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Economic Forecaster Advises Patience for Remainder of 2018

ATLANTA–Following a quarter-point rate hike in March, expect the Federal Reserve to raise rates twice more this year, according to Rajeev Dhawan of the Economic Forecasting Center at Georgia State University's J. Mack Robinson College of Business.

"We will get a rate hike in June," Dhawan wrote in his "Forecast of the Nation," released today (May 23). "Then the Fed will wait until December to see the impact of its previous hikes.

"Two factors may come in to play as the Fed waits to take further action," Dhawan said. "First, evidence has to emerge that tax cut-induced consumer spending is finally taking hold as weak retail sales numbers in the first quarter were a snapback from a hurricane rebuilding spending surge in the last quarter of 2017. But the real reason to wait between hikes is to allow the factors that determine a rise in long-bond yields to play out."

Despite other forecasters and members of the media signaling that an inverted yield curve could be on the horizon, potentially indicating a recession, Dhawan believes the Fed can hold off these concerns.

"Recession talk is premature," Dhawan wrote. "What happens to the long-bond yield as the Fed hikes rates is key. Long-bond yields are determined both by global capital flows (especially foreign demand for Treasurys) and the domestic debt issuance in response to the federal fiscal deficit. Global capital flows may fluctuate with the volume of trade but it's clear given the recent budget passage of spending increases and last December's tax cuts that issuance of Treasury bills is expected to rise sharply in the coming quarters."

Dhawan expects a steady rise in the long-bond yields.

"After the two remaining hikes in 2018, expect two more in 2019 and one in 2020. This is a perfect soft-landing forecast with no recession," said Dhawan.

Dhawan advises patience when reviewing poor consumption and retail sales figures from the first quarter.

"Consumers have just begun to experience the tax cuts in their paychecks, but they still haven't registered fully," Dhawan said. "Some purchasing power has been eaten away by elevated gas prices, which will delay the impact of the tax cut led spending boom small businesses are eagerly awaiting."

Gas prices have soared, mostly because of a catastrophic drop-off in imports from Venezuela as OPEC producers have kept supply constant. Dhawan expects oil to level off in the $70 per barrel range for the remainder of 2018, but cautions any NAFTA trade fallout involving Canada, which provides 50 percent of oil imports, could be devastating.

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The forecaster expects job growth to remain around the same level due to a slight pickup in business investment.

“We heard a lot of companies making plans to bring back their cash from abroad, but it seems to have gone into share buybacks,” Dhawan wrote. “Tax changes take time to filter through, and businesses require much calmer financial markets than we are currently experiencing.”

As a result of this corporate investment, Dhawan expects GDP to grow by a strong 2.9 percent in 2018. Growth in 2019 will be 2.4 percent, then further moderate to 1.8 percent in 2020.

The forecast has a caveat: No major trade war or skirmish in the coming quarters. Skirmishes at the physical level, including tariffs on goods by each side, are easy to analyze and may not be even that costly.

“But, the biggest unknown of trade actions is their impact on global capital flows,” Dhawan said. “If tariffs on our major trading partners, especially China, drive them out of the U.S. Treasury market, it will make 10-year bond yields rise in three months. In a normal forecast, that would happen in three years.”

If such a scenario occurs, Dhawan said all bets on a soft landing are off.

“But, forecasting the probability of a trade war is more dependent upon political calculations than economic logic,” said Dhawan. “Thus, we aren’t forecasting it, but cannot deny this as a potential outcome.”

Highlights from the Economic Forecasting Center’s National Report

- Following GDP growth of 2.3 percent in the first quarter of 2018, the economy will expand at 2.9 percent in 2018, 2.4 percent in 2019 and 1.8 percent in 2020.
- Business investment grew 6.1 percent in the first quarter of 2018. Growth will settle at 5.9 percent in 2018, 4.8 percent in 2019 and 3.8 percent in 2020. Jobs will grow by a monthly rate of 180,200 in 2018, 158,700 in 2019 and 111,800 in 2020.
- Housing starts will average 1.297 million units in 2018, fall slightly to 1.267 in 2019 and rise again to 1.303 in 2020. Expect auto sales of 17.0 million units in 2018, 16.2 in 2019 and 16.0 in 2020.
- The 10-year bond rate will average 3.2 percent in 2018, 3.9 percent in 2019 and 4.0 percent in 2020.

