Financial Market Weekly

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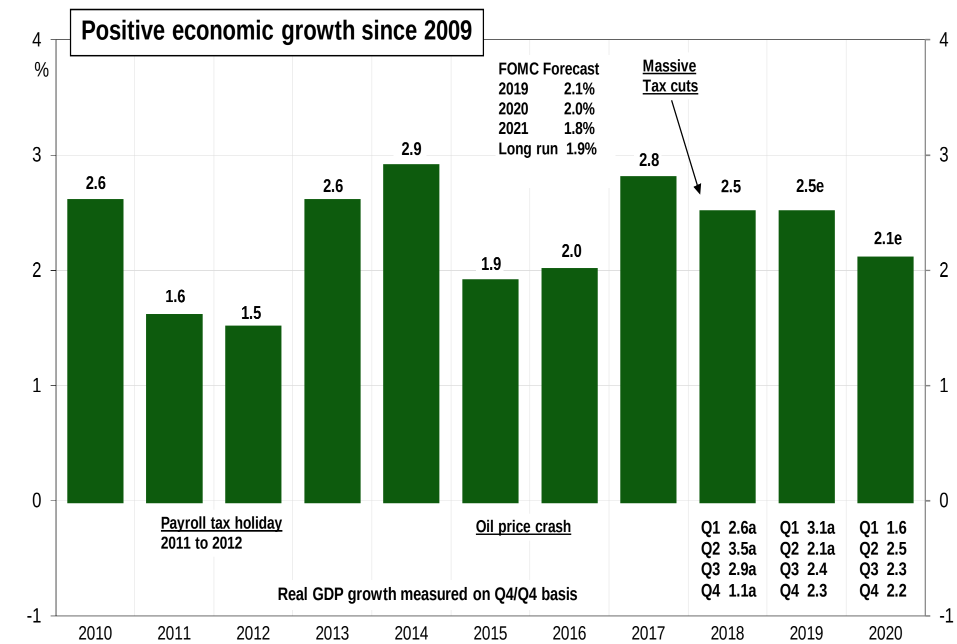
GDP AIN'T WHAT IT USED TO BE, AIN'T WHAT IT USED TO BE



We've seen some odd benchmark revisions over time, but this one takes the cake. Another reason businesses should be careful in basing their budget planning on real GDP growth. It turns out that there was more growth under Obama now than under Trump.

All the King's horses and all the King's men can't get the economy moving forward again. Tax Cuts and Jobs Act, deregulation and the cutting of red tape, trade wars and sanctions to bring jobs and factories back to the USA, none of these measures are boosting economic growth. With today's revisions to GDP back to 2014 it turns out that the economy did better in the last administration than under the current administration. Economic growth was 3.0% in 2018, but now it looks like the Tax Cuts and Jobs Act did little to affect the course of the economy as growth has been revised down to a cooler 2.5%. However, growth was revised up in the first year of Trump's presidency to 2.8% in 2017 from 2.5% before. Meanwhile, lo and behold, growth under President Obama was revised up to 2.9% in 2014 before the oil price crash slowdown of investment spending, and 2.9% is the best growth we have yet to see for the economy in the last five years over both administrations.

> Donald J. Trump 7-26-19 10:40AM EDT
> @realDonaldTrump
> Q2 GDP Up 2.1% Not bad considering we have the very heavy weight of the Federal Reserve anchor wrapped around our neck. Almost no inflation. USA is set to Zoom!

