GDP.

Put it all together, and we get 0.7% as a forecast for Q1. Some may say this is the end for the Plow Horse Economy. But, as we saw last year, even a Plow Horse varies its speed a little bit. Any temporary slowness will be offset by a faster pace for the rest of the year. Most importantly, don't forget that all of this is in the rearview mirror. It is data for April and May that the Fed, and investors, should watch.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-22 / 9:00 am	Existing Home Sales – Mar	5.030 Mil	**5.080 Mil**		4.880 Mil
4-23 / 7:30 am	Initial Claims Apr 18	289K	**284K**		294K
9:00 am	New Home Sales – Mar	0.515 Mil	**0.474 Mil**		0.539 Mil
4-24 / 7:30 am	Durable Goods – Mar	+0.6%	**+1.0%**		-1.4%
7:30 am	Durable Goods (Ex-Trans) – Mar	+0.3%	**+0.3%**		-0.6%