Small Businesses Set to Benefit from Tax Cut, But Not Enough to Break Moderating Trend

ATLANTA–Positive tailwinds triggered by income tax cuts are expected to provide a big boost to small businesses but will not be enough to overcome global headwinds, according to Rajeev Dhawan of the Economic Forecasting Center at Georgia State University’s J. Mack Robinson College of Business.

“International headwinds from tariff talk will create jitters in globally connected sectors, and moderation in catalyst sector job growth will produce trickle-down impacts throughout the Georgia labor market,” Dhawan wrote in his quarterly Forecast of Georgia and Atlanta, released today (May 23). “Maintaining the 2017 pace of 72,100 job additions will be a real victory, as that number was a 30 percent drop from the 101,600 jobs gained in 2016.”

Even with benchmarking revisions that turned manufacturing job losses into superlative job gains, job creation in this important catalyst sector has been moderating since 2014. The chief reasons were weak global growth, especially among top export destinations, combined with a strengthening dollar in the 2014-16 period. Even as the dollar has weakened in the last few months, it will take time for this to play out for this sector. Meanwhile, this catalyst sector saw a reduction of 100 jobs in the first quarter of 2018.

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"However, recent news related to manufacturing goods for domestic consumption as well as relocation of small manufacturers from Europe remains favorable," Dhawan wrote. "We still expect job growth in manufacturing, but it will take place outside the Atlanta metro area, particularly in Augusta, Gainesville and Savannah."

Dhawan expects these metro areas to grow stronger than the overall state's growth rate in coming years.

Employment in transportation and warehousing, fueled by domestic demand, grew by a decent 6,100 jobs in 2017, but this was a moderation from 9,000 additions in 2016. Going forward, Dhawan expects job growth to be buoyed by online spending growth, which has been spurred by recent tax cuts, demand for air travel and growth at the port. The only constraining factor is the shortage of workers, such as truck drivers.

The corporate sector grew by only 11,600 new positions in 2017, a sharp moderation from 22,400 job gains in 2016. However, Dhawan expects to this trend to reverse in 2018, due in part to small business growth.

"We expect large corporations to experience some turbulence from tariff imposition threats and financial market volatility," Dhawan wrote. "At the same time, corporate and individual tax cuts will aid small businesses and lift overall growth of the corporate sector."

Dhawan also expects small business growth due to the tax cuts will contribute to growth in the retail trade sector, which lost 400 jobs in 2017.

In total, Georgia saw 72,100 new jobs added in 2017, and Dhawan anticipates a similar 69,800 jobs to be added in 2018.

Metro Atlanta is expected to experience the same impacts as the state overall.

"The metro area contains a bigger portion of the state's large corporations, so we could see stronger effects there," Dhawan wrote. "Yet, similar to the state, small business growth is expected to offset any negative effects."

Total housing permits in the metro region amounted to 32,205 in 2017. Going forward, it will be what Dhawan characterizes as "a victory" to maintain an annual pace of 33,000 permits.

"Multifamily permits remain near the 2017 level of 8,000 when activity in other counties will not be able to make up for Fulton's decline," Dhawan wrote. "Meanwhile, single-family permit growth will remain tempered due to rising financing costs and the lack of affordable lots in the core counties."

Highlights from the Economic Forecasting Center's Report for Georgia and Atlanta

- Georgia employment will add 69,800 jobs (14,900 premium jobs) in 2018, 60,200 jobs (13,300 premium) in 2019 and 55,300 (12,100 premium) in 2020.
- Nominal personal income will rise 4.2 percent in 2018, 5.2 percent in 2019 and 5.3 percent in 2020.
- Atlanta will add 48,900 jobs (10,700 premium jobs) in 2018, 44,200 jobs (9,700 premium) in 2019 and 40,200 jobs (9,000 premium) in 2020.
- Atlanta permitting activity in 2018 will increase 3.1 percent, increase 1.1 percent in 2019 and 1.0 percent in 2020.

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