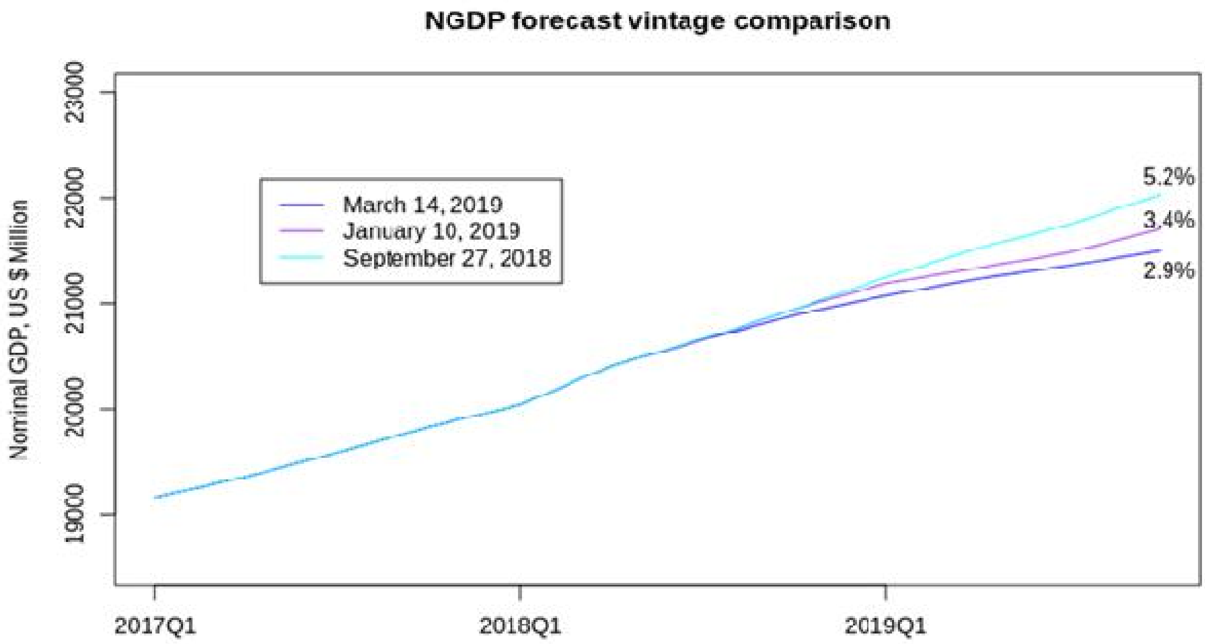
NGDP Outlook Update – Outlook Moves Lower

The NGDP outlook continues to deteriorate. We'd known for a few quarters now that growth was likely to slacken in 2019 compared with the robust 2018, but the combined effects of the market draw down and weaker than forecasted NGDP and NGDI have sapped the model's outlook far beyond what was anticipated.

To put some numbers to it, in late September 2018, our system forecasted about 5.2% year-over-year growth in Q4 2019. The Q4 2019 forecast fell further to 3.4% in mid-January and thence to a meager 2.9% in the latest read.

[Note that if you look at the NGDP forecast plot, these numbers won't necessarily line up, as for simplicity we only publish forecasts for the year-ahead quarter in each vintage, though we do have more detail data as a byproduct of the forecast methodology.]



The plot above compares NGDP forecasts from three recent vintages, in their dollar-value form, as opposed to % change. The less dramatic
dollar-level plot is nevertheless stark to us NGDP-watchers. The first series,
the level forecast for the day of September 27, 2018, was hopeful at 5.2%. This
rate would have seen the improvements in labor force participation, manufacturing employment and wages continue in 2019, however, the financial
market tumble in late 2019 and January 2019 undid this outlook, pulling this
same Q4 2019 figure down to 3.4%. An NGDP figure of 3.4% is unimpressive, and
in line with the trend seen in the bleak Bernanke and Yellen "expansion" years.

The outlook deteriorated further when we received the first print for Q4 2018 NGDP. While the print
was hardly catastrophic, with an annualized quarterly growth rate of 4.6%, this
figure was much lower than the 5.7% model had expected. Because our

model
methodology forecasts NGDP recursively, taking one-quarter steps, then using
the resulting forecast to drive the next quarterly forecast, a big difference
in expectations vs measured reality can derail the forecast. Such a derailment
occurred, sending the Q4 2019 number lower still to 2.9%.

Nominal growth of 2.9% wouldn’t have caused a recession in
say, 2013 or 2016, when firms and households were still scalded from the Great
Recession, and cautiously positioned operationally. However, after the brief
return to “normal” NGDP growth in 2018, we cannot be so certain the economy
retains this robustness. For example, the 2001 recession saw YoY NGDP growth
fall, at worst, to 2.1%. The US economy in 2019 is not the highly leveraged,
complacent network of households and firms which characterized the Great
Moderation economy of 2001, certainly, and we are not calling a recession. This
said, the US worker is now in a vulnerable position.

Physical and labor investments were made in 2017 and 2018
that assumed stronger nominal income growth in the medium term. This leaves the
economy vulnerable to destabilizing realignment as reality is too far from this
assumption. Markets are telling us that growth is liable to be weak over the
next year.