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Weekly Economic Monitor

Gross Domestic Product

Samuel Blodget was an early American merchant, amateur architect, and economist. He wrote *Economica: A Statistical Manual for the United States*, considered to be the first American book on economics. The modern concept of Gross Domestic Product was developed by Simon Kuznets in 1934. Methodology has changed over time, along with the economy, and the current measure is not without its flaws – but it is the [illegible]

Source: Smithsonian (National Portrait Gallery)

According to the Bureau of Economic Analysis, the National [illegible] of U.S. production, consumption, investment, exports and [illegible] rom Econ 1, Gross Domestic Product measures the value of the goods and services produced by the U.S. economy in a given time period (usually quoted as quarterly at an annual rate). Real (constant $) GDP is simply nominal (current $) GDP adjusted for inflation.

GDP is made up of many components, each with their own methodologies. Details arrive over time. The advance GDP estimate, which is released in the month following the end of the quarter, is based on preliminary data. The 2nd estimate, released a month later, is based on more information. The 3rd is a more complete picture. As we see regularly, the reported GDP growth figure can change a lot with each estimate, but the underlying story typically does not change much.

Once a year, in late July, we get annual benchmark revisions to the GDP data. This can include methodology and definitional changes, but more often, the revisions simply reflect better [illegible] - [illegible] next, but not necessarily much higher or lower overall.

Note that GDP data are reported on a seasonally adjusted basis (unadjusted figures will begin to arrive with the 2018 benchmark revision). Over the last several years, there appears to have been some residual seasonality in the GDP figures. Specifically, first quarter growth figures have been significantly lower than in quarters two through four. That likely reflects a permanent change in behavior following the financial crisis. If there are permanent shifts in the seasonal pattern (for example, less variation in winter consumer spending as the population growth moves to the south and west), the seasonal adjustment will adapt over time. The Bureau of Economic Analysis is aware of seasonal anomalies and is [illegible] residual seasonality removed until the 2018 benchmark revision.

Net exports and the change in inventories make up relatively small portions of GDP, but they account for more than their fair share of GDP growth. Fed Chair Yellen has stressed Private Domestic Final Purchases (PDFP), which is GDP less government, net exports, and the change in inventories (or equivalently, consumer spending, business investment, and residential investment) as a preferred measure of private domestic demand. PDFP is less volatile than GDP.

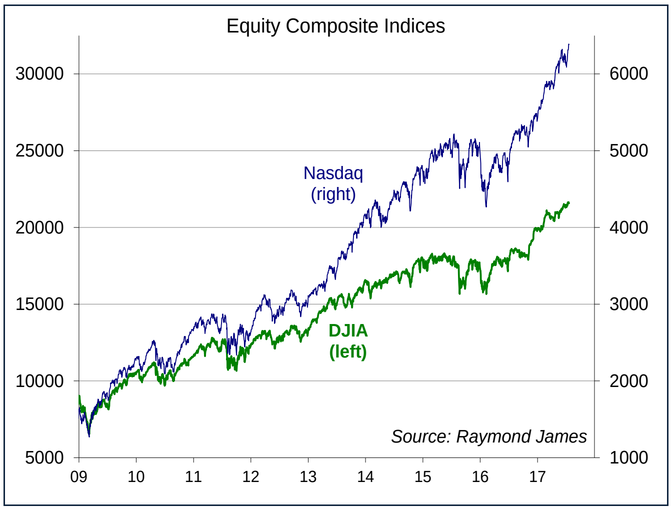
What do we expect for 2Q17 GDP growth? We started the quarter with high hope. Consumer spending growth, soft in the first quarter, was expected to rebound sharply. That rebound now appears to have fallen far short of expectations. Business fixed investment surged in 1Q17, with the rebound in energy exploration (capital intensive) accounting for more than 40% of that. Capital spending likely remained strong in 2Q17, but will almost certainly be less robust than in the first quarter. The mild winter appears to have pulled forward some of the seasonal gains in residential homebuilding (stronger 1Q17, softer April and May), but the trend is still higher. Inventory growth slowed sharply in the first quarter, subtracting more than a full percentage point from headline GDP growth. We have an incomplete inventory picture for 2Q17 and price adjustments [illegible] the kind of inventory rebuild that was anticipated at the start of the quarter. Foreign trade figures are often choppy, but the data in hand suggests that next exports may make a mild subtraction from headline GDP growth.

