ECONOMIC UPDATE

REGIONS

April 29, 2021

Q1 2021 GDP: Getting Closer To Where We Started From

- The BEA's initial estimate shows real GDP grew at an annualized rate of 6.4 percent in Q1 2021
- Consumer spending, residential and business fixed investment, and government spending were the main drivers of Q1 growth

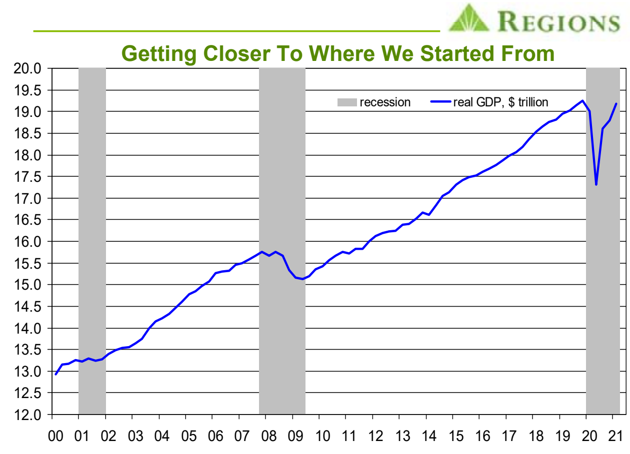
Real GDP expanded at an annualized rate of 6.4 percent in Q1 2021, below what we (7.4 percent) and the consensus (6.7 percent) expected. Our forecast miss in part reflects a larger drag from nonfarm inventories than we anticipated, but also reflects a larger increase in the GDP Price Index – up at an annualized rate of 4.1 percent – than we anticipated, which held down the level of inflation adjusted GDP. Consumer spending, residential and business fixed investment, and government spending were the drivers of Q1 growth, more than offsetting drags from net exports and inventories. As we do each quarter, we'll note that the BEA's initial estimate of GDP in any given quarter is based on highly incomplete source data and, as such, is prone to sizable revision. As the data now stand, however, the level of real GDP as of Q1 is $19.09 trillion, which is 0.86 percent below the level as of Q4 2019, the last quarter before the effects of the pandemic and the efforts to stem its spread began working their way through the economy. The remainder of that gap will easily be filled in during Q2.

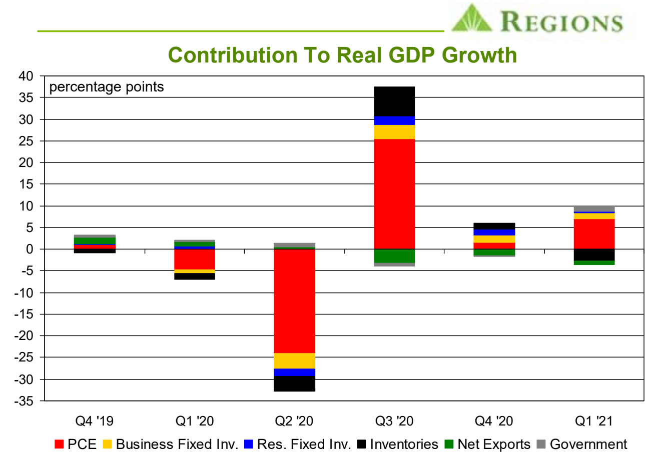
Real consumer spending grew at an annualized rate of 10.7 percent in Q1, adding 7.02 points to top-line real GDP growth. Real spending on goods grew at an annualized rate of 23.6 percent, with spending on consumer durable goods such as motor vehicles, furniture, and appliances, rising at an annualized rate of 41.4 percent. Real spending on household services grew at a more sedate (annualized) rate of 4.6 percent in Q1. Patterns in consumer spending shifted markedly during the pandemic, reflecting much of the services sector being shut down or allowed to operate at only partial capacity and the magnitude of fiscal transfers to the household sector. As such, spending on goods grew dramatically, to the point that as of Q1 2021 the level of real consumer spending on goods is 12.5 percent above the level of Q4 2019. In contrast, real spending on services is 5.7 percent below the level of Q4 2019, but this figures to be the area in which we will see the biggest gains in consumer spending in the months ahead as more and more people are vaccinated and the economy more fully reopens. Clearly consumers will have the means to ramp up spending on services, with the personal saving rate rising to 21.0 percent in Q1. Recall that the second round of Economic Impact Payments hit in January, and the third round hit in March, which contributed to disposable personal income rising at an annualized rate of 61.3 percent in Q1. To put the impact of fiscal transfers in perspective, excluding transfer payments, real disposable personal income grew at an annualized rate of 0.2 percent in Q1.

Real business fixed investment grew at an annual rate of 9.9 percent in Q1, with robust growth in spending on equipment and machinery and intellectual property products more than offsetting a decline in spending on business structures, the sixth consecutive quarterly decline. Firms have spent heavily on computer and communications equipment and on software over the course of the pandemic, thus facilitating remote work arrangements. At the same time, spending on industrial equipment and machinery has grown at a rapid rate, in part reflecting firms upgrading capital stocks, something that had long been overdue. Outlays on research and development account for the bulk of spending in the intellectual property products category, and higher R&D spending tends to lead faster growth in labor productivity. We see further upside room for business investment over coming quarters even if the rate of growth slows. Single family construction continues to drive growth in total residential fixed investment, which grew at an annualized rate of 10.8 percent in Q1. Total government spending grew at an annualized rate of 6.3 percent in Q1, with federal government spending rising at a 13.9 percent rate and state and local government spending rising at a 1.7 percent rate.

To the downside, the trade deficit widened in Q1, with imports growing at a 5.7 percent rate and exports contracting at a 1.1 percent rate. The wider trade deficit took 0.87 percentage points off of top-line real GDP growth. Nonfarm business inventories fell sharply in Q1, knocking 2.64 percentage points off of top-line real GDP growth. This could remain a drag on growth over coming quarters given that supply chain/logistics issues continue to hamper growth in manufacturing output.

Though by no means clear of the downside risks posed by the COVID-19 virus, the next few quarters will be marked by robust real GDP growth. The answer to the "okay, then what?" question has yet to be determined.





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