First Trust
Monday Morning OUTLOOK

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Slower Growth in Q1

Real GDP, in the US, grew 5.5% in 2021, the fastest growth for any calendar year since the Reagan Boom in the mid-1980s. In spite of this, for the two years ending Q4-2021, real GDP grew just 1.6% annually, which is below its pre-shutdown trend.

Because of the shutdown and government actions growth has been uneven. Goods consumption is up 7.5% at an annual rate in the past two years, while services consumption has declined 0.4%. Thanks to a boom in investment during the second half of 2021, investment (including inventories and home building) is up an annualized 5.9% during the past two years.

These uneven growth rates will start to balance out during 2022 and beyond. And in the first quarter of this year, we are tracking a real GDP growth rate of 1.5%, although our forecast may change based on reports to be released in the next week and a half. The bottom line is that this is a far cry from the stellar growth of 2021, but not a recession, either. We expect growth will be a little faster in the second quarter, but, again, not nearly as fast as in 2021.

Right now, the US economy is a battle between forces boosting growth and forces dragging it down. What's supporting growth? First, continued re-opening from COVID-19. Americans are still in the process of returning to normal, but we're not completely there yet.

Second, monetary policy is still very loose. Even if the Federal Reserve raises rates by 2.25 percentage points this year, real interest rates will still be negative and monetary policy will not be tight.

Third, tax rates remain relatively low and are likely to stay that way. Major transformational legislation seems unlikely.

Meanwhile, the economy also faces some headwinds. The Russia-Ukraine War and lockdowns in China are further disruptions to supply chains and the Biden Administration is ramping up regulation, adding to business costs.

Put it all together, positives and negatives, and we're forecasting about 2.5% real GDP growth this year (Q4/Q4), with slower growth in 2023-24 as monetary policy gets tight and the benefits of getting the economy back open eventually run out.

In the meantime, here's how we get to our 1.5% real GDP growth forecast for the first quarter.

Consumption: Car and light truck sales jumped at a 44.2% annual rate in Q1 while "real" (inflation-adjusted) retail sales outside the auto sector rose at a 5.3% rate, and it looks like real services spending should be up at a solid pace, as well. Putting it all together, we estimate real consumer spending on goods and services, combined, increased at a moderate 3.8% annual rate, adding 2.6 points to the real GDP growth rate (3.8 times the consumption share of GDP, which is 68%, equals 2.6).

Business Investment: We estimate an 11.0% growth rate for business equipment investment in the first quarter, with commercial construction unchanged, and investment in intellectual property rising at a typically strong rate. Combined, business investment looks like it grew at an 8.0% annual rate, which would add 1.0 points to real GDP growth. (8.0 times the 13% business investment share of GDP equals 1.0).

Home Building: Residential construction looks like it accelerated to a 6.0% annual rate in the first quarter, with demand for new housing and improvements remaining strong. A growth rate of 6.0% would add 0.3 points to real GDP growth. (6.0 times the 5% residential construction share of GDP equals 0.3).

Government: Remember, only direct government purchases of goods and services (and not transfer payments like unemployment insurance) count when calculating GDP. We estimate federal purchases shrank at a 0.6% annual rate in Q1, which would subtract 0.1 point from real GDP growth. (-0.6 times the 17% government purchase share of GDP equals -0.1).

Trade: Imports have continued to soar in the first quarter while exports have not grown as quickly. As a result, the trade deficit is likely to expand significantly, which will be a temporary drag on real GDP growth in the US. At present, we're projecting that the increase in imports relative to exports will subtract 2.3 points from real GDP growth in Q1, although a report on the trade deficit in March, which arrives on April 27, may alter that forecast.

Inventories: Inventories look like they grew at almost exactly the same pace in the first quarter that they did in the last quarter of 2021. If we're right, that would mean inventories have zero net impact on GDP in Q1.

Add it all up, and we get a 1.5% annualized real GDP growth for the first quarter. Look for continued growth in 2022 but not nearly as fast as in 2021.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
4-19 / 7:30 am	Housing Starts – Mar	1.740 Mil	**1.739 Mil**		1.769 Mil
4-20 / 9:00 am	Existing Home Sales – Mar	5.780 Mil	**5.630 Mil**		6.020 Mil
4-21 / 7:30 am	Initial Claims – Apr 16	180K	**175K**		185K
7:30 am	Philly Fed Survey – Apr	21.4	**24.1**		27.4