

## US stagflation fears on the rise

A surprise GDP contraction at a time when inflation is running at 40-year highs will inevitably lead to more talk of stagflation, particularly with the Fed set to hike interest rates aggressively. However, major trade and inventory swings masked decent underlying domestic demand with 2Q activity set to be much better

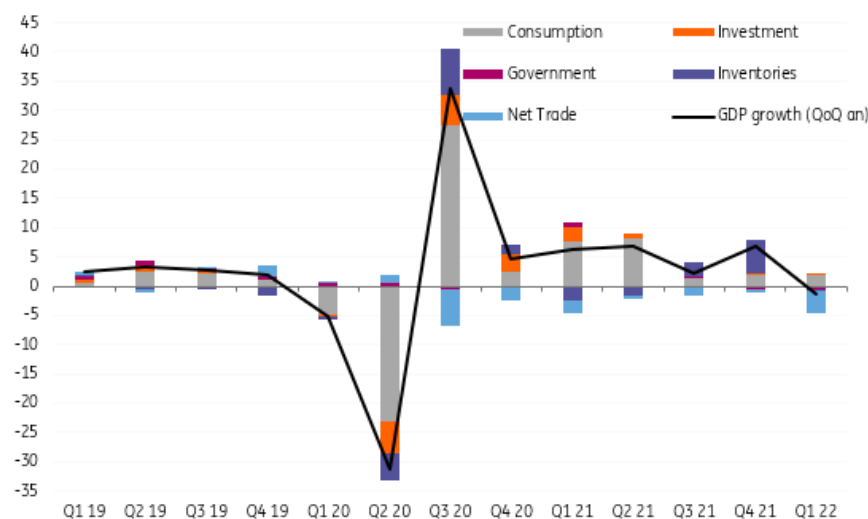


**-1.4%** Annualised growth in 1Q

### GDP falls, but details offer reasons for optimism

Well that will get all the stagflation worriers out in force! US GDP contracted 1.4% annualised in the first quarter versus expectations of a 1% increase. However, we wouldn't get too carried away since the details are not as bad as the headline figure suggests. Domestic demand actually held up pretty strongly, especially when we take into account the hit to economic momentum caused by the Omicron wave late last year. In fact consumer spending grew 2.7%, while non-residential investment expanded 9.2% and residential investment posted a 2.1% gain.

## Contributions to annualised GDP growth (%)



Source: Macrobond, ING

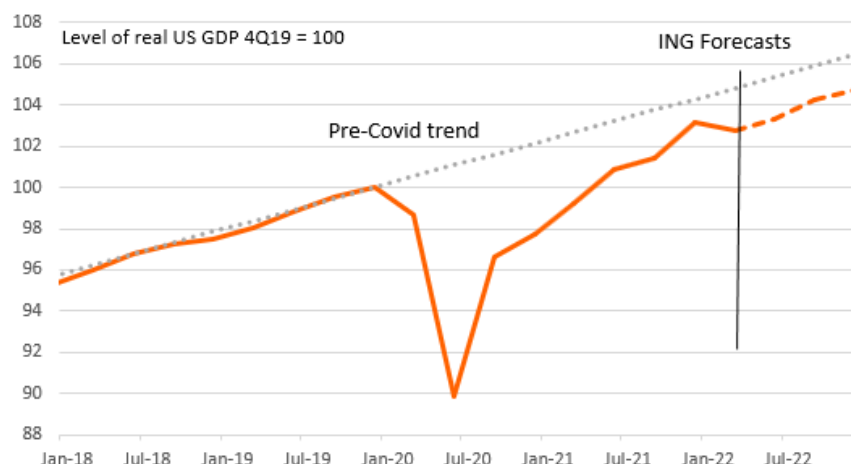
The negative GDP number is caused by a drop in exports (weak foreign demand due to Covid restrictions) and a surge in imports that meant net trade subtracted a full 3.2 percentage points from headline GDP growth. Inventories run downs amid ongoing supply chain disruptions subtracted a further 0.8% while government spending fell in consecutive quarters and subtracted 0.5pp.

## 2Q growth should rebound

Looking to 2Q, we are confident the growth number will be better despite fiscal and monetary policy becoming less supportive. While inflation is hurting spending power, nominal incomes are rising strongly and there are decent employment gains that in combination can keep spending firm. On top of that there is the legacy of higher savings accrued through the pandemic and large wealth gains caused by rising asset values that can additionally be used to keep consumer spending growing nicely.

Residential construction continues to perform well with rising housing starts and building permits, while robust durable goods orders point to a positive corporate investment backdrop. We are also expecting to see less of a drag from net trade, although it still will be a drag given strong domestic demand relative to elsewhere, while companies will continue to seek to rebuild inventory levels.

## GDP levels versus pre-Covid trend



Source: Macrobond, ING

## Fed still set to hike by 50bp in May

We are looking for 2Q annualized growth to come in at 2.0-2.5% and with inflation pressures remaining elevated and the labour market looking so tight, today's disappointing GDP outcome shouldn't alter the outlook for a 50bp Federal Reserve interest rate increase next week.

### Author

**James Knightley**

Chief International Economist

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.