US 1Q GDP growth concerns mount on weak spending and surging imports

The economy has started 2025 on a weak footing with the 'negatives' from President Trump's policy thrust taking an early toll via weaker consumer confidence and spending at the same time as importers look to front run the threat of tariffs

Government austerity, initiated by Elon Musk's Department of Government Efficiency, is prompting concerns in both the public and private sectors about job security and entitlements

Spending slides as consumers become more nervous

This morning's US data flow includes very soft US consumer spending numbers for January, falling 0.5% month-on-month in real terms, significantly below the -0.1% forecast. This is a really important story for 1Q GDP growth as even if we get a 0.4% MoM rebound in February and a 0.3% increase in March the US would record 1Q consumer spending growth of just 1.6% annualised – the weakest since 2Q 2023.

We already knew that retail sales fell. This was possibly cold weather-induced with some marginal impact from the LA fires, but there was an assumption that services spending would partially offset that. In the end it didn't and shows the US economy started 2025 on a weak footing. This suggests that the steep fall in consumer confidence since peaking in November when President Trump won the election, may be translating into cooler spending.

There was a sizeable increase in personal income of 0.9% MoM. Wages and salaries rose only 0.4% though with the strength coming from a 1.8% increase in government social benefits, 1.7% increase in dividends and a 39% increase in farm incomes. This led to a sizeable jump in the household savings ratio from 3.5% to 4.6%. Rounding out the numbers, the Federal Reserve's favoured measure of inflation was in line, rising 0.3% MoM/2.6% YoY - down from 2.9% YoY in December. To three decimal places, it was a 0.285% MoM increase, not brilliant, but much better than the 0.446% increase seen in core CPI.

Trump policy 'negatives' outweighing the 'positives'

At the start of the year there was optimism that President Trump's policy mix of light-touch regulation and lower taxes would turbo charge growth in an already solid looking economy. However, there has been little progress made on the 'positives' for growth – tax cuts and deregulation. Instead, the administration has been focusing on policies that yield 'negative' outcomes. Government austerity, as being initiated by DOGE, is prompting concerns in both the public and private sectors about job security and also entitlements while already financially-stressed lower- and middle-income households are not seeing any relief in the form of the lower prices they were promised. There is possibly also a growing awareness that tariffs will put up costs even more.

Another headwind for 1Q GDP growth has come from the advanced January goods trade report, which showed the merchandised trade gap widening to a record deficit of $153.3bn in January from $116.6bn in December. This is clear evidence that importers have tried to front run tariffs with imports surging 11.9% MoM. Industrial supply imports jumped from $67bn in December to $89.3bn in January with consumer goods imports jumping $6bn to $78.2bn. Interestingly automotive didn't move much. Exports rose 2% MoM, but this did follow a 3.8% drop in December.

The upshot of all this is that the market is seemingly starting to put more emphasis on the growth story over the inflation story, with Fed funds futures contracts now pricing in 61bp of Fed rate cuts for this year versus the 28bp priced just over two weeks ago. That looked too low to us and for now we are sticking with our two 25bp rate cut call for 2025 (September and December) with a third cut coming next March.

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