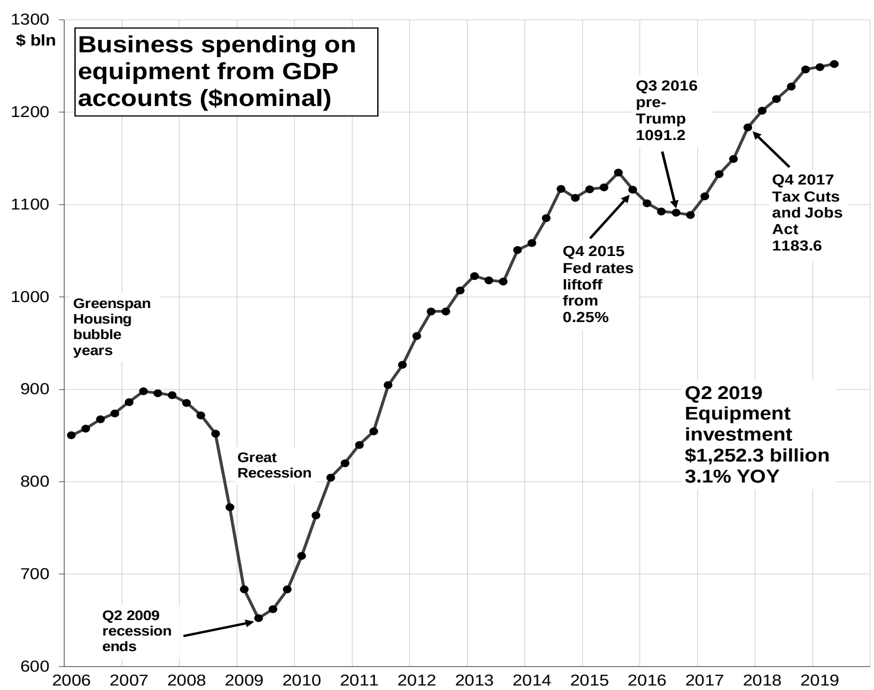
The trend of growth this year is better than feared with real GDP growth of 2.1% in the second quarter and the first quarter holding at 3.1%, and we expect growth of 2.0 to 2.4 percent over the second half of 2019 despite the headwinds of uncertainty. It is true that the government is picking up the bill for economic growth in the second quarter however by adding 0.9 percentage points, accounting for nearly half of the 2.1% GDP growth. Federal government spending bounced back from the government shutdown and added 0.5 percentage points and State & local government spending added 0.4 percentage points.

	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19p
REAL GDP	2.5	3.5	2.9	1.1	3.1	2.1
REAL CONSUMPTION	1.7	4.0	3.5	1.4	1.1	4.3
CONSUMPTION	1.2	2.7	2.3	1.0	0.8	2.9
Durables	0.2	0.6	0.3	0.1	0.0	0.9
Nondurables	0.1	0.6	0.5	0.2	0.3	0.8
Services	0.9	1.6	1.6	0.7	0.5	1.2
INVESTMENT	1.1	-0.3	2.3	0.5	1.1	-1.0
Business Plant	0.4	0.3	-0.1	-0.3	0.1	-0.3
& Equipment and	0.4	0.2	0.2	0.4	0.0	0.0
Intellectual Property	0.4	0.5	0.2	0.5	0.5	0.2
Homes	-0.2	-0.2	-0.2	-0.2	0.0	-0.1
Inventories	0.1	-1.2	2.1	0.1	0.5	-0.9
EXPORTS	0.1	0.7	-0.8	0.2	0.5	-0.6
IMPORTS	-0.1	0.0	-1.3	-0.5	0.2	0.0
GOVERNMENT	0.3	0.4	0.4	-0.1	0.5	0.9
Federal defense	0.0	0.3	0.1	0.2	0.3	0.1
Fed nondefense	0.2	0.0	0.1	-0.1	-0.2	0.4
State and local	0.2	0.2	0.2	-0.1	0.4	0.4

Below line: Percentage point contributions to Q2 2019 2.1% real GDP

Second estimate for Q2 is Thursday, August 29

Net, net, the economy is firing on all cylinders from consumers shopping at the mall to companies ordering up new investment to lay the foundation for stronger growth ahead. The economy finished ten full years of recovery from the Great Recession and is likely to continue moving forward as there is no sign in the real data that the economy is going off the track in today's report with revisions back to 2014.



