

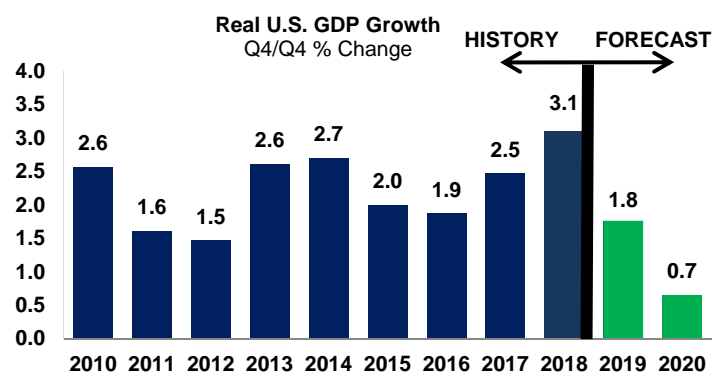
Date	Indicator	For	Estimate	Consensus*	Previous Period
4-Mar-2019	Construction Spending MoM	Dec	0.2%	0.3%	0.8%
5-Mar-2019	Markit US Services PMI	Feb F	56.1	56.2	56.2
5-Mar-2019	Markit US Composite PMI	Feb F	NA	NA	55.8
5-Mar-2019	ISM Non-Manufacturing Index	Feb	57.1	57.2	56.7
5-Mar-2019	New Home Sales	Dec	585k	579k	657k
6-Mar-2019	ADP Employment Change	Feb	190k	185k	213k
6-Mar-2019	Trade Balance	Dec	-\$56.8b	-\$51.2b	-\$49.3b
6-Mar-2019	U.S. Federal Reserve Releases Beige Book				
7-Mar-2019	Initial Jobless Claims	02-Mar	229k	NA	225k
7-Mar-2019	Nonfarm Productivity	4Q F	1.7%	1.5%	2.2%
7-Mar-2019	Unit Labor Costs	4Q F	1.9%	2.0%	0.9%
7-Mar-2019	Household Change in Net Worth	4Q	NA	NA	\$2070b
7-Mar-2019	Consumer Credit	Jan	\$16.000b	\$17.000b	\$16.554b
8-Mar-2019	Change in Nonfarm Payrolls	Feb	190k	185k	304k
8-Mar-2019	Change in Manufacturing Payrolls	Feb	9k	NA	13k
8-Mar-2019	Unemployment Rate	Feb	3.9%	3.8%	4.0%
8-Mar-2019	Average Hourly Earnings MoM	Feb	0.3%	0.3%	0.1%
8-Mar-2019	Average Weekly Hours All Employees	Feb	34.5	34.5	34.5

*Consensus from Bloomberg

The 2018 U.S. GDP Victory Rings Hollow

Fourth quarter GDP growth beat economists' expectations, coming in at 2.6% annualized, giving the Trump administration a reason to celebrate four quarters of 3.0% plus growth, a new expansion record. The Administration sold the 2018 Tax Cuts and Jobs Act by promising 3.0%-plus GDP growth over the coming decade, and at least over the first four quarters since passage, the economy managed to hit the mark. Don't expect a repeat performance. In retrospect, the 2018 U.S. GDP growth victory will likely ring hollow. Outside the Beltway, I don't see a lot of high fives and party hats being distributed. Perhaps the biggest tell is the fact the U.S. equity markets closed down on the day of the release.

A Hollow GDP Growth Victory

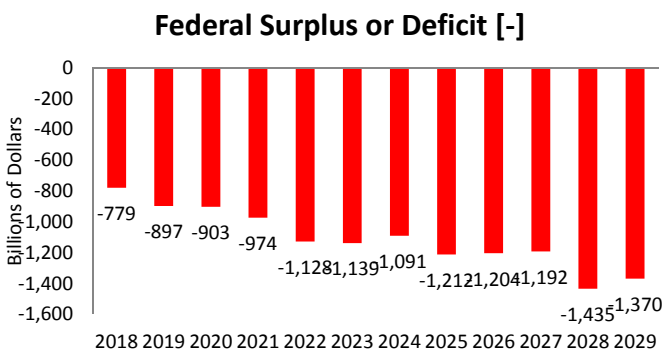


Source: Bureau of Economic Analysis; Bank of the West Economics

Moving beyond the self-congratulatory headlines, let's dig into what's going on beyond the topline growth numbers and review the behind the scene costs of this added growth over the past four quarters, and why the party can't last.

