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First Trust

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Monday Morning Outlook

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Don't Be An Economic Hypochondriac

Over the past year, as we have defended our forecast of a V-shaped recovery and the economy has clearly turned upward, two things have happened. First – slowly and quietly the consensus forecast for economic growth has been lifted – to roughly 3% real GDP growth from an anemic 2%. We expect this to continue as the consensus forecast continues to move toward our 4%+ forecast.

Second – the list of worries over the economy has grown. Remember credit card fears? Well, delinquency rates are declining now. What about Credit Default Swaps (CDS's)? Yeah, what about them? As you read this, AIG is writing the value of these contracts up. And who could forget Dubai? Oh, you already did?

Well, no matter how many of these economy killers disappear into the mist of history, there are more to take their place. A commercial real estate collapse, the "real" unemployment rate, housing foreclosures, ARM resets, deficits, government-created uncertainty, the lack of bank lending, universal healthcare, cap and trade, looming tax hikes, China, Greece, and don't forget the unwinding of economic intervention by the Fed and Treasury and the petering out of stimulus.

It's almost as if the better the economic data, the more things people worry about.

We don't want to say that all these worries are not important, or misplaced. There are problems and issues, but we do believe they are being overblown. For example, the national office vacancy rate is 17.5% – high – but still lower than it was in the 1990-91 recession, and lower than one would expect when the unemployment rate is 9.7%. And now with unemployment declining, vacancy rates should fall as well.

Many people fear a "real" unemployment rate of 16.5% (which includes the official unemployment rate plus marginally attached workers). But this rate is always above the official unemployment rate and moves along with it. In other words it offers no new information. Everyone knows unemployment is high, but recoveries always begin when unemployment is high.

Government deficits are high, and it is true that government activity is creating uncertainty, but this has stirred political push-back rarely seen in the US. It is very likely that the awakened and renewed political energy showing up these days will finally force Congress to address the issues of its long-term unfunded liabilities and its out-of-control spending. In other words, the worry and fear may finally produce action.

Finally, bank lending, or the lack of it, is bothering many. Conventional wisdom suggests that the economy cannot recover (at least strongly) without a pick-up in bank lending. However, this theory leaves us wanting. After declining in the past two years, total loans and leases held by commercial banks stood at $6.76 trillion at the end of 2009, which was above year-end 2007 levels or any time before that. In other words, bank lending is currently at levels above those that existed during what most people call a "bubble" in bank lending.

Much of this is about attitude. If you want to find things to worry about, you always can. It's like hypochondria. But, in the end, with monetary policy accommodative and the panic over, the economy is heading upward. And it's funny how so many problems seem to dissolve when growth gets underway.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
2-23 / 9:00 am	Consumer Confidence - Feb	55.0	**53.6**		55.9
2-24 / 9:00 am	New Home Sales - Jan	0.354 Mil	**0.352 Mil**		0.342 Mil
2-25/ 7:30 am	Durable Goods - Jan	+1.4%	**+3.6%**		+1.0%
7:30 am	Durable Goods (Ex-Trans) - Jan	+1.0%	**+0.7%**		+1.4%
7:30 am	Initial Claims - Feb 20	460K	**467K**		473K
2-26 / 7:30 am	Q4 GDP Preliminary	+5.7%	**+5.8%**		+5.7%
7:30 am	Q4 GDP Chain Price Index	+0.6%	**+0.6%**		+0.6%
9:00 am	Chicago PMI - Feb	59.0	**62.8**		61.5
8:45 am	U. Mich. Consumer Sentiment	74.0	**75.0**		73.7
9:00 am	Existing Home Sales - Jan	5.500 Mil	**5.410 Mil**		5.450 Mil