First Trust
Monday Morning OUTLOOK

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Foreign Slowness Not an Obstacle

Brian S. Wesbury – *Chief Economist*
Robert Stein, CFA – *Dep. Chief Economist*
Strider Elass – *Senior Economist*

One consistent theme we've heard lately among pessimistic analysts and investors is that slower growth abroad is a headwind for economic growth in the US. Softness in Europe or China, they say, bodes poorly for the continuation of US expansion. The standard theory, the conventional wisdom, is that slower growth abroad means slower growth in US exports.

Superficially, there is some data to back up that theory. Over the past four quarters, real GDP expanded 1.5% in the 28 countries that make up the European Union, the slowest pace since 2013. China's real GDP is up 6.4% from a year ago, the slowest gain in decades.

We have some relatively good recent news out of Japan, where real GDP expanded at a 2.1% annual rate in the first quarter. But real GDP in Japan is up only 0.8% from a year ago versus a healthier 1.4% gain the years ending in the first quarter of 2017 and 2018. (Remember, Japan's population has been shrinking so their GDP growth rates have been, and will remain, persistently lower than in the US).

By contrast, US growth has been accelerating. Real GDP rose at a 3.2% annual rate in the first quarter, and was up 3.2% from a year ago, at least according to the report released a month ago. A revised report on GDP arrives Thursday, and we anticipate mild downward revisions on net, but the figure for first quarter growth should remain near 3.0%.

The recent trend in real GDP growth is a clear acceleration from the average annualized growth rate of 2.2% seen during the Plow Horse recovery from mid-2009 through early 2017. Even more impressive is the acceleration in productivity growth, which averaged 1.1% annualized during the Plow Horse era but grew 2.4% in the past year.

In other words, the data already contradict the pessimistic theory that slow growth abroad will cause the US to decelerate.

So why is this happening? What could explain why the US has been so resilient relative to major economies abroad?

Under "normal" conditions, the pessimistic theory could make sense. If foreign countries have less purchasing power, then, yes, that could be a headwind for the US. Imagine a town where the local ranchers produce less; yes, obviously that can be a problem for local restaurants and merchants who sell to those ranchers.

But US growth has accelerated thanks to changes in policy; a combination of lower marginal tax rates - particularly on corporate profits - as well as deregulation.

That policy-led acceleration in US growth is also why some major foreign economies are doing worse. Lower tax rates and deregulation have made the US a better place to conduct business activity and have made other countries with similar standards of living (Europe and Japan) relatively worse. We think the data will ultimately show that businesses have shifted resources in response to the new direction of US policy, which means less activity than would otherwise be the case for our trading partners.

China, too, has been affected by the trade conflict. For the past 20 years, US presidents of both major parties have looked the other way while China pirated our intellectual property. That policy – or "non-policy" – represented a huge subsidy for China. Now that indirect subsidy looks like it's coming to an end.

None of this means we are rejoicing that foreign economies are growing more slowly. We're not. We're merely pointing out that foreign growth and US growth are de-coupling. The US is now picking up growth because of more competitive policies. These new policies are reducing the previous incentives which damaged US competitiveness, and often pushed growth overseas.

Don't panic if, and when, you hear of slow growth abroad. A large part of the reason is better policies in the US, which will help support growth here.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
5-30 / 7:30 am	Initial Claims May 25	215K	**215K**		211K
7:30 am	Q1 GDP Preliminary Report	3.0%	**2.9%**		3.2%
7:30 am	Q1 GDP Chain Price Index	0.9%	**0.9%**		0.9%
5-31 / 7:30 am	Personal Income – Apr	+0.3%	**+0.3%**		+0.1%
7:30 am	Personal Spending – Apr	+0.2%	**+0.2%**		+0.9%
8:45 am	Chicago PMI	54.0	**53.8**		52.6
9:00 am	U. Mich Consumer Sentiment- May	101.0	**102.0**		102.4