Negative Q2 GDP Signals Technical Recession

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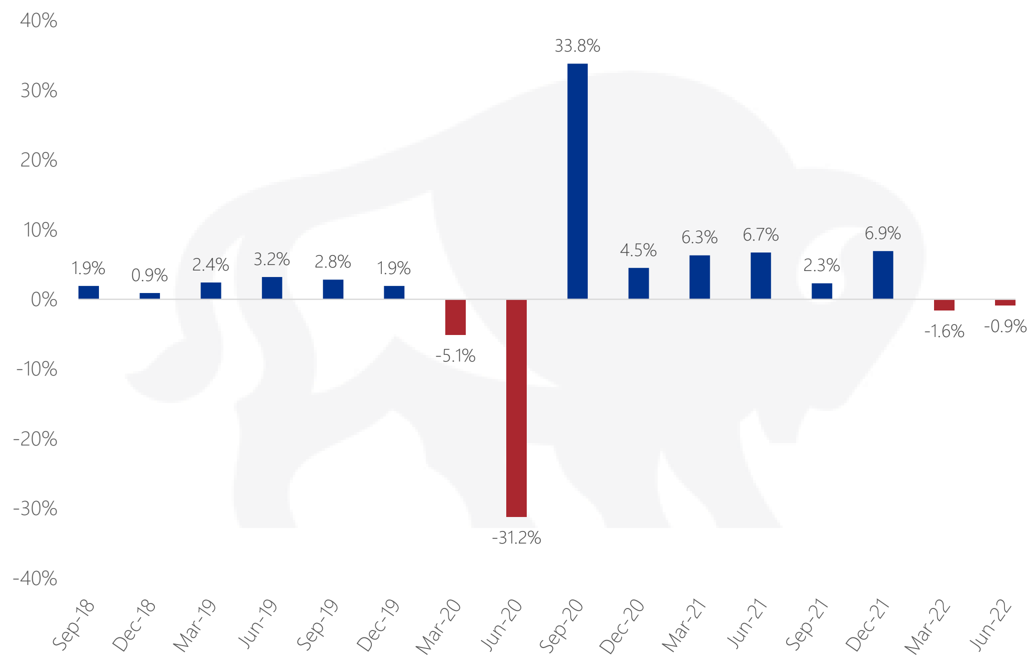
The U.S. economy unexpectedly contracted for the second straight quarter. Although this doesn't necessarily mean the country is in recession, two consecutive quarters of negative growth is the textbook definition. Ultimately, the National Bureau of Economic Research (NBER) will make the official call months from now based on a number of variables.

GDP fell -0.9% in the second quarter, significantly weaker than the +0.4% median forecast, following a -1.6% decline in the first quarter of the year. The worst performing sector was private investment, which was responsible for carving 2.7 percentage points from the headline. Within that number, residential investment (housing) subtracted 0.7.

U.S. GDP - Quarterly Annualized Percent Change



Source: US Census Bureau

Personal consumption (consumer spending) held up reasonably well, up +1.0% for the second quarter following a +1.8% increase in the previous period, and adding 0.7 to overall GDP. The consumption breakdown showed a significant shift from goods to services during the quarter with goods purchases subtracting 1.1 percentage points and services adding 1.8. The NBER views consumption, along with labor market health as primary factors in determining recession. Anyone arguing that the U.S. isn't in recession will point to these two areas of growth.

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In the first quarter, net trade and business inventories combined to subtract a massive four percentage points, and were entirely to blame for the overall Q1 contraction. The prevailing thought at the time was that both categories would make *positive* contributions in the second quarter. As it turned out, net trade did add 1.4 percentage points as exports improved, but inventory accumulation was weak yet again, subtracting two full percentage points.

Government spending declined for the third consecutive quarter, subtracting 0.3 from overall GDP.

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Bond yields have fallen sharply in early trading as investors grapple with the notion that the Fed will be less determined to hike rates to slow economic growth if the economy has already stalled. However, inflation is still at a 41-year high and taming price pressure remains job one for Fed officials. Thus, another large rate hike (50 bps) is still expected at the September FOMC meeting with a 25 bp increase expected in November. The futures market is still indicating a 25 bp hike at the December meeting, but this move is no longer fully priced in. *After December, the market is indicating the first move in 2023 will be a rate cut.*

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It's important to remember that between now and the September FOMC meeting, Fed officials will see two CPI reports, two retail sales reports, and the first of two GDP revisions. *Nothing's certain...except volatility*.

Stocks are down this morning, but the notion of a less aggressive Fed should generally be positive for equities going forward.

Market Indications as of 9:19 A.M. Central Time

DOW	Down -153 to 32,044 (HIGH: 36,800)
NASDAQ	Down -102 to 11,930 (HIGH: 16,057)
S&P 500	Down -16 to 4,008 (HIGH: 4,797)
1-Yr T-bill	current yield 2.90%; opening yield 2.93%
2-Yr T-note	current yield 2.88%; opening yield 2.98%
3-Yr T-note	current yield 2.81%; opening yield 2.93%
5-Yr T-note	current yield 2.69%; opening yield 2.81%
10-Yr T-note	current yield 2.67%; opening yield 2.75%
30-Yr T-bond	current yield 2.98%; opening yield 3.04%