Trend Macrolytics, LLC
Donald Luskin, Chief Investment Officer
Thomas Demas, Managing Director
Lorcan Roche Kelly, Chief Europe Strategist
John Clinton, Principal

TRENDMACRO LIVE!

On Q3 2011 GDP

Thursday, October 27, 2011

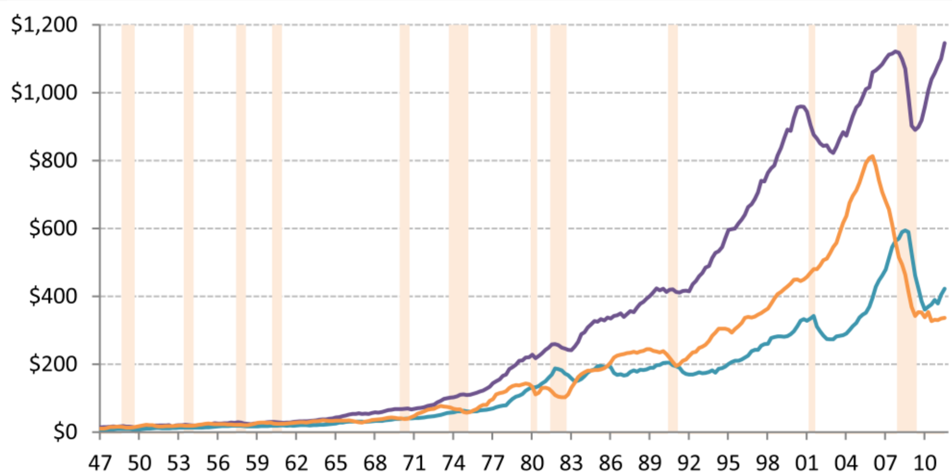
Donald Luskin

How can 2.5% growth be at consensus, when the consensus expects a recession?

[This morning's GDP report] came in precisely as expected by the consensus, with 2.5% real growth. And here's a paradox: at the same time, there is a strong plurality within the consensus that the economy is slipping into recession. 2.5% growth isn't a great number, but it's not a recessionary number. And some key internals are actually quite encouraging for a stronger Q4. All the more so, as yesterday's conclusion to a marathon European summit dramatically lowers the perceived risk of a 2008-type global banking hardstop -- the one real threat to at least moderate growth.

- Q3 now marks the point at which US real output broke out to new high ground, above the peak set in Q4 2007.
- Nominal investment in capital goods -- equipment and software -- finally made new all-time highs, above the peak set in Q4 2007 (please see the chart below). It is still far below trend, and the other categories of fixed investment -- housing and commercial real estate -- remain woefully depressed. But at least it represents some restoration of risk-taking.

Fixed investment — Capital goods — Housing — CRE Recessions
Nominal USD billions, SAAR



Source: Bureau of Economic Analysis, TrendMacro calculations

Update to strategic view

US MACRO: No sign of recession in this morning's Q3 2011 GDP report. Several key internals point to strong growth in Q4. It's a remarkable and encouraging performance considering the general atmosphere of fear that dominated the quarter. As we've been saying, the economy's weakness is its hidden strength -- it's hard to fall into recession with such a large output gap.

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- This is remarkable when set against a backdrop of what seemed to be general fear, uncertainty and doubt. As we've been saying, it will be difficult for the economy to fall into recession when the output gap is as high as it is (see, among many, "Testing 1, 2, 3" September 7, 2011).
- Personal consumption made a new high, too, but it had already bested its prior cycle peak five quarters ago.
- There was no help here from inventories -- in fact they subtracted from growth for the second quarter in a row. Because changes in inventories, by construction, must sum to zero across time, two quarters of negative contribution sets up for a positive contribution next quarter.
- There was no help from government. Federal was a positive contributor, state and locals a perfectly offsetting negative. Whatever the economy did in Q3, it did it on its own.
- The dark side to this morning's report was disposable personal income, down 1.7% in real terms. This is not to sugar-coat it, but it was up 0.59% in nominal terms, and would have been up twice that if it weren't for the diminishment of transfer payments.

Bottom line

No sign of recession in this morning's Q3 2011 GDP report. Several key internals point to strong growth in Q4. It's a remarkable and encouraging performance considering the general atmosphere of fear that dominated the quarter. As we've been saying, the economy's weakness is its hidden strength -- it's hard to fall into recession with such a large output gap.

Contact TrendMacro

On the web at
trendmacro.com

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Donald Luskin
Menlo Park CA
650 429 2112
don@trendmacro.com

Thomas Demas
Charlotte NC
704 552 3625
tdemas@trendmacro.com

Lorcan Roche Kelly
Sixmilebridge Ireland
212 537 9067
lorcan@trendmacro.com

John Clinton
Charlotte NC
704 552 3629
jclinton@trendmacro.com

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