ECONOMIC UPDATE

REGIONS

May 28, 2020

Q1 2020 GDP: "Bad" Is Still "Bad," Just A Little More So . . .

- The BEA's second estimate shows real GDP contracted at an annualized rate of 5.0 percent in Q1 2020
- Pre-tax corporate profits declined by 13.9 percent between Q4 2019 and Q1 2020

Revised and more complete source data show real GDP contracted at an annualized rate of 5.0 percent in Q1 2020, slightly deeper than the BEA's initial estimate of a 4.8 percent contraction. The biggest factor in the downward revision to top-line real GDP is the drawdown in business inventories is now reported to be significantly larger than the BEA first estimated, while the contraction in real private domestic demand is not as severe as was initially estimated. Today's release includes the BEA's initial estimate of Q1 corporate profits; pre-tax corporate profits fell 13.9 percent in Q1 (this is not annualized), the largest decline since Q4 2008 which leaves them down 8.5 percent year-on-year. As is the case with real GDP, the decline in corporate profits in Q2 will be significantly worse than that seen in Q1.

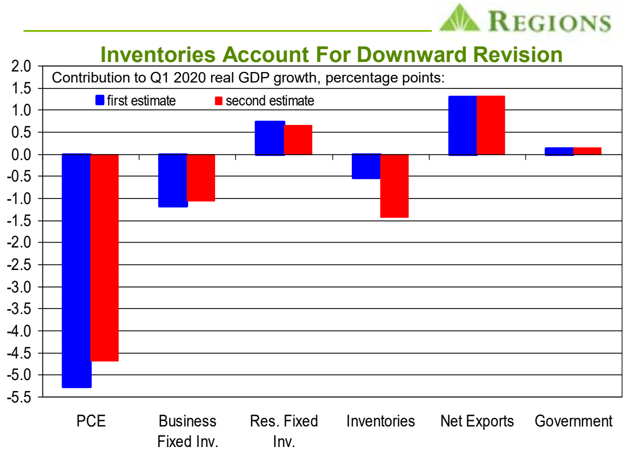
Real consumer spending is now reported to have contracted at a 6.8 percent rate in Q1, compared to the initial estimate of a 7.6 percent rate. The declines in real spending on household services and on consumer durable goods are less harsh than had previously been estimated, while the growth in spending on nondurable consumer goods is now shown to be faster than had previously been estimated.

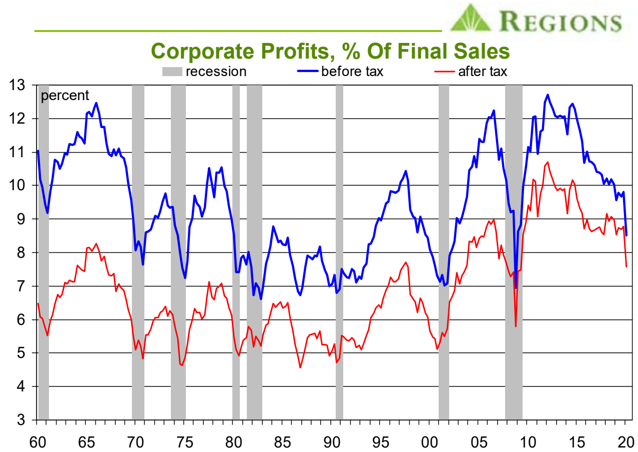
Real business fixed investment contracted at an annualized rate of 7.6 percent in Q1, a bit less harsh than the initial estimate of 8.6 percent. The decline in business spending on structures was less pronounced than had previously been estimated and business spending on intellectual property products grew at a faster rate relative to the initial estimate, and this combination more than offset a downward revision to business spending on equipment and machinery, now reported to have contracted at a 16.7 percent rate. Real residential investment is now reported to have grown at an annualized rate of 18.5 percent in Q1, a downward revision to the initial estimate of 21.0 percent growth. With the revisions to consumer spending and business investment, real private domestic demand is now reported to have contracted at an annualized rate of 5.9 percent in Q1, compared to the initial estimate of 6.6 percent. One reason we focus on private domestic demand is that it is a more reliable gauge of underlying demand, free of the noise from inventories and net exports that can lead to sharp swings in top-line real GDP growth from one quarter to the next though, at present, that may be a distinction without a difference.

Today's release includes the BEA's initial estimate of Gross Domestic Income (GDI), an alternative measure of the size of the economy. In Q1, real GDI contracted at an annualized rate of 4.2 percent, after having risen at a (revised) rate of 3.1 percent in Q4 2019. Real disposable personal income is now reported to have risen at a faster pace in Q1 relative to the initial estimate, with annualized growth of 1.4 percent, with upward revisions to most of the underlying components. Estimates of wage and salary income for Q4 2019 were revised, reflecting the data from the most recent Quarterly Census of Employment and Wages, and this basically put a higher base under the Q1 data.

The other large component of GDI is corporate profits which, as noted above, declined by 13.9 percent in Q1. Domestic profits declined by 14.9 percent in Q1, with foreign profits declining by 10.8 percent, and the decline in profits in the financial sector was harsher than the decline in profits in the nonfinancial sector. Note that the detail on profits across specific industry groups comes with a lag, and in any given quarter are not available until the third estimate of GDP, so it will be another month before we can do any sort of analysis across industries. By that time, however, the focus will have shifted to what will be an even bleaker view of Q2 corporate profits.

That, unfortunately, is a point that can be made more broadly. However bad the Q1 data on GDP and corporate profits may be, we know the Q2 data will be far worse, to a degree that would have been unthinkable prior to the COVID-19 virus. At the same time, however, the prospect of different segments of the economy being opened up in the weeks ahead suggests the contraction in GDP will not persist into the back half of 2020. As we discussed in the May edition of our *Monthly Economic Outlook*, the annualized rates of contraction/growth we'll see over the next few quarters will have little practical context. We think the primary focus should be on how long it will take real GDP to recapture the level seen in Q4 2019, which at present we do not expect before 2H 2022.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com