No recession on the horizon with no uncertainty postponing the spending of consumers and businesses means the widely expected Federal Reserve rate cut at next week's meeting looks premature and out of practice with how the central bank has operated in other times and under other presidents. Rate cuts now sound like Washington politics at its worst. We didn't need a tax cut with the economy not in a recession, and we don't need an interest rate cut with the economy not in a recession either. This economy is strong and does not need additional monetary stimulus as insurance for a rainy day or for any other precautionary reason. Fed officials would benefit from not warning markets and the world that the sky is falling. The USA is not Europe or South Korea or Australia, there is no need for a cut in interest rates here. The economy is better than you think. Bet on it.

$BLN Nominal GDP expenditures	Q4 15	YOY%	Q4 16	YOY%	Q4 17	YOY%	Q1 18	Q2 18	Q3 18	Q4 18	YOY%	Q1 19	Q2 19	SAAR
Equipment & Intellectual Property	1893.6	1.9	1917.5	1.3	2054.5	7.1	2101.4	2142.0	2166.0	2205.5	7.3	2236.9	2258.5	4.9
EQUIPMENT	1116.3	0.8	1088.9	-2.5	1183.6	8.7	1201.8	1214.3	1227.9	1246.4	5.3	1249.0	1252.3	0.9
Information processing equipment	356.3	2.0	358.1	0.5	396.7	10.8	404.4	405.8	414.8	409.5	3.2	416.0	418.8	4.6
Computers	99.4	-4.1	99.7	0.3	109.7	10.0	117.2	120.1	120.2	117.7	7.3	119.4	122.0	7.4
Other processing equipment 1	256.9	4.6	258.4	0.6	287.1	11.1	287.2	285.7	294.6	291.8	1.6	296.6	296.9	3.5
Industrial equipment	218.4	0.3	217.6	-0.4	238.2	9.5	243.1	242.1	246.9	251.6	5.6	250.8	251.4	-0.2
Transportation equipment	306.3	8.5	283.6	-7.4	288.7	1.8	294.9	301.5	299.7	311.0	7.7	309.4	306.1	-3.1
Other equipment 2	235.3	-8.8	229.6	-2.4	260.0	13.2	259.3	265.0	266.5	274.2	5.5	272.9	276.0	1.3
INTELLECTUAL PROPERTY	777.3	3.4	828.6	6.6	870.9	5.1	899.6	927.7	938.1	959.1	10.1	987.9	1006.2	10.1
Software	312.3	3.2	334.2	7.0	354.3	6.0	367.9	377.3	383.8	391.0	10.4	404.1	412.8	11.5
Research & Development (R&D)	386.3	3.3	411.9	6.6	430.9	4.6	444.4	461.6	464.1	476.8	10.7	492.0	500.9	10.4
Entertainment, literary, artistic	78.7	4.9	82.5	4.8	85.8	4.0	87.2	88.9	90.2	91.3	6.4	91.8	92.4	2.4
1 Communication, medical, photocopy, office and accounting equipment; nonmedical instruments														
2 Furniture; agriculture, construction, mining/oilfield, and service industry machinery; electrical equipment														

