STEUBEN TRUST COMPANY

ONE STEUBEN SQUARE • HORNELL, N Y 14843
WWW.STEUBENTRUST.COM • TELEPHONE (800) 588-5010

V I E W P O I N T

THE ECONOMY

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4Q GDP GROWTH RATE SLIPS TO 2.6%

The Commerce Department indicated that its "initial" estimate of 4Q18 GDP growth was 2.6%. This "initial" estimate essentially combined the traditional "advance" and "second" estimates that Commerce typically provides (but was not able to publish in January due to the record-long U.S. government shutdown). The results portray a U.S. economy that remains in excellent shape (the long-term growth forecast for GDP is 2.0%), but is slowing from an unsustainable growth rate above 4% earlier in 2018.

As we typically do for the second estimate, we'll take a closer look at the key contributing sectors to GDP.

* First, the Consumer. During 3Q, Personal Consumption Expenditures grew at a healthy 2.8% pace, just above the rate of overall growth, and contributed 60.9% of core demand (which we define as Personal Consumption Expenditures, Information Technology and Intellectual Property spending, Housing, Exports and Government Expenditures). This is in line with the 10-year average of 60.8%, as the consumer continues to drive the U.S. economy. Drilling deeper, we note a reasonable pick-up in spending on durable goods, which increased at a 5.9% pace, up from 3.7% growth in 3Q.

* Spending on Equipment (generally Cap ex, including Information Technology) and Intellectual Property advanced at a faster rate in the quarter (up 9.9% on average) and accounted for 9.9% of core demand versus the historical average of 8.4%. Looking ahead, we expect that low interest rates and technological innovations will continue to support solid cap-ex spending, though growth may slow if oil prices fall below $50 per barrel.

* Housing has struggled in recent quarters. In 4Q, residential investment declined 3.5%. That's the sixth decline in the past seven quarters. The housing market has recovered from the collapse of 2008-2009 (somewhat slowly, at least compared to the auto market) and does not appear to be in bubble territory. But the Federal Reserve's campaign to raise interest rates has had a clear and negative impact on the sector in recent quarters.

* Exports rebounded in 4Q. Export spending advanced 1.6%, after falling 4.9% in 3Q due to the impact of the trade wars. Looking ahead, we continue to anticipate bumpy trends in export growth in the next few quarters as politicians debate tariffs and trade.

* Government spending remains weak on an historical basis but has strengthened somewhat over recent quarters. Typically, government spending accounts for 17.0% of total demand; but in 4Q18, the share was only 15.2%. We note, though, that the trend in government spending generally has been toward improvement over the past two years.

Our forecasts for GDP growth calls for economic expansion in the 1.5%-2.5% range through 2019. This is lower than the recent trend and reflects the impact of the government shutdown, falling oil prices and strong dollar.

Risks of Recession

Since the current economic expansion began in the fourth quarter of 2009, the economy has grown for 37 quarters in

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a row. In the post-World War II era, the U.S. has experienced 10 periods of economic growth, which have averaged 20 quarters, or five years. The longest expansion was 39 months; the shortest was five.

Recently, expansions have been more durable. The six expansions since 1960 have averaged 27 quarters. But they all end at some point, and it is reasonable to believe that the current expansion is closer to an end than it is to the beginning.

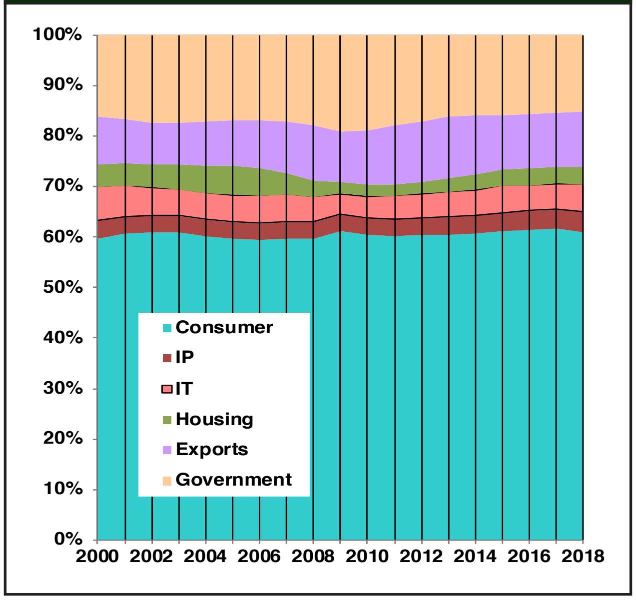
That said, we note that neither our current estimates nor the Fed's forecasts call for a recession in the U.S. through 2020. We believe that key forward-looking indicators -- jobless claims, housing starts, new orders from Purchasing Managers, the stock market and the slope of the yield curve -- are positive enough to keep the economy on a growth track, despite the unpredictable impacts of stock-price swings, global events, weather and other non-economic shocks.

