US 2017 Q1 GDP

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National Australia Bank

NAB Group Economics

Sluggish March quarter GDP growth suggests the economy got off to a slow start in 2017. However, March quarter weakness is not uncommon and business surveys and consumer confidence remain solid. The outlook for the US economy – of modestly above trend growth – remains unchanged.

A slow start to the year...again

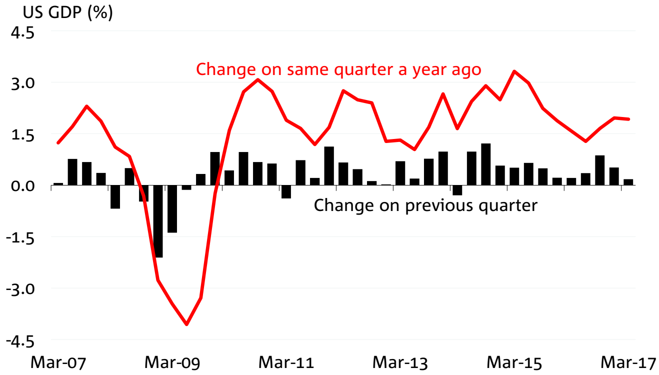
March quarter 2017 US GDP grew by just 0.2% mom, or 0.7% on an annualised basis. As growth at the start of last year was similarly sluggish, the annual growth rate was only down slightly to 1.9% yoy.

The details for quarterly growth, while mixed, where not as bad as the headline result. On the negative side, private consumption growth slowed significantly, and government demand declined. However, while inventories also detracted from growth it does not appear to be the start of a sustained inventory correction. Moreover, a clear positive was that investment – both businesses and in housing - was strong.

Real private consumer spending grew by only 0.1% qoq; the slowest quarterly growth rate since the end of 2009. Consumption may have been affected by delayed tax refunds. The weakness was particularly evident in motor vehicles and parts, housing & utilities, clothing, and gasoline & other energy goods. The fall in motor vehicle consumption followed a period of rapid growth and, with the level of vehicle purchases high, the scope for rapid growth may be limited. Gasoline consumption was probably affected by rising prices, although the worst of the price increases has probably passed. Moreover, the decline in housing & utilities almost certainly reflects the impact of unseasonably mild weather on utility consumption – which will reverse in time.

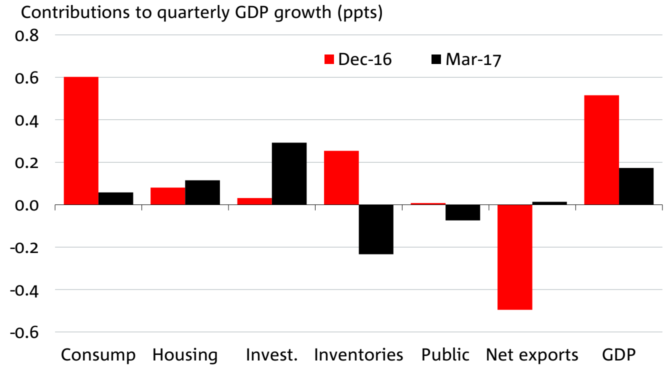
In contrast, business fixed investment recorded its strongest quarterly growth since the end of 2013. Mining structures investment (up 53% qoq) was a strong contributor, spurred by the recovery in oil prices; the oil and gas rig count so far in the June quarter is already tracking well above the March quarter level so the upswing in this sector is not done yet. Equipment investment also grew strongly, building on the recovery started at the end of last year following four consecutive quarterly declines.