Interest and appreciation of Alexander Hamilton has been on [illegible] -Manual [illegible] hit Broadway musical – and rightly so. Hamilton was a true visionary. Without him, the U.S. would not have its current financial system. Samuel Blodget, on the other hand, was eventually put in a debtors' prison and died insolvent.

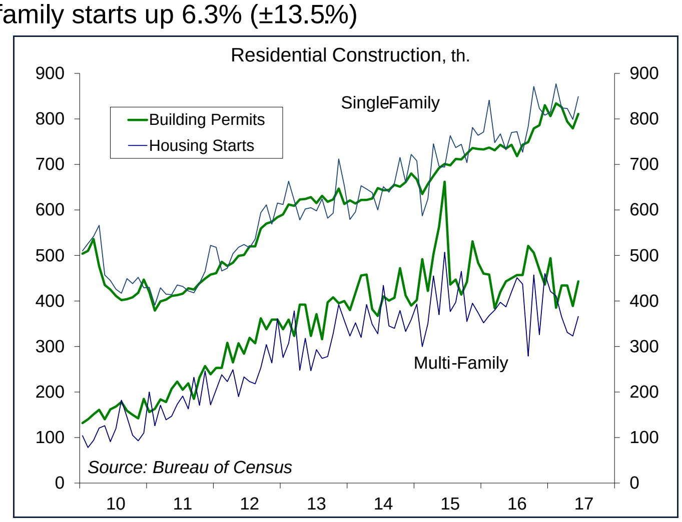
	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	$/Euro	$/BP	JY/$	CD/$	NASD	SPX	DJIA
6/23/17	0.97	1.10	1.21	1.34	1.48	1.77	2.15	2.71	1.120	1.273	111.26	1.326	6265.25	2438.30	21394.76
7/14/17	1.04	1.12	1.22	1.35	1.54	1.87	2.33	2.91	1.145	1.308	112.66	1.266	6312.47	2459.27	21637.74
7/21/17	1.17	1.12	1.22	1.34	1.50	1.80	2.24	2.81	1.167	1.299	111.11	1.254	6385.84	2472.54	21580.07

Recent Economic Data and Outlook

The economic calendar was thin and largely inconsequential. Earnings reports were important, but Washington developments (Senate failure to repeal the ACA, a widening Mueller investigation) did not escape the attention of market participants.



Building Permits rose 7.4% (±1.1%) in June, to a 1.254 million seasonally adjusted annual rate (+5.1% y/y). Single-family permits rose 4.1% (±0.8%), with positive results across regions (Northeast +11.5%, Midwest +11.1%, South +1.8%, West +3.3%). Multi-family permits rose 13.9% (-1.6% y/y). Unadjusted single-family permits for 2Q17 were up 7.1% y/y. **Housing Starts** rose 8.3% (±15.8%), to a 1.215 million pace (+2.1% y/y), with single-family starts up 6.3% (±13.5%).



Homebuilder Sentiment slipped to 64 in July, vs. 66 in June (revised from 67). The National Association of Realtors noted [illegible] concerned ov[illegible]

Import Prices fell 0.2% in June (+1.5% y/y). Petroleum was flat (+6.9% y/y), while natural gas fell 1.0% (+58.6% y/y). Ex-food & fuels, import prices were unchanged (+0.8% y/y). Ex-fuels, prices of imported supplies and materials fell 0.2% (+5.2% y/y). Capital goods rose 0.2% (-0.1% y/y). Consumer goods slipped 0.1% (0.0% y/y). In other words, prices of imported raw [illegible] inflation pressure coming from imported finished goods.

The Index of **Leading Economic Indicators** rose 0.6% in the initial estimate for June. A pickup in jobless claims (still very low by historical standards) made the only subtraction. Positive contributions were led by building permits, ISM new orders, the yield curve, and the Leading Credit Index. The Conference Board indicated that the LEI was consistent with a continued [illegible] upside potential for growth in the second [illegible]al

No surprise, the **European Central Bank** [illegible] left short-term interest rates unchanged and did not alter its asset purchase program. Market participants were hoping for a signal of a possible change in the stance of future policy. It his post-[illegible] substantial degree of monetary accommodation is still needed for underlying inflation pressures to gradually build up and support headline inflation developments in the [illegible]m. He stressed that the ECB could expand its asset purchase program (currently set to end in December) if needed. In Q&A, Draghi indicated the officials will discuss possible changes to the asset purchase program in autumn (no precise date).