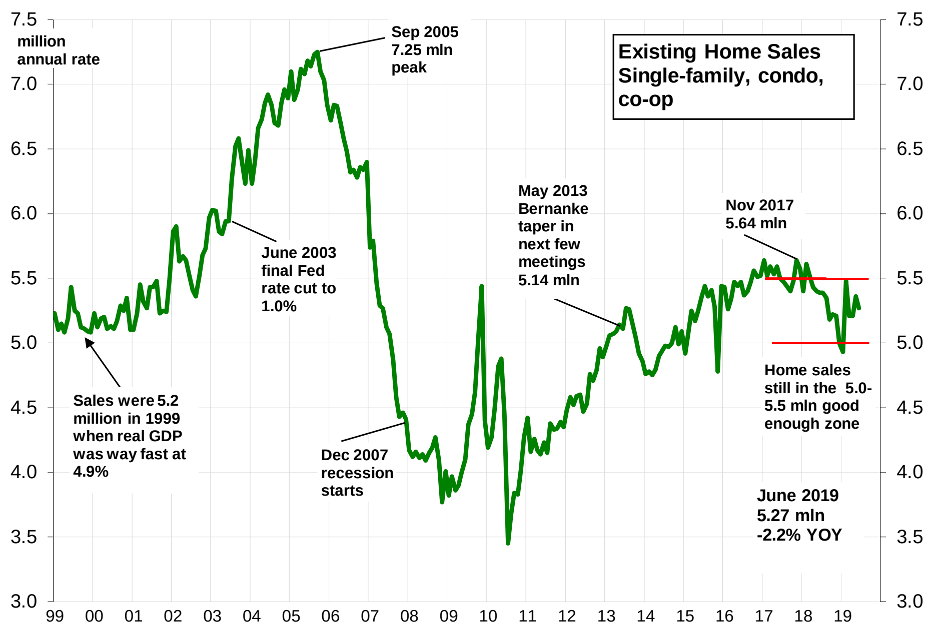
FEDERAL RESERVE POLICY

We expect rate cuts at the next two Fed meeting decision dates on July 31 and September 18. After that we think the Fed will hold rates at 2.0% through the end of 2020.

OTHER ECONOMIC NEWS THIS WEEK

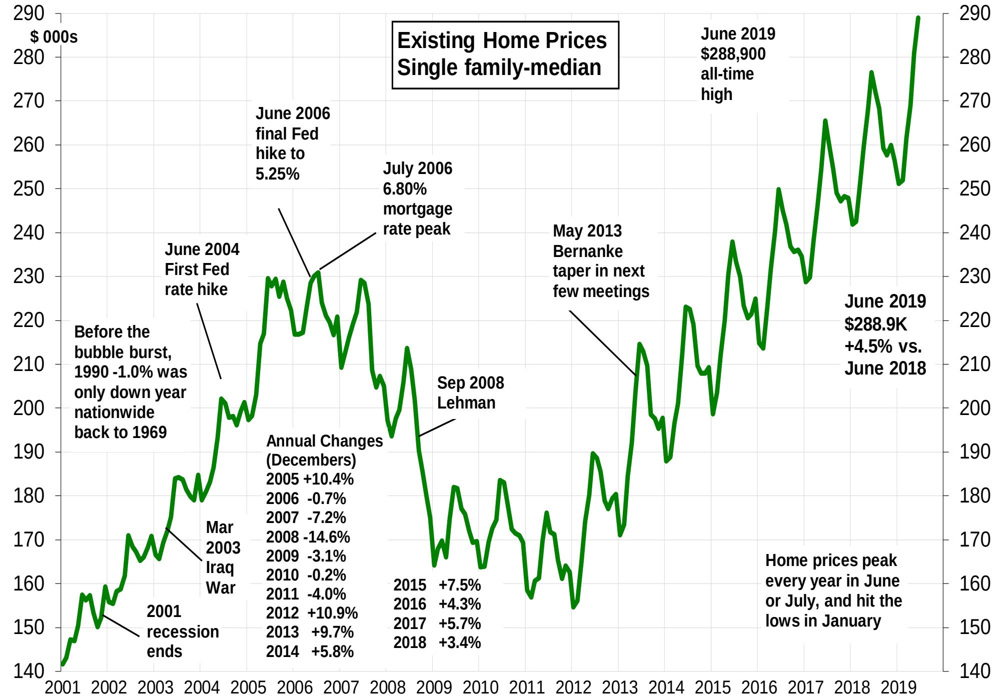
Existing homes sales not seeing lift from low 3.8% mortgage rates (Tuesday)

Breaking economy news. Existing home sales fell 1.7% in June to 5.27 million at an annual rate. Sales were down in the South 2.33 to 2.25 and in the West 1.13 to 1.09, both in millions at an annual rate. Sales were modestly better in the Midwest (1.25) and Northeast (0.68). It was somewhat cooler in June and this may have affected spring buying fever.