Another slow start to the year in Q1



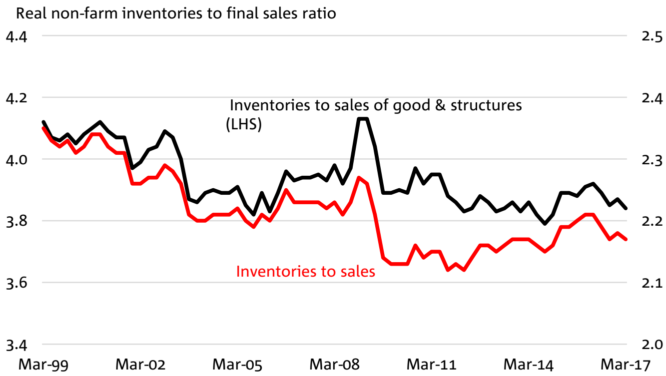
Sources: BEA, NAB

...but not all bad as investment takes off



Sources: BEA, NAB. Data not annualised

Inventory weakness looks like a one-off



Source: BEA

However, the strength in business investment did not flow through to inventories where there was a marked slowdown in inventory accumulation. As a result inventories made a substantial detraction from GDP growth. However, inventory to sales ratios do not look particularly high, suggesting that a sustained detraction from GDP growth – as we saw from mid-2015 to mid-2016 – is unlikely.

Residential investment continued to recover from its mid-2016 slump, growing by a strong 3.3% qoq. The rebound in residential investment occurred despite the rise in mortgage rates since last November's elections. Mortgage rates have partially unwound some of their post-election gains since late March, so it looks like the rise in mortgage rates won't be strong enough to derail the housing market.

Net exports (exports less imports) were a neutral factor on GDP growth in the March quarter, with both exports and imports growing solidly by 1% or more. The annual growth rate also strengthened, with the pick-up in trade not only consistent with other indicators such as the ISM trade orders measures, but also with a solid US economy and an improvement in the global economy as well.

Annual headline personal consumption expenditure (PCE) inflation was 2.0% yoy in the March quarter 2017; the first time it has been at the Fed's 2% target since the start of 2012. However, core (ex energy and food) inflation – which the Fed regards as providing a better signal of future inflation – was unchanged at 1.7% yoy. Moreover, the quarterly number is consistent with the March month annual inflation declining to 1.6% yoy.

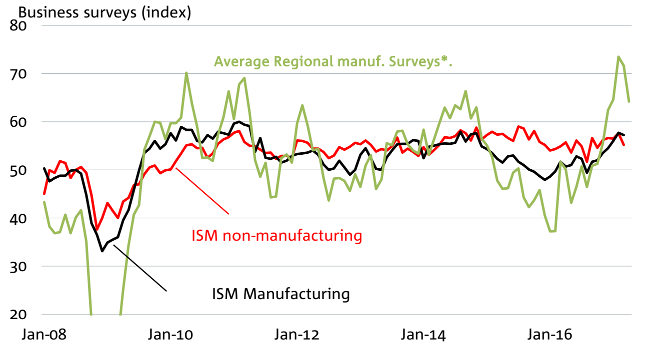
Assessment

The weak March quarter GDP outcome was broadly in line with expectations, both in terms of size and composition, so it does not fundamentally change the outlook.

As we have noted previously, in recent years March quarter growth has generally been much weaker than in the rest of the year. Whether just a coincidence, or due to problems with the statistician's seasonal adjustment, is still up for debate.

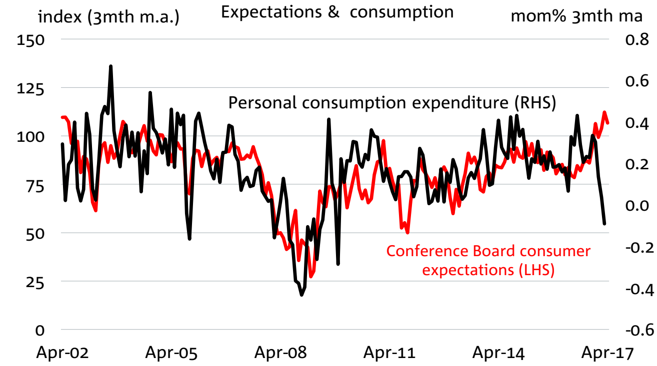
In any event, survey measures of the economy are suggesting that it is performing better than the GDP data suggest. Business confidence is solid and consumer confidence measures show positive sentiment amongst households. Consumer expectations broadly track actual consumption over time but right now there is a significant divergence, suggesting that the March quarter weakness will prove to be only temporary.