Economic Outlook (3Q17): around 2.0% GDP growth, following about 2.5% (expected) for 2Q17.

Employment: The trend in job growth remains moderately strong, but should trend slower as the labor market tightens.

Consumers: Job gains and wage growth are supportive. Purchasing power should improve as gasoline prices stabilize. Debt levels are manageable, with few signs of strain overall.

Manufacturing: Factory output has been uneven in recent months, but the trend appears to be moderate, supported by the energy recovery and better global growth.

Housing/Construction: Job growth has been supportive, with perhaps some weather-related shift into the earlier part of the year. Higher home prices and rising building costs are restraints.

Prices: Ex-food & energy, the PCE Price Index has continued to [illegible]2 % [illegible] consumer goods. Inflation in services has been boosted by higher rents. Wage growth has been moderate.

Interest Rates: The Fed remains in tightening mode, and is expected to continue raising short-term rates gradually. Balance sheet reduction will start (gradually) by year end.

This Week:					[illegible]	last	last–1	comments
Sunday	7/24	23:00	IMF World Econ Outlook					updated
Monday	7/24	10:00	Existing Home Sales, mln	Jun	5 5	5.62	5.56	seen a bit lower
			% change		-1	+1.1	-2.5	held back by supply of homes for sale
Tuesday	7/25	10:00	**CB Consumer Confidence**	Jul	610	118.9	117.6	likely lower
		1:00	Treasury Note Auction					$26 billion in 2-year notes
Wednesday	7/26	10:00	New Home Sales, th.	Jun	620	610	593	these data are erratic
			% change		+1	+2.9	-7.9	watch for revisions
		11:30	FRN Auction					$15 billion in 2- year FRNs
		1:00	Treasury Note Auction					$34 billion in 5-year notes
		2:00	**FOMC Policy Decision**					no change, no Yellen press conference
Thursday	7/27	8:30	Jobless Claims, th.	7/22	24 5	233	248	still subject to seasonal noise
		8:30	**Durable Goods Orders**	Jun	+2.2 %	-0.8%	-0.8%	Boeing reported a surge in orders
			ex-transportation		0+ 4 %	+0.3%	-0.4%	moderate otherwise
			nondef cap gds ex-aircraft		0+3%	+0.2%	+0.3%	moderate
		8:30	Advance Econ Indicators:	Jun				filling in the 2Q17 picture
			merch. trade deficit, $bln		NF	-66.3	-67.1	likely to have narrowed
			retail inventories		NF	+0.5%	-0.2%	slower in 2Q17
			wholesale inventories		NF	+0.4%	-0.4%	slower in 2Q17
		10.00	**Quarles Nom Hearing**					for Fed VC of Supervision
		1:00	Treasury Note Auction					$28 billion in 7-year notes
Friday	7/28	8:30	**Real GDP (advance)**	2Q17	2+5%	+1.4%	+2.1%	annual benchmark revisions due
			Priv. Dom Final Purchases		2+ 6 %	+2.9%	+3.4%	underlying demand strong
		8:30	**Employment Cost Index**	2Q17	0+6%	+0.8%	+0.5%	1Q figure surprised to the upside
			year-over-year		2+4%	+2.4%	+2.2%	some concern to the Fed
		10:00	UM Consumer Sentiment	Jul	93	95.1	97.1	93.1 at mid-month
Next Week:								
Monday	7/31	9:45	Chicago Business Baromet	Jul	5 4	65.7	59.4	seen lower, but still strong
		10:00	Pending Home Sales Index	Jun	NF	-0.8%	-1.7%	likely to pick up
Tuesday	8/01	8:30	Personal Income	Jun	0+5%	+0.4%	+0.3%	led by wages and salaries
			Personal Spending		0+2 %	+0.1%	+0.4%	soft
			PCE Price Index ex-f&e		0+1 %	+0.1%	+0.1%	the core CPI rose 0.119%
		10:00	**ISM Manf. Index**	Jul	5 6	57.8	54.9	moderate
		10:00	Construction Spending	Jun	+1 %	-0.0%	-0.7%	likely to have picked up a bit
		tbd	Motor Vehicle Sales, mln	Jul	NF	16.4	16.6	trend is a bit lower
			domestically built		NF	12.8	12.8	how much inventory clearing?
Wednesday	8/02	8:15	**ADP Payroll Estimate, th.**	Jul	165	+158	+230	moderately strong
Thursday	8/03	8:30	Jobless Claims, th.	7/29	242	245	233	still subject to seasonal noise
		10:00	Factory Orders	Jun	NF	-0.8%	-0.3%	aircraft orders expected to dominate
		10:00	**ISM Non-Manf. Index**	Jul	57	57.4	56.9	moderately strong
Friday	8/04	8:30	**Nonfarm Payrolls, th.**	Jul	15	+222	+152	subject to seasonal noise (school year)
			private-sector		10	+187	+159	a moderately strong trend
			Unemployment Rate		4.3 %	4.4%	4.3%	seen little changed
			employment/population		60.2 %	60.1%	60.0%	edging higher
			Avg. Weekly Hours		35	34.5	34.5	should be steady
			Avg. Hourly Earnings		0+3 %	+0.2%	+0.1%	moderate wage pressures
		8:30	Trade Balance, $ bln	Jun	NF	-46.5	-47.6	likely to have narrowed
			goods only		NF	-67.5	-68.4	minor implications for GDP revisions

