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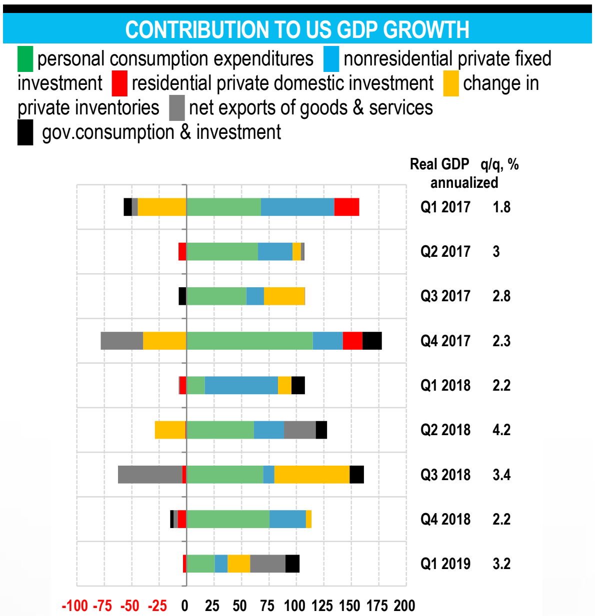
United States: Strong growth but questions about quality

■According to Jerome Powell, the fundamentals supporting the US economy remain solid ■First quarter growth has been robust but underlying concerns about the quality of growth have emerged ■Growth has benefitted from a drop in imports and rising inventory levels while residential investment acted as a drag ■ In the coming months, imports should rebound and inventories should witness a scale back. The onus will fall on consumer spending and corporate investment to neutralise the effects of these anticipated headwinds on growth.

According to Federal Reserve Chairman Jerome Powell, the fundamentals supporting the US economy are solid. One can think of the very low unemployment rate, the sustained pace of job creation, the growth of real disposable income, corporate profitability, the level of real interest rates, etc. One ponders, though, whether solid fundamentals have translated into solid growth? The Bureau of Economic Analysis reported last week that in the first quarter, real GDP increased at an annualized rate of 3.2% versus the previous quarter[1]. At first glance, this shows a strong performance of the economy, with growth accelerating following a slowdown in Q4 (2.2%). However, the quality of growth is an issue. Personal consumption expenditures increased a meagre 1.2%, residential investment contracted for the fifth consecutive quarter while growth in equipment investment remained basically flat. In contrast, investment in intellectual property products continued to grow strongly (+8.6%). Exports increased 3.7%, but imports surprisingly declined 3.7% resulting in net exports providing a strong boost to GDP growth. Finally, government consumption and investment increased 2.4%. In terms of contribution, of the 3.2% increase in GDP, 0.82 percentage points came from personal consumption expenditures (with half of the contribution emanating from health care related expenses), 0.65 p.p. stemmed from an increase in inventories, 0.58 p.p. from a decline in imports, 0.45 p.p. from exports, 0.41 p.p. from government expenditures (principally state and local investment), 0.38 p.p. from non-residential investment (entirely explained by intellectual property products). Residential investment acted as a drag (-0.11 p.p.). The chart takes a longer perspective by decomposing the annualized quarterly growth rates in terms of its main contributors since the start of 2017[2]. The contribution of residential investment has been negative for several quarters in a row. The contribution of non-residential private fixed investment has broadly shrunk over the past year. Meanwhile, changes in inventories have had a positive contribution since the third quarter of 2018. All in all, this shows that, although growth may be solid, its quality may be less so. This suggests a number of possible developments in the coming months. The recent decline in imports seemed out of line, so one should expect a rebound (if this were not to happen, it would send a chilling signal about the future course of aggregate demand). A scale back in inventory accumulation by companies also seems inevitable given the build-up over the past several quarters. This should weigh on production and ultimately on growth. Moreover, the strengthening of the real effective exchange rate since the spring of last year could weigh on exports.



Source: BEA - Bureau of Economic Analysis, BNP Paribas calculations

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[1] The Bureau of Economic Analysis insists that this 'advance estimate' is based on incomplete data and could be subject to revisions. A second estimate will be released on May 30th. The average magnitude of the revisions in absolute terms has been 0.5 percentage points. This would imply a growth rate in a range of 2.7-3.7%.

[2] The p.p contributions of the GDP components have been scaled into percentages to help illustrate how the drivers of growth have evolved over the selected time period.

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