Business confidence more positive than Q1 GDP



Sources: ISM, Conference Board, Univ.of Michigan/Thomson Reuters, Richmond, Dallas, Kansas City, Philadelphia & New York Federal Reserves (*simple average of survey results plus 50)

Consumer confidence consistent with much stronger consumption



Source: BEA, NAB.

The truth is probably somewhere in the middle of the survey and GDP data. This would suggest that the economy is growing modestly above trend – consistent with the ongoing decline in the unemployment rate over time we are seeing.

We continue to expect that the Fed will next raise rates at its June meeting. Fed members will not be surprised by the Q1 slowdown but will want to see partial indicators to soon start providing evidence that it is only temporary. The dip in March inflation also increases the risk that the Fed will go slow. However, the Fed will take comfort from the Employment Cost Index (ECI), released the same day as the March quarter GDP estimate, which recorded its strongest quarterly increase in several years, consistent with the general picture that wages growth is gradually strengthening.

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U.S. ECONOMIC & FINANCIAL FORECASTS

	Year Average Chng %					Quarterly Chng %									
						2016		2017				2018			
	2015	2016	2017	2018	2019	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
US GDP and Components															
Household consumption	3.2	2.7	2.3	2.5	2.0	0.7	0.9	0.1	**0.7**	**0.6**	**0.6**	**0.6**	**0.6**	**0.6**	**0.5**
Private fixed investment	4.0	0.7	4.5	3.4	2.5	0.0	0.7	2.5	**1.0**	**0.9**	**0.8**	**0.9**	**0.8**	**0.8**	**0.7**
Government spending	1.8	0.8	0.0	1.3	1.6	0.2	0.0	-0.4	**0.3**	**0.3**	**0.3**	**0.4**	**0.4**	**0.4**	**0.4**
Inventories*	0.2	-0.4	0.0	0.1	0.0	0.1	0.3	-0.2	**0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Net exports*	-0.7	-0.1	-0.3	-0.2	-0.1	0.2	-0.5	0.0	**-0.1**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
Real GDP	**2.6**	**1.6**	**2.1**	**2.3**	**2.0**	**0.9**	**0.5**	**0.2**	**0.7**	**0.6**	**0.6**	**0.6**	**0.6**	**0.5**	**0.5**
Note: GDP (annualised rate)						*3.5*	*2.1*	*0.7*	*2.9*	*2.3*	*2.3*	*2.4*	*2.3*	*2.2*	*2.0*
US Other Key Indicators (end of period)															
PCE deflator-headline															
Headline	0.4	1.4	2.1	2.1	1.8	0.4	0.5	0.6	**0.4**	**0.5**	**0.6**	**0.5**	**0.5**	**0.6**	**0.5**
Core	1.4	1.7	1.9	2.2	1.9	0.4	0.3	0.5	**0.4**	**0.5**	**0.6**	**0.5**	**0.6**	**0.5**	**0.5**
Unemployment rate - qtly average (%)	5.0	4.7	4.3	4.2	4.2	4.9	4.7	4.7	**4.5**	**4.4**	**4.3**	**4.2**	**4.2**	**4.2**	**4.2**
US Key Interest Rates (end of period)															
Fed funds rate (top of target range)	0.50	0.75	1.50	2.25	2.50	0.50	0.75	1.00	**1.25**	**1.50**	**1.50**	**1.75**	**2.00**	**2.00**	**2.25**
10-year bond rate	2.27	2.45	2.75	3.00	3.00	1.6	2.4	2.4	**2.5**	**2.8**	**2.8**	**3.0**	**3.0**	**3.0**	**3.0**

Source: NAB Group Economics

*Contribution to real GDP

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