This Week…

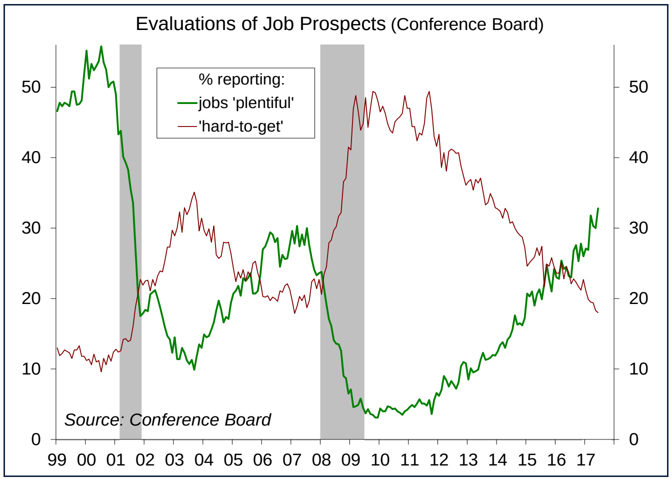
The economic calendar begins to heat up, but the Fed policy meeting is not the highlight. No change in policy is expected and there is no Yellen press conference. Instead, the focus is [illegible] uncertainty in the advance growth estimate, but this release will also include annual benchmark revisions, adding another layer of uncertainty. For the financial markets, the Employment Cost Index, an important piece of information in the inflation outlook, will likely get lost in the shadow of the GDP report, but the Fed will be watching it closely.

Monday

Existing Home Sales (June) – Higher home prices have reduced affordability, but a limited supply of homes for sale are also an issue. The Pending Home Sales Index has been trending lower.

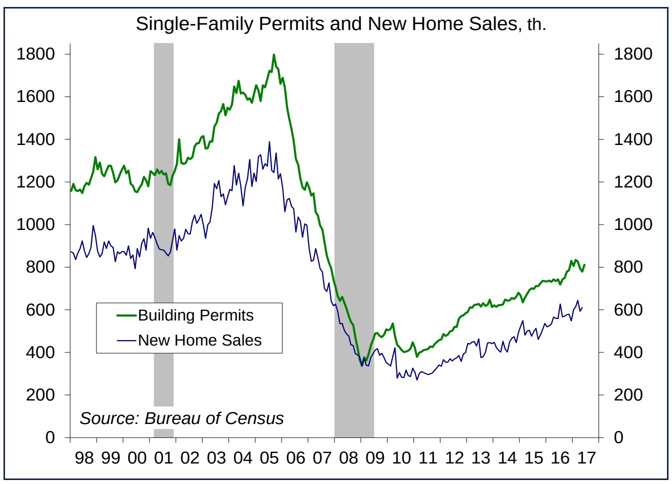
Tuesday

Conference Board Consumer Confidence Index (July) – The headline figure is likely to remain relatively strong in the initial estimate for July, but ought to fall back some. Labor market perceptions have continued to improve, but respondents may be a little more unsettled in their outlook for the future.