Existing single-family home prices reach the peak in June each year when demand hits a fever-pitch for the year. The median price of a single-family home rose to a new record of $288.9 thousand in June which is $8 thousand more than May and $12.4 thousand more than a year ago. Prices are 4.5 percent higher than last year and with home prices rising faster than 3% wages, homes are going to move out of the range of many buyers in terms of affordability, and maybe that is what we are already seeing. The borrowing cost of buying a new home is down, but it does not make up for sky-home prices. Five years ago in June 2014, single-family homes cost $223.0 thousand and today they are $288.9 thousand which is thirty percent more expensive which outstrips most consumers wages over the period.

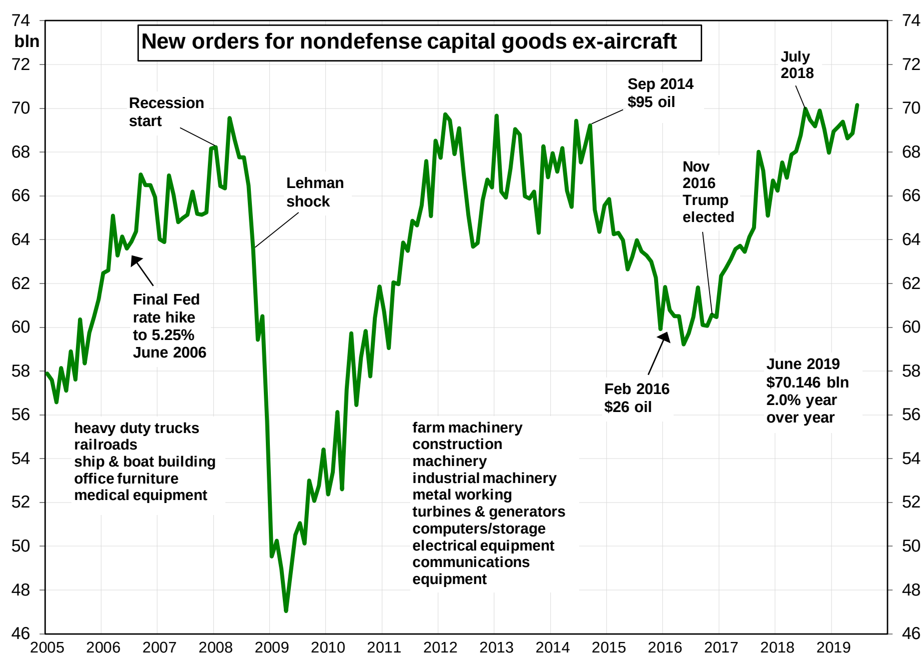
Net, net, home buyers are still lacking the confidence to put a down payment on a new home purchase which is somewhat puzzling as mortgage rates have fallen over a percentage point and consumers remain upbeat according to surveys of consumer sentiment. The trend of sales has been extremely volatile with a huge drop to 4.93 million in January during the stock market turbulence and Federal government shutdown.



The sales turnover of existing homes had been as high as 5.61 million in February last year. 5.27 million is back in the middle of the high/low range for 2018-19. This is one soft economic data point that the Federal Reserve may be able to bolster with a rate cut or two next week, although don't hold your breath. Central banks around the world are facing a credibility crisis where the public no longer believes they have the tools to improve financial conditions and the broader economy. Stay tuned. Story developing.

