

Upcoming Fed Meeting Should be Mercifully Dull

The highlight of a mostly quiet economic week was Thursday's release of Q1 GDP and Q1 personal consumption expenditures (PCE), which combined to imply an unwelcome combination of slower growth and rising prices.

Real GDP grew at an unexpectedly soft +1.6% quarter-over-quarter annualized pace during the first three months of 2024, well below the +2.5% Bloomberg median forecast and the weakest since Q2 2022. *Note that this measure is adjusted for inflation which was higher than expected during the first quarter, so the real number is lower than it would have been otherwise.*

Personal consumption (consumer spending), which historically contributes the vast majority of GDP growth, rose at a +2.5% pace during the quarter, lower than the median forecast (+3.0%) and the previous period (+3.7%). Fixed business investment, residential investment (new home construction) and state and local government spending were among the positive contributors. Housing, which has subtracted from growth during much of the pandemic era, contributed half a percentage point to the overall number.

Imports rose considerably more than exports, reflecting recent dollar strength and resulting in a decrease in net trade which subtracted 0.9 percentage points from the headline, while lower business inventories subtracted another 0.4. Real final sales, which exclude the volatile inventory component and are probably a more indicative growth measure, were up +2.0%.

Core PCE for the first quarter was released at the same time as GDP and unfortunately this key inflation indicator came in higher than expected. The +3.7% reading was above the +3.4% median forecast, but more importantly (from an optics perspective) nearly twice the +2.0% pace of the previous quarter.

If weakening Q1 GDP wasn't accompanied by the quarter-over-quarter inflation surge, the bond market would have likely rallied, but the scent of "stagflation" resulted in a selloff in both stocks and bonds.

Yesterday's warmer Q1 price data, *which obviously includes last month*, hinted at upside risk to this morning's March PCE deflator release. So, the fact that both headline and core PCE came in *as expected* for the month (+0.3%) was a relief and has prompted a modest rally today in both stocks and bonds. On an annual basis, core PCE held steady at +2.8%, matching the median forecast.

Today's rally indicates Thursday's reaction to slower growth and rising inflation was a bit overdone. In all fairness, the first quarter inflation story had been widely telegraphed by three ugly CPI readings and the bond market had already sold-off in response. The first month of the second quarter is almost over and very early *Nowcast* indications by the Cleveland Fed suggest some cooling in April.

Scott McIntyre, CFA

HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2009
scott.mcintyre@hilltopsecurities.com

Greg Warner, CTP

HilltopSecurities Asset Management
Senior Portfolio Manager
Managing Director
512.481.2012
greg.warner@hilltopsecurities.com

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The GDP data is still subject to two revisions and both net trade and business inventories are notoriously volatile, so it's premature to assume a downtrend.

The Fed meets next Wednesday, although this might be an uncharacteristically uneventful meeting. There will be no rate change announcement, no updated summary of economic projections, no fresh dot plot, and with so many Fed officials (including Powell) weighing in with opinions last week, the market has already digested Fed thoughts. This week's data releases are unlikely to change that thinking.

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Market Indications as of 11:18 A.M. Central Time

DOW	Up 167 to 38,253 (HIGH: 39,807)
NASDAQ	Up 314 to 15,925 (HIGH: 16,442)
S&P 500	Up 51 to 5,100 (HIGH: 5,254)
1-Yr T-bill	current yield 5.19%; opening yield 5.17%
2-Yr T-note	current yield 4.98%; opening yield 5.00%
3-Yr T-note	current yield 4.83%; opening yield 4.85%
5-Yr T-note	current yield 4.68%; opening yield 4.72%
10-Yr T-note	current yield 4.67%; opening yield 4.71%
30-Yr T-bond	current yield 4.79%; opening yield 4.82%

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