Markets Up, NGDP Up

The Week Ending Friday January 26 2018

This was quite a week. The S&P 500 rose 2.4%, Friday-to-Friday, the dollar index was down -1.7% and the GDP report was about as strong as expected, at least on the nominal figures we are focused on. Hard as it is to believe, WTI crude oil is selling for $66 a barrel, no doubt in part a result of the 9% drop in US crude stockpiles from this time last year. While we're at it, let's note the 5-year yield is at 2.47%, the highest level since 2011, though hardly back to a "normal" 3%-6%.

Data

The big news this week was the rather strong Q4 number for nominal GDP. Roughly in line with expectations, the first estimate of last quarter's quarterly growth rate compounds to 5% yearly, after rounding. This is after a 5.3% yearly pace in Q3, a fact that should not be underrated.

The statistical signal of the two latest quarters being so high, has lifted our forecast to a cautious-looking 4.4% year-ahead outlook. The more bearish may see this number as optimistic, the bullish may dismiss it, with dreams of 5.0+%. The statistical model doesn't get caught up in hormonally-mediated optimism or pessimism though, so we just let it run, right now it says 4.4%.

A year-ahead 4.4% for NGDP growth might not look too impressive to those who follow NGDP movements. It is well within what we've seen in the lousy post-recession years. It's worth noting, however, that we've had two growth slumps in recent years, bottoming in 2013 Q2 and 2016 Q2, both around 2.5% year-over-year.

When it comes to the matter of income, it's quite a bit better to have 4.4% of a big number than 2.5%. If we do only get 4.4%, it should still mean improvements in the main economic reports, in corporate profits and in worker pay, as we have been stuck around 3.5% since 2014. There were other data releases, last week, though with the exception of a respectable Durable Goods report, and waning petroleum inventories, they weren't particularly informative nor market-moving.

Down goes the Dollar

It’s an uncommon thing to see a sitting U.S. president talk down the dollar. It seems that Trump himself as well as his Wall Street hostage Mnuchin, favor a weak dollar.

We suspect the upcoming Fed Chairman Jerome Powell will too. Talking about a “strong” or a “weak” dollar in this context is regrettable, though if one were to work for a weaker US dollar through the near term through monetary easing, it would certainly boost the economy.

Be aware, however, when reading financial press, of buying into the contention that a weak dollar boosts the economy primarily through trade. The US is far too big to be an exporting economy, and a weak currency from a change in monetary policy doesn’t make one a competitive exporter in the long term. Printing money can’t turn a country into Japan or Germany. Instead, a weak dollar is simply a side effect of expected higher inflation.

The continued drop in the dollar is providing support to our nominal GDP forecast, which now stands at about 4.4%, using Friday’s GDP figure.

Next Week

The Personal Income report for December comes out on Monday, followed by the Employment Cost Index and Pending Home Sales on Wednesday, Vehicle Sales on Thursday and a jobs report on Friday.

These are among the more important monthly reports, and could be market-moving, but are also for a quarter for which we already have an NGDP estimate. Data won’t be terribly interesting until later in February, when we get monthly reports for January and a revised GDP number for Q4 (potentially shifting the forecast). The markets, of course, are always worth watching.