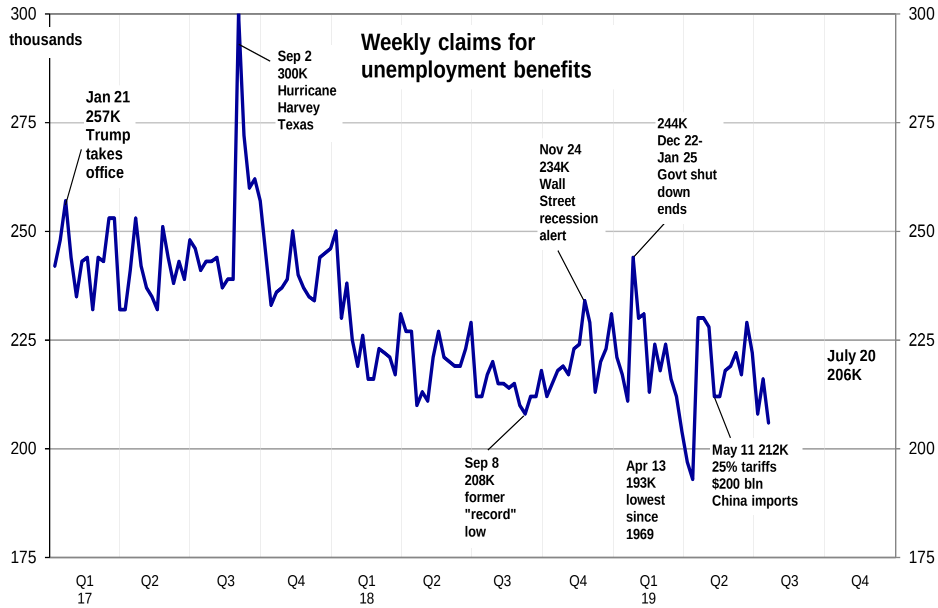
First consumers, now business investment spending soars to record (Thursday)

Breaking economy news. Nondefense capital goods orders jumped 1.9% in June and set an all-time record for investment spending in equipment. Machinery up 2.4% in June. Communications equipment rose 4.0% in June. Fabricated metals rose 2.1% in June. And motor vehicles are not exactly capital equipment but they rose 3.1% so there can't be that much wrong with the auto industry.



Uncertainty that Fed officials say is weighing on the outlook isn't affecting companies hiring plans either. Initial jobless claims fell 10 thousand to 206 thousand in the July 20 week showing the labor market is tight as a drum this summer and this is likely to cause wages to heat up further. There is uncertainty perhaps from the trade war between the US and China but it is not affecting business spending or hiring decisions. The manufacturing purchasing managers surveys may have picked up a softer tone in recent months, but companies are hiring new equipment and workers with abandon. This is not an economy that needs the Federal Reserve to put another log on the fire, the economy is roaring hot enough already.

Net, net, business investment finished the ten year expansion in June setting an all-time record. Fed officials have said that sure the consumer is doing well, but they were worried about a slowdown in business capital spending. No more! Stop worrying be happy is our advice for the Fed. Take the summer off and do nothing.



The thought of Fed officials lowering their guard against future inflation while economic demand pressures continue to build would have been unthinkable to Fed Chairs working under presidents in the decades before this. The Federal Reserve may be bending a little too far to find reasons to give the Trump administration the rate cuts they so sorely think they need to win elections and boost economic growth. This economy is already going up like a rocket after ten years of an expansion and does not need additional monetary stimulus to light a fire under economic growth.

Keep your powder dry is what we are advising Fed officials as the economy has bounced back strongly from the worries and drop in orders and spending from consumers and businesses at the turn of the year. Growth comes back in the spring and now in the summer… pow! The Fed doesn't need to take out insurance for the economy with a rate cut or two or three. This economy doesn't need a rate cut at all; it can be argued that rates are still below normal and not impeding growth in any way because demand is so strong. Companies with strong demand don't fire workers, they hold onto them and that's what the rock-bottom level of job layoffs are telling you. You can't have a recession without job losses and right now there aren't any. Uncertainty isn't killing growth. The economy is just fine. The Fed has teed up a rate cut at next week's meeting, but this will be the most unneeded rate cut in economic history. If the Fed goes it will look like it has buckled under to the demands of the Trump administration. Follow your hearts is the right advice. Just do the right thing. Stop telling the world that the economy is facing uncertainty.

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