

Q2 Rebound is No Big Deal

President Trump announced higher tariffs were on the way almost as soon as he took office. As a result, businesses focused on buying foreign goods in advance, to front run those tariffs, putting some of their purchases from domestic producers on the backburner. The result was a massive surge in imports in Q1 that made trade the largest drag on real GDP growth for any quarter since at least the 1940s.

Now trade has gone in reverse, with purchases shifted back to US producers, which means trade will make a large contribution to real GDP in Q2 and real GDP will rebound sharply. How much it will rebound will be unclear until Tuesday morning, when we get a report on June trade and inventories, which could lead to substantial revisions in our forecast.

In the meantime, we are forecasting 3.0% annualized growth in Q2 versus a consensus expected 2.4%. But don't get too excited if we're right. Real GDP has averaged 2.0% per year the past twenty years, so one quarter with 3.0% growth after a quarter of -0.5% is not a sign of an economic boom.

Consumption: Auto sales declined at an 8.6% annual rate in Q2 while “real” (inflation-adjusted) retail sales excluding autos rose at a 1.0% rate and real service spending appears up at a 1.0% pace. This brings our estimate of real consumer spending on goods and services, combined, to a 0.5% rate, adding 0.3 points to the real GDP growth rate (0.5 times the consumption share of GDP, which is 68%, equals 0.3).

Business Investment: We estimate a 2.1% growth rate for business investment, with gains in equipment and intellectual property leading the way. A 2.1% growth rate would add 0.3

points to real GDP growth. (2.1 times the 14% business investment share of GDP equals 0.3).

Home Building: Residential construction declined at about a 5.0% rate in the second quarter, possibly reflecting a lack of workers to build homes while strict immigration enforcement makes more units available for rent. A 5.0% annualized decline would be a 0.2 point drag on real GDP growth. (-5.0 times the 4% residential construction share of GDP equals -0.2).

Government: DOGE and other Trump Administration efforts are cutting back on federal payrolls and transfers to NGOs, but only direct government purchases (not government salaries or transfer payments) count when calculating GDP. We estimate these purchases were up at a 1.2% rate in Q2, which would add 0.2 points to the GDP growth rate (1.2 times the 17% government purchase share of GDP equals 0.2).

Trade: The trade deficit plummeted in Q2 as businesses stopped front-running tariffs. This forecast may change a great amount when the “advance” report on trade arrives the morning of Tuesday July 29, but for now we're projecting net exports will increase the Q2 real GDP growth rate by 3.4 percentage points.

Inventories: After an import-related surge in Q1, inventories should grow much more slowly in Q2, generating what we are estimating as a 1.7 percentage point drag on real GDP growth.

Add it all up, and we get a 3.0% annual real GDP growth rate for the second quarter, a sharp rebound from the decline in Q1, but not a sign of an economic boom.

| Date/Time (CST) | U.S. Economic Data | Consensus | First Trust | Actual | Previous |
|-----------------|--------------------------------|-----------|-----------------|--------|----------|
| 7-30 / 7:30 am | Q2 GDP Advance Report | +2.4% | +3.0% | | -0.5% |
| 7:30 am | Q2 GDP Chain Price Index | +2.2% | +1.5% | | +3.8% |
| 7-31 / 7:30 am | Initial Claims – July 26 | 223K | 221K | | 217K |
| 7:30 am | Personal Income – Jun | +0.2% | +0.2% | | -0.4% |
| 7:30 am | Personal Spending – Jun | +0.4% | +0.4% | | -0.1% |
| 8:45 am | Chicago PMI – Jul | 42.0 | 40.7 | | 40.4 |
| 8-1 / 7:30 am | Non-Farm Payrolls – Jul | 109K | 221K | | 217K |
| 7:30 am | Private Payrolls – Jul | 100K | 132K | | 74K |
| 7:30 am | Manufacturing Payrolls – Jul | 0K | 122K | | -7K |
| 7:30 am | Unemployment Rate – Jul | 4.2% | 4.2% | | 4.1% |
| 7:30 am | Average Hourly Earnings – Jul | +0.3% | +0.3% | | +0.2% |
| 7:30 am | Average Weekly Hours – Jul | 34.3 | 34.2 | | 34.2 |
| 9:00 am | ISM Index – Jul | 49.5 | 49.3 | | 49.0 |
| 9:00 am | Construction Spending – Jun | 0.0% | +0.3% | | -0.3% |
| afternoon | Total Car/Truck Sales – Jul | 15.8 Mil | 16.3 Mil | | 15.3 Mil |
| afternoon | Domestic Car/Truck Sales – Jul | 12.3 Mil | 12.5 Mil | | 12.0 Mil |