ECONOMIC UPDATE

REGIONS

April 30, 2025



## Q1 2025 GDP – 1st Estimate: Surge In Imports Sinks GDP; Private Domestic Demand Solid

- The BEA's initial estimate shows real GDP <u>contracted</u> at an annualized rate of 0.3 percent in Q1 2025 after growth of 2.4 percent in Q4 2024
- Net exports were a major drag on Q1 real GDP, more than offsetting strong growth in real private domestic demand

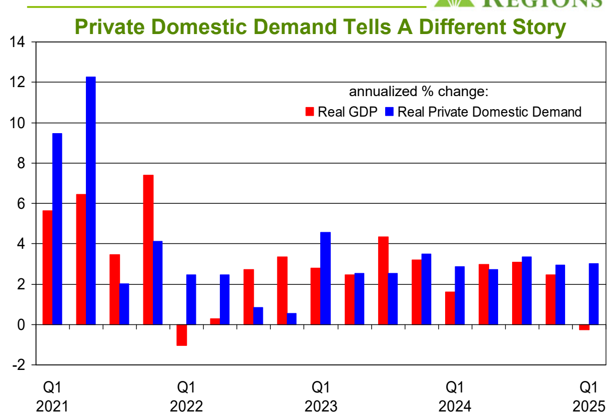
The BEA's initial estimate shows real GDP contracted at an annual rate of 0.3 percent in Q1 as a surge in imports into the U.S. countered a solid advance in private domestic demand (combined business and household spending). Initially, we had expected real GDP to increase at an annual rate of 0.4 percent, but in light of yesterday's release of the advance data on trade in goods for the month of March, which showed a significantly wider deficit than expected, we revised our forecast down, as did many of our counterparts. Our revised forecast anticipated real GDP would contract at an annual rate of 0.8 percent. Either way, we've long argued that real private domestic demand is a more reliable gauge of the underlying health of the U.S. economy, but the headline real GDP growth print and the 3.0 percent annualized growth in real private sector demand in Q1 have this in common – both were heavily swayed by the prospect of higher tariffs leading to higher prices and/or shortages of inputs to production and finished goods in the months ahead. Indeed, the Q2 data could easily show real GDP growth outperforming growth in private sector demand as the data will inevitably bring reversals for much of what we see in the Q1 data. As for what this all means for the economy going forward, about as precise as we can be at this point is to say that there is an unusually wide range of potential economic outcomes which, loosely translated, basically means that your guess is probably as good as ours.

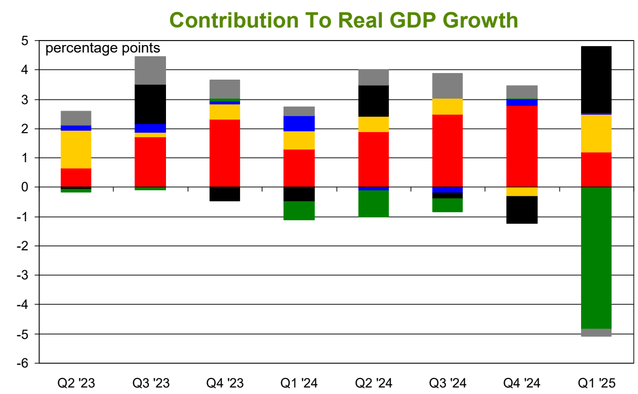
In any given quarter, the BEA's initial estimate of GDP is based on highly incomplete source data, and as the holes in the data are plugged and prior estimates are revised, the estimate of real GDP can change materially. We'll be watching for revisions to the initial estimates of Q1 net exports and inventory accumulation. The initial estimate shows imports of goods grew at an annual rate of 50.9 percent in Q1, swamping growth in U.S. exports and leading to a significant widening in the trade deficit. This knocked 4.79 percentage points off top-line real GDP growth. To the extent that the surge in inventories reflected manufacturers and retailers pulling orders ahead to avoid higher tariffs, it is unsurprising that Q1 also saw a significant build in inventories, which added 2.25 percentage points to top-line real GDP growth. Still, we anticipated a larger build in stocks in Q1, and given that BEA does not yet have full-quarter data on business inventories, subsequent passes at Q1 GDP may show a narrower gap between the increase in imports and the increase in inventories. Also, as there are already clear signs of a marked slowdown in global trade flows, imports of goods are likely to fall sharply in the Q2 data while inventories will likely be pared down, perhaps significantly. As such, the effects on measured GDP seen in Q1 will to some extent reverse in the Q2 data.

As noted above, real private domestic demand grew at an annual rate of 3.0 percent in Q1, easily ahead of our forecast. Real consumer spending grew at an annual rate of 1.8 percent, slower than the 4.0 percent growth seen in Q4 2024 but ahead of our forecast. Keep in mind that spending patterns were meaningfully distorted by atypically harsh winter weather in January and February, some of which was made up for in March. That, combined with purchases of consumer durables being pulled forward, led to a sizable increase in consumer spending in March. For instance, unit sales of new motor vehicles rose to an annual rate of 17.8 million units in March, the fastest monthly sales rate since April 2021. While the data show vehicle sales were strong through the middle of April, subsequent months will bring payback which, along with signs of weakening demand for discretionary services spending, sets up further slowing in the growth of real consumer spending going forward.

Real business fixed investment grew at an annual rate of 9.8 percent in Q1, adding 1.29 percentage points to top-line real GDP growth. Outlays on equipment and machinery grew at an annual rate of 22.5 percent, with growth in spending on information processing equipment growing at a rate more than three times faster. This is one area where businesses pulled purchases forward in anticipation of higher tariffs. More broadly, the data on core capital goods orders over the past several months showed signs of pre-emptive ordering and, much like in the consumer spending space, coming months will bring payback that will weigh on GDP growth as soon as the Q2 data. Residential fixed investment was a modest support for Q1 GDP, but that too is likely to reverse in the Q2 data.

We'd argue that the economy is neither as troubled as implied by Q1 real GDP growth nor as robust as implied by growth in real private domestic demand. It does, however, seem clear that the economy continues to slow, and the two measures are likely to converge over coming quarters.

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