The GDP growth lift from the fourth quarter of 2017 is only 0.6 percentage points of GDP, or just over \$100 billion in added spending and production. Meanwhile, the cost to the U.S. Treasury has been substantial. The Congressional Budget Office (CBO) estimates the U.S. budget deficit increased by \$113 billion between FY 2017 (which ended in Oct. 2017) and FY 2018 (which ended in Oct. 2018). That's \$1.13 of added national debt for every dollar of added real GDP. The deficit is projected to rise another \$118 billion in FY 2019. I would conclude that the marginal cost of the tax cuts have been higher than the marginal benefit so far and the math is bound to get worse in the future.

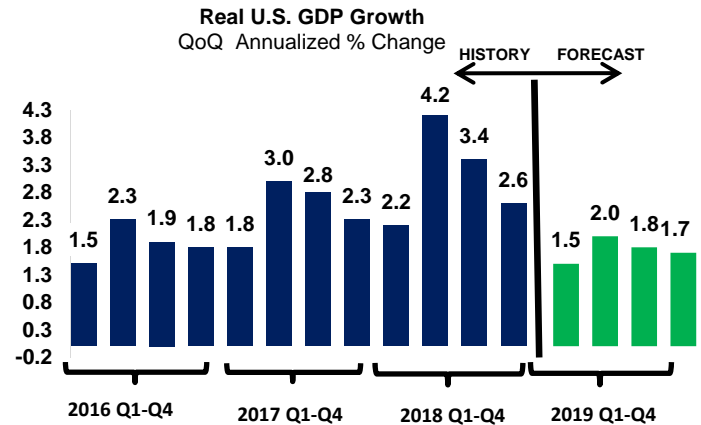
The Marginal Costs Outweigh the Marginal Benefits



Source: CBO

While year-on-year growth hit a new expansion high of 3.1% in the fourth quarter, sequential GDP growth peaked in the first quarter after passage of the Tax Cuts and Jobs Act at 4.2%. Since then, GDP growth has decelerated for two consecutive quarters to a much less heady 2.6% and our early estimate of Q1 2019 growth is only 1.5% annualized. If realized, the first quarter of 2019 could be the slowest quarterly growth performance for the U.S. economy since the first quarter of 2016.

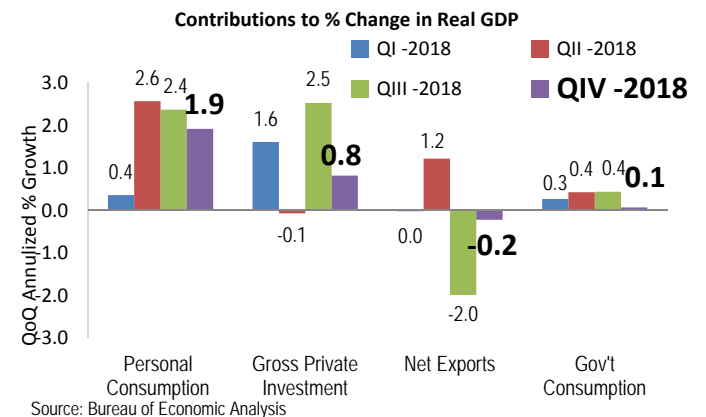
GDP Growth Actually Peaked More Than Six Months Ago



Source: Bureau of Economic Analysis; Bank of the West Economics

Looking at the components of GDP and their contribution to the change in GDP growth in each quarter of 2018 shows a much more mixed message.

A Mixed Performance under the Surface



Source: Bureau of Economic Analysis

Consumer spending was boosted early in 2018 only to fade in the second half of 2018. Gross private investment has been running hot and cold quarter-to-quarter and the increase in Q3 was due to an unwelcome build-up of business inventories that appears to have continued into the fourth quarter. This build-up in inventories will need to be worked off in future quarters, weighing further of 2019 GDP growth. Lastly, the damage of the trade war with China and others is clearly visible in the GDP trade accounts. While not enough to cause a recession on its own, the U.S. trade deficit continues to widen and has become a consistent drag on GDP growth. So forgive me for not joining in the celebration.

