Amid historic GDP plunge, economists temper predictions of Q3 surge

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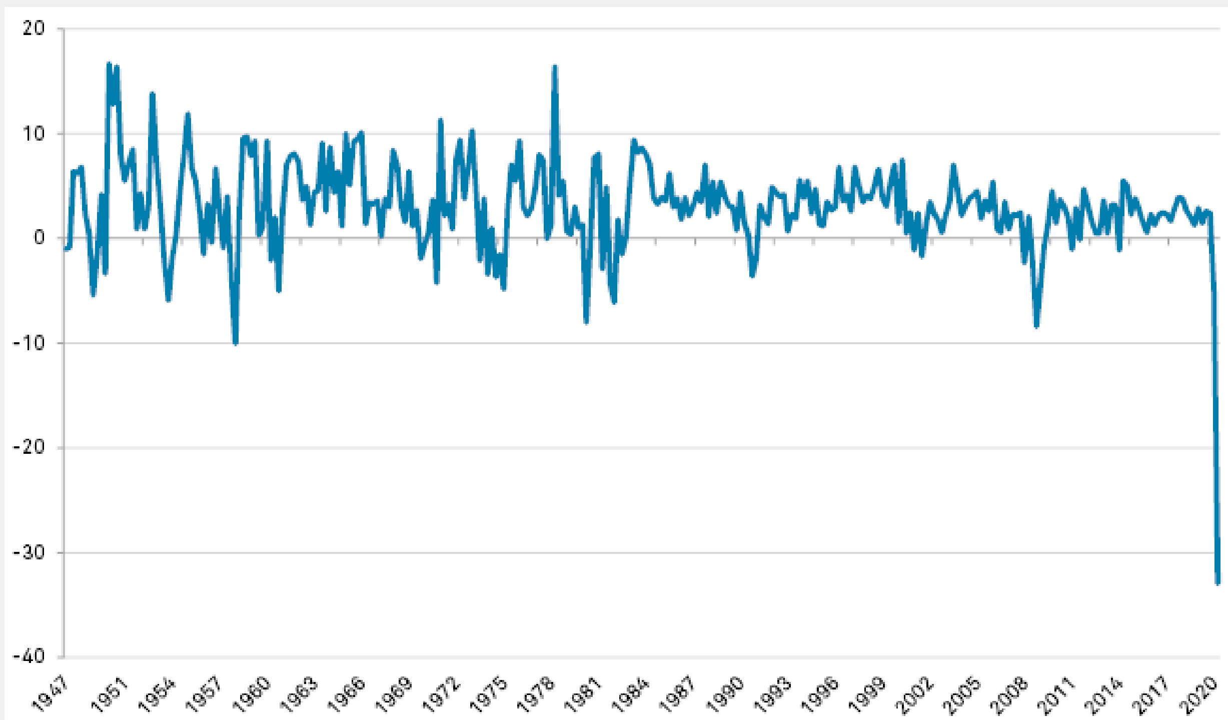
After a record drop in real GDP, the U.S. economy is widely expected to stage a frantic rebound in the third quarter, but stalled unemployment relief and persistent outbreaks of the coronavirus are beginning to temper those hopes.

Second-quarter GDP fell at a 32.9% annualized rate from the first quarter as real personal consumption expenditures were down 34.6% on an annualized basis, residential investment fell 38.7% and U.S. exports plunged by 67.6%. The previous largest annualized decline in quarterly GDP was 10% in 1958, according to Bureau of Economic Analysis data that goes back to 1947.

The contraction could have been even worse, said Rajeev Dhawan, director of the economic forecasting center at Georgia State University. Projections had reached as dire as a 45% annualized drop several weeks ago, but the actual decline was mitigated in part by the consumption rebound in May and June when states began to reopen and purchases of durable goods like furniture and computers rose as more people worked from home, Dhawan said.

US GDP sees historic plummet in Q2 (%)



Data compiled July 30, 2020.
The data represents annualized quarterly change in GDP.
Source: U.S. Bureau of Economic Analysis

Looking ahead to the third quarter, forecasts call for big jumps as the lockdowns imposed in April and May have been largely lifted, but some have been revised downward amid the recent resurgence of COVID-19 and the dialing back of states' reopenings, including in Florida, Texas and California, which account for roughly 20% of annual U.S. GDP.

That, coupled with still-elevated jobless numbers and federal unemployment insurance benefits expiring, point to a drag on future GDP gains.

"We've been expecting a slower and longer climb back from the bottom, but now with the signs that COVID-19 is not necessarily contained, it's going to be even slower than that," Beth Ann Bovino, chief U.S. economist for S&P Global Ratings, said in an interview.

Bovino projects a 22.2% annualized jump in third-quarter GDP, a forecast that assumes Congress renews the federal unemployment insurance benefits enacted under April's CARES Act at its $600-per-week level. However, should it be reinstated at $400, the midpoint of Republican and Democratic proposals, that estimate dips to 18%.

"Even with this [third-quarter] jump, we are still far from climbing out of the hole," Bovino said. "I am concerned that this 22% came before new social distancing restrictions across regions were implemented. There's nothing but downside for the forecast."

Among the most critical elements of consumption is healthcare spending, Dhawan said, which was down $472.6 billion in Q2.

"This number will come back. It's just a question of how much," Dhawan said. "If the virus spreads again, the elective procedures will again come down. That’s why the virus dictates the timeline and the speed and strength of recovery."

Wells Fargo Securities forecasts 18% growth in third quarter GDP, a projection it revised downward by 6 percentage points due to the recent acceleration in U.S. coronavirus cases and subsequent pause button hit by states in their reopening efforts. It is also basing its prediction that a generalized lockdown similar to the one the U.S. saw in March and April does not reoccur.

It will likely take several years for the economy to return to pre-pandemic levels, said Jay Bryson, Wells Fargo's acting chief economist. He estimated that the U.S. unemployment rate, which was 3.5% in February and 11.1% in June, will recede to 8% at the end of 2020 and stay elevated at 6% at the end of 2021.

Even with the recovery, Wells Fargo projects that GDP in the fourth quarter of 2021 will be roughly 3% lower than the same period in 2019.

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