Other risks to growth include volatile oil prices; a weaker-than-expected recovery in China; additional economic trouble in Europe related to Brexit or government finance problems; a dollar that continues to rise and limits export growth; a steep stumble in the housing market or in consumer confidence; or inflationary conditions, which cooled off a bit in the latest GDP report.

In summary, our growth forecasts into 2020 call for GDP expansion in the 1.5%-2.5% range, versus the current rate of growth in the 3% range. Investors likely should expect heightened market volatility as the economy cools off.

John Eade,
President, Argus Research

GDP CONTRIBUTORS



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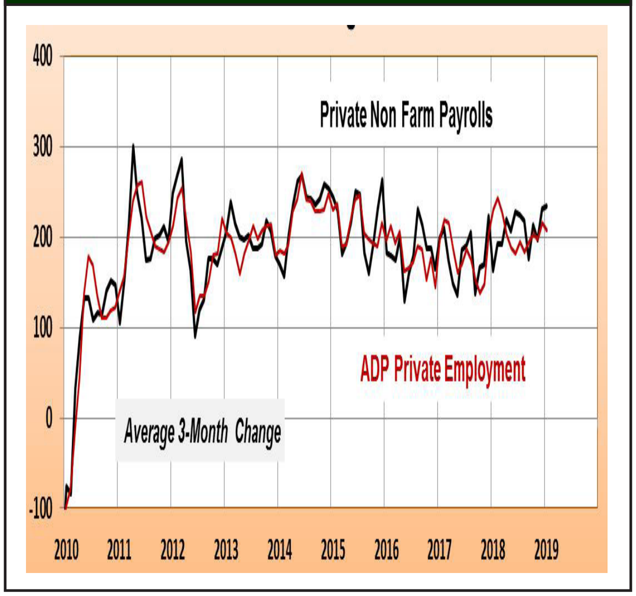
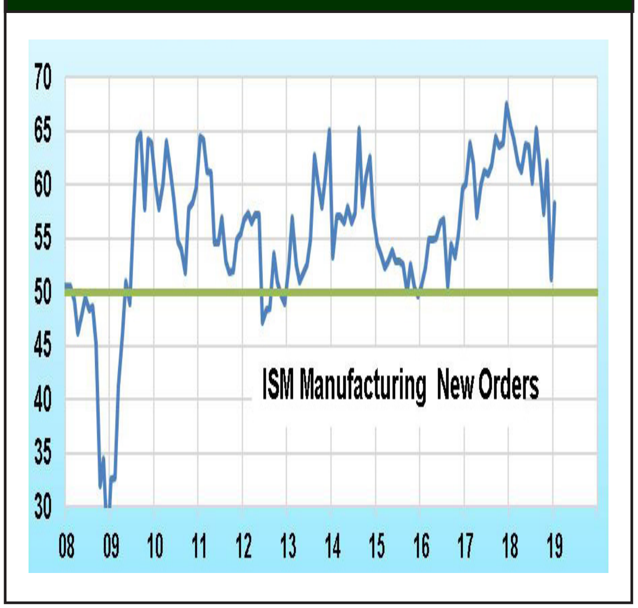
JOB GAINS



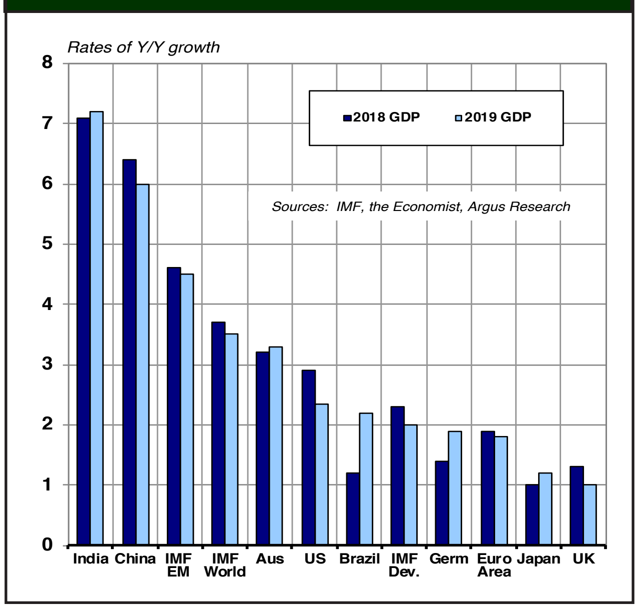
Last year showed the strongest job growth since 2015. Gains in Private payrolls were particularly strong in the fourth quarter and that momentum appears to be carrying over into the first quarter.

ISM NEW ORDERS



ISM New Orders fell 10.5 points to 51.3 in December but rebounded to a strong 58.2 reading in January, boding well for continued manufacturing growth in 2019.

GLOBAL GDP FORECASTS (%)



GDP forecasts around the world are moderating slightly, though the IMF sees stronger global growth for 2019 (3.5%) compared to 2014-2016 (3.1%-3.2%).