GDP: Speed vs. Accuracy

We get the first snapshot on Q3 economic output tomorrow. The consensus of economists projects 4.3% Q3 real GDP growth. The Atlanta Fed’s GDPNow forecast is even higher at 5.4%. Several observations are worth noting.

One, **real GDP is prone to substantial revision.** According to Bureau of Economic Analysis (BEA) calculations, one standard deviation on revisions is worth one full percentage point. That is large. But our calculations show that the revisions are almost twice that amount near economic inflection points. In fact, it is not unusual for the economy to have a growth fillip right before peaking. It has occurred ahead of four out of the last six recessions, with real GDP on average printing a solid, 3%-plus figure.

Two, **three-quarters of the expected Q3 splurge in output is coming from the consumer.** But given households’ high relative share of durable goods spending, and the fact that financing is harder to get and more expensive, a big slowdown should be in the offing. And many consumers once again have student loan payments to make. That is a big tax hike that could be worth upward of $160B per annum.

Three, **GDP is essentially a lagging indicator.** It tells us (imprecisely, given the revisions) where the economy was last quarter. But it does not tell us where the economy is going. For that, we need to look at leading indicators of the economy, such as the treasury yield curve. While bear steepening, the curve has been inverted since July 2022 and is thus sending an ominous economic signal.

Fourth, and maybe more importantly, **the income side of the economy has been telling us something entirely different than the product side of the economy** from which the GDP figures are derived. Presently, there is a near record large gap (known as the statistical discrepancy) between the income and product sides of the economy.

As we can see in the chart below, **real gross domestic income (GDI) has barely been grown over the past few quarters** while real GDP appears to be accelerating. Why focus on GDI? Because income is based on tax revenues, and businesses and households do not pay tax on phantom income. Arguably, this makes the GDI data more accurate than the GDP data. The reason investors focus more on the latter is partly because the product data are timelier.

![Real GDI and Real GDP chart](chart-image-url)
Disclaimers

This document is provided by SMBC Nikko Securities America, Inc. ("SMBC Nikko"), the US-registered broker-dealer affiliate of Sumitomo Mitsui Banking Corporation, for informational purposes only. This document was prepared by SMBC Nikko’s economist(s). The views statements, assumptions and forecasts expressed herein are those of the author(s) and do not reflect the judgment of any other person or of SMBC Nikko. It does not constitute an offer, or solicitation of the sale or purchase, of securities or other investments. The information contained herein is obtained or derived from sources believed to be reliable, but SMBC Nikko and the author(s) make no representations as to its accuracy or completeness. In some cases, such information may be incomplete or summarized. This document has been prepared based on assumptions and parameters determined by the economist(s) in good faith. The assumptions and parameters used are not the only ones that could have been selected, and therefore no guarantee is given as to the accuracy, completeness, or reasonableness of any such quotations, disclosures, or analyses. Past performance is not a reliable indicator of any future results.

This document has been prepared for and is directed at institutional investors and other market professionals, and is not intended for use by retail customers. It does not take into account any specific investment objective, financial situation, or particular need of any recipient. The information contained herein should, for whatever purpose, be used solely at the discretion and responsibility of the recipient. SMBC Nikko and its affiliates do not accept any liability or responsibility for any results in connection with the use of such information. Recipients are responsible for making final investment decisions and should do so at their own discretion after conducting a careful examination of all documentation delivered prior to execution, explanatory documents pertaining to listed securities, prospectuses, and other relevant documents, and their own independent analysis and assessment of the merits of any transaction. The financial instruments discussed may be speculative and may involve risks to principal and interest.

Conflicts of Interest Disclosures

The views statements, assumptions and forecasts expressed herein may differ from those expressed in globally branded research produced by SMBC Nikko or its affiliates. The trading desks of SMBC Nikko and its affiliates trade or may trade as principal in the financial instruments that are the subject of this material, and the author(s) of this document may have consulted with the trading desks while preparing this document. The proprietary interests of SMBC Nikko and its affiliates may conflict with those of the recipient. SMBC Nikko and its affiliates may seek to do business with the companies mentioned in this material and the trading desks may have accumulated, be in the process of accumulating, or accumulate long or short positions in the financial instruments mentioned and may have acquired them at prices no longer available. The trading desks may also have or take positions inconsistent with the views expressed in this document or may have already traded on those views.

This material is not a research report, and neither this material nor its author(s) is subject to SMBC Nikko policies and procedures that apply to the globally branded research reports and research analysts of SMBC Nikko and its affiliates or to legal requirements designed to promote the independence of investment research. It is not subject to any prohibition on dealing ahead of the dissemination of investment research. This means that on the date of this document, SMBC Nikko, its affiliates, and their respective directors, representatives, or employees, may have a long or short position in any of the instruments mentioned in this document and may make a market or trade in instruments economically related to the securities, derivatives or other underlying assets mentioned herein, in each case either as principal or as agent.

No part of the author(s) compensation was, is, or will be, directly or indirectly related to the specific recommendations or views expressed herein. The personal views of authors may differ from one another.

Distribution, possession or delivery of this document in, to or from certain jurisdictions may be restricted or prohibited by law. Recipients of this document are required to inform themselves of and comply with all such restrictions or prohibitions.

© 2023 SMBC Group. All rights reserved.