
# Yesterday The Beatles, 1965

The numbers are out: the US economy grew by 2.6% over the fourth quarter of 2018, well above most economists' expectations and above ours. Recession was not on the cards for 2018 and market pessimism in December was overdone. However, this GDP number harks back to yesterday. We think that investors should focus on what is happening between now and tomorrow. Now looks decent but tomorrow seems worse and we are still struggling to gauge the extent of this deceleration. Any market collapse is a combination of a deteriorating macro situation and a trigger: these triggers are by essence hard to anticipate but we can think of a good number of them, from a monetary policy mistake to a negative growth shock in the Eurozone or the materialisation of trade tensions on the economy. This makes the macro analysis of the current situation all the more important. The world is indeed slowing down and we remain convinced that the performance and situation of tomorrow will not be nearly as good as that of *Yesterday*.

## WHAT'S NEXT?

**A decent yet blurry US picture in Q4**

Many market observers were prepared for disappointment, but Q4 US GDP growth came out at 2.6%, rather than the 2.2% as anticipated by economists, comfortably beating expectations. Over the past quarter, still-decent consumption continued to support overall growth: that was particularly the case with durable goods consumption, which grew by nearly 6% with most of this figure coming from solid growth in vehicle sales. Non-durable goods consumption on the other hand, grew slower than in the past as clothing sales grew at a much slower pace. Non-residential investment, most of it reflecting corporate investments, continued to grow at a slow pace, the way it has since the end of the Great Financial Crisis. Finally, the blot on the landscape is clearly the housing market: residential investment declined by 3.5% this quarter, the fourth quarterly decline in a row.

We follow the evolution of economic growth on a daily basis using our proprietary nowcasting indicators. These indicators combine a large number of real-time data series into a gauge of current economic activity. How is this GDP growth number consistent with our US Growth Nowcaster? At a global level, significantly: across Q4, our Growth Nowcaster remained above the zero line, indicating above-potential growth (1.5% according to IMF's estimates). Digging into the components, we expected consumption growth to remain good while investment was also expected to be a net positive contributor. The "housing" component has been negative over the past two quarters: here again, the latest GDP readings are nothing but consistent with our signals.

However, this number remains surprising from two angles: first, it is quite elevated given the intensity of the slowdown in the macro indicators. Across the fourth quarter, 55% of the underlying data feeding into our US Growth Nowcaster deteriorated. This deceleration actually started in November, with the economic impetus still strong in October when 53% of the data was still improving, meaning that most of the deceleration happened in an increasing way towards the end of the year. The second surprising element is durable goods consumption. It came out quite strong although we have witnessed early signs of a slowdown in long-term consumption decision-making across the fourth quarter. Here again, a distinction must be made between what happened at the beginning and at the end of the quarter. A significant part of the macro deceleration we observed actually happened at the end of it, partly explaining the still elevated growth figures.

**A slowdown is on the cards**

Our focus is not on past data, but rather on what comes next: how did our indicators evolve since the start of the year, now that we are entering into the last month of this quarter? Put bluntly, the deceleration is still there: every component in our US Growth Nowcaster points to slower growth conditions. The housing component remains negative. Compared to a year ago, consumption-related data is slowing. Production expectations moved from very high levels back to their long-term level, while investment perspectives and financing conditions did the same. From the perspective of these indicators, Q1 GDP growth is unlikely to be higher than Q4 last year: deceleration is coming our way and a 2% growth for Q1 would barely come as a surprise given the consistency of the growth deceleration across the different components of our Nowcaster. We are not the only one seeing this deceleration: the New York Fed nowcaster expects +1.2% for Q1 while the Atlanta Fed nowcaster reached +1.9%. With analysts discounting a +7% earnings growth across S&P500 firms, these companies will need to have strong sales exposure to regions with stronger GDP growth – if there are any.

When it comes to the rest of our nowcasters, their message is consistent: most of the developed world is decelerating, with 60% of the data deteriorating across it, according to our estimates. Our Canadian Growth Nowcaster hints at entry into a recession for the first quarter of this year. Another two months of deceleration and the Eurozone should also enter into a recession. The UK situation is no better: what used to be a Eurozone deceleration has now become common to all developed economies. This slowdown remains young by historical standards, but again, we are more focused on tomorrow rather than on yesterday's situation.

If the current trends remain in place, what we read in our indicators is a definitive call for cautiousness. But the road until the breaking point can be long. March 2006 is an interesting reference point: the US housing sector contracted in the midst of a world deceleration. It still took another 15 months until a large enough trigger occurred. Patience and caution are essential.

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