First Trust
Monday Morning OUTLOOK

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Resilient Economy

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It wasn't that long ago that some economists and investors were seriously concerned about US growth going negative for the first quarter. Now, based on our calculations, which we discuss below, it looks like real GDP grew at a respectable 2.6% annual rate in Q1, meaning that US real output was 3.1% larger than Q1-2018.

What makes this even more impressive is that, in spite of attempts by the government to fix seasonal adjustment issues, the first quarter has been weaker than other quarters, averaging only 1.7% growth between 2010 and 2018 versus 2.5% growth for the other three quarters. Time will tell, but we think growth will be higher, on average, for the remainder of 2019 as well.

Remember all those obsessing about the "second derivate" of GDP? That is just a fancy way of saying whether the growth rate is getting faster or slower. The economy grew at a 2.2% annual rate in Q4, which was slower than the 3.4% pace in Q3, which, in turn, was lower than the 4.2% pace in Q2. The theory was that the trend would continue until we were back in recession.

But now it looks like real GDP re-accelerated in Q1. The "second derivate" argument doesn't work unless fundamentals have changed enough to push the economy into recession. Clearly, this hasn't happened.

Monetary policy is not tight, companies are still adapting to lower marginal tax rates, and the odds of a full-blown trade war are diminishing. In addition, deregulation is having a positive effect on the willingness to invest in businesses. The only major problem is an unwillingness to tackle the long-term spending path the federal government is following, but we don't see that taking down the economy in the near or medium term. We still have time to address spending before it seriously threatens growth.

Here's how we get to our 2.6% real growth forecast:

Consumption: Automakers say car and light truck sales fell at a 13.4% annual rate in Q1 while "real" (inflation-adjusted) retail sales outside the auto sector slipped 0.1%. However, most consumer spending is on services, where the data are more sparse. We estimate real personal consumption (goods and services combined) grew at a 1.0% annual rate, contributing 0.7 points to the real GDP growth rate (1.0 times the consumption share of GDP, which is 68%, equals 0.7).

Business Investment: Reports on durable goods shipments and construction suggest that all three components of business investment – equipment, commercial construction, and intellectual property - rose in the first quarter. A combined growth rate of 3.6% translates into adding 0.5 points to real GDP growth. (3.6 times the 14% business investment share of GDP equals 0.5).

Home Building: If there's one area of the US that remains a conundrum it's housing, where it looks like we had the fifth straight quarter of slowed activity. We expect that to change moving forward, but for the time being we see a decline at a -2.6% annual rate, which translates into a 0.1 point drag on real GDP growth. (-2.6 times the 4% residential construction share of GDP equals -0.1).

Government: Looks like a relatively large 2.3% increase in real public-sector purchases in Q1, which would add 0.4 points to the real GDP growth rate. (2.3 times the government purchase share of GDP, which is 17%, equals 0.4).

Trade: Net exports' effect on GDP has been very volatile in the past year, possibly because of companies front-running, and then living with, some tariffs and (hopefully) temporary trade barriers. First quarter data suggest net exports should add an unusually large 1.1 points to real GDP.

Inventories: We only have data for inventories through February, but what we have suggests companies continued the same rapid pace of inventory-building that was happening late last year. As a result, inventories should neither add to nor be a drag on real GDP growth in Q1.

Add it all up, and we get 2.6% annualized growth. The US economic expansion is alive and well.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-22 / 9:00 am	Existing Home Sales – Mar	5.300 Mil	**5.410 Mil**	5.210 Mil	5.510 Mil
4-23 / 9:00 am	New Home Sales - Mar	0.650 Mil	**0.634 Mil**		0.667 Mil
4-25 / 7:30 am	Initial Claims – Apr 20	200K	**200K**		192K
7:30 am	Durable Goods – Mar	+0.7%	**+0.7%**		-1.6%
7:30 am	Durable Goods (Ex-Trans) – Mar	+0.2%	**+0.3%**		-0.1%
4-26 / 7:30 am	Q1 GDP Advance Report	2.2%	**2.6%**		2.2%
7:30 am	Q1 GDP Chain Price Index	1.2%	**1.6%**		1.7%
9:00 am	U. Mich Consumer Sentiment- Apr	97.0	**97.0**		96.9