Wednesday

New Home Sales (June) – These figures are reported with a huge amount of statistical uncertainty. Monthly changes are erratic, but there is an underlying trend of improvement. Note that the Bureau of Census figures, which measure initial transactions (a down payment or a signed contract), exclude sales where the land and home are sold separately.



FOMC Policy Decision – There is a very small chance that the Fed could announce the beginning of its balance sheet unwinding, but that will almost certainly wait until later this year (most likely, October). There is no Yellen press conference and no release of revised economic projections, so all we have to go on is the wording of the policy statement, which ought not to change much from what we had six weeks ago.

Thursday

Jobless Claims (week ending July 22) – The figures will still be subject to seasonal noise, but that should fade soon, leaving the underlying trend at a relatively low level.

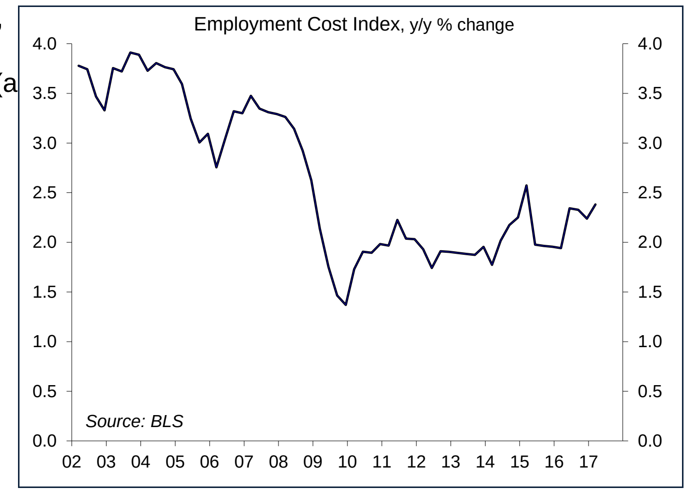
Durable Goods Orders (June) – Boeing reported a large increase in orders in June. Ex-transportation, orders are likely to have risen moderately. The shipment and inventory data will have some implication for 2Q17 GDP estimates.

Advance Economic Indicators (June) – Foreign trade and inventories account for more than their fair share of volatility in quarterly GDP growth. These estimates (merchandise trade, wholesale and retail inventories) will help fill in the 2Q picture.

Friday

Real GDP (2Q17 advance, annual benchmark revisions) – Consumer spending growth, which ended the quarter on a soft note, should have picked up relative to the first quarter. Business fixed investment is expected to have remained strong, although not quite as robust as in the first quarter. Residential homebuilding continued to improve, but the mild winter appears to have pulled some strength from 2Q17 to 1Q17. Inventory growth failed to rebound as much as anticipated. Net exports may subtract a bit from overall growth. Bear in mind that figures will be revised (and revised, and revised).

Employment Cost Index (2Q17) – As a measure of labor cost pressures, the ECI is preferred over average hourly earnings. Quarterly figures can be uneven, but the trend is higher.



Next Week ...

The ISM survey results will be important, but the July payroll figures will carry a lot more weight. Seasonal adjustment is tricky in July, so we could easily get a surprise – but the trend is likely to be moderately strong.

Coming Events and Data Releases

August 10	Producer Price Index (July)
August 11	Consumer Price Index (July)
August 15	Retail Sales (July)
August 16	Building Permits, Housing Starts (July) FOMC Minutes (July 25-26)
August 24-26	Fed Camp (Jackson Hole)
August 30	Real GDP (2Q17, 2nd estimate)
September 4	Labor Day Holiday (markets closed)
September 20	FOMC Policy Decision, Yellen press conf.
November 1	FOMC Policy Decision (no press conf.)
December 13	FOMC Policy Decision, Yellen press conf.