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Key Economic and Interest Rate Forecasts

Economic Data	History				Forecast								Yr/Yr % chg or Annual Avg.			
	2018.1	2018.2	2018.3	2018.4	2019.1	2019.2	2019.3	2019.4	2020.1	2020.2	2020.3	2020.4	2017	2018	2019	2020
Real GDP*	2.2	4.2	3.4	2.6	1.5	2.0	1.8	1.7	1.0	0.6	0.5	0.5	2.2	2.9	2.2	1.1
Personal Consumption Expenditures*	0.5	3.8	3.5	2.8	1.3	2.3	2.1	1.9	1.5	1.0	1.0	1.0	2.5	2.6	2.3	1.5
Non-residential Fixed Investment*	11.5	8.7	2.5	6.2	4.6	4.1	3.7	3.4	1.5	1.5	1.5	1.5	5.3	7.0	4.6	2.3
Private Housing Starts (000s units)	1,317	1,261	1,234	1,167	1,260	1,240	1,220	1,210	1,190	1,185	1,180	1,175	1,208	1,245	1,233	1,183
Vehicle Sales (mill. Units, annualized)	17.1	17.1	16.9	17.5	16.9	16.8	16.7	16.5	16.2	15.9	15.6	15.9	17.2	17.1	16.7	15.9
Industrial Production*	2.5	5.2	4.9	4.6	2.1	2.0	1.7	1.5	-0.5	-1.0	-1.0	-1.0	1.6	4.0	3.0	0.1
Nonfarm Payroll Employment (mil.)	148.0	148.7	149.4	150.1	150.7	151.2	151.7	152.1	152.4	152.0	151.6	151.4	146.6	149.1	151.4	151.9
Unemployment rate	4.1	3.9	3.8	3.8	3.9	3.7	3.6	3.7	3.9	4.2	4.5	4.8	4.4	3.9	3.7	4.4
Consumer Price Index* (percent)	3.2	2.1	2.0	1.5	1.1	2.1	2.1	2.1	1.8	1.8	1.7	1.6	2.1	2.4	1.7	1.9
"Core" CPI* (percent)	2.7	1.9	2.0	2.2	2.2	2.1	2.1	2.1	2.0	1.9	1.8	1.8	1.8	2.1	2.1	2.0
PPI (finished goods)* (percent)	3.6	2.9	2.2	-0.2	-0.1	2.1	1.8	1.8	1.3	1.4	1.4	1.4	3.2	3.0	1.1	1.6
Trade Weighted Dollar (Fed BOG, major)	86.2	88.2	90.2	91.4	91.3	90.6	89.6	88.5	88.3	88.0	87.5	87.0	91.1	89.0	90.0	87.7
Crude Oil Prices -WTI (\$ per barrel)	63	68	70	60	54	54	53	53	51	50	47	46	51	65	54	49

*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

Financial Data	History				Forecast								Annual Average			
	2018.1	2018.2	2018.3	2018.4	2019.1	2019.2	2019.3	2019.4	2020.1	2020.2	2020.3	2020.4	2017	2018	2019	2020
S & P 500	2,733	2,703	2,850	2,699									2,449	2,746		
Dow Jones Industrial Average	25,127	24,556	25,595	24,916									21,745	25,048		
Federal Funds Rate (effective)	1.45	1.74	1.92	2.22	2.38	2.38	2.38	2.46	2.54	2.29	2.04	1.79	1.00	1.83	2.40	2.17
Treasury-3 Month Bills (yield)	1.58	1.87	2.07	2.36	2.37	2.39	2.48	2.56	2.65	2.40	2.15	1.89	0.95	1.97	2.45	2.27
Treasury-2 Year Notes (yield)	2.16	2.48	2.67	2.80	2.51	2.50	2.60	2.65	2.75	2.60	2.35	2.15	1.40	2.53	2.57	2.46
Treasury-5 Year Notes (yield)	2.53	2.77	2.81	2.88	2.50	2.52	2.65	2.70	2.70	2.50	2.30	2.25	1.91	2.75	2.59	2.44
Treasury-10 Year Notes (yield)	2.76	2.92	2.92	3.04	2.68	2.70	2.80	2.88	2.95	2.77	2.57	2.50	2.33	2.91	2.77	2.70
Treasury-30 Year Notes (yield)	3.03	3.09	3.06	3.27	3.02	3.08	3.20	3.28	3.30	3.10	2.90	2.80	2.90	3.11	3.15	3.03
Prime Rate	4.53	4.80	5.01	5.28	5.50	5.50	5.50	5.58	5.66	5.38	5.13	4.87	4.10	4.90	5.52	5.26
Libor 3-Mo. U.S. Dollar	1.93	2.34	2.34	2.62	2.77	2.76	2.79	2.87	2.95	2.70	2.42	2.13	1.26	2.31	2.80	2.55
Mortgage-30 Year (yield)	4.28	4.54	4.57	4.78	4.43	4.45	4.60	4.75	4.85	4.70	4.50	4.40	3.99	4.54	4.56	4.61
BAA Corporate (yield)	4.47	4.78	4.81	5.14	5.10	5.30	5.50	5.80	6.10	6.20	6.20	6.10	4.44	4.80	5.43	6.15

Source: Bank of the West Economics, Bloomberg, Federal Reserve