OUR BRILLIANT CATEGORIES

WOLF STREET REPORT

Imploded Stocks
Brick & Mortar
California Daydreamin'
Cars & Trucks
Commercial Property
Companies & Markets
Consumers
Credit Bubble
Energy
Europe's Dilemmas
Federal

That Q1 GDP Drop Was a Freak Event that'll Get Unwound in Q2

by Wolf Richter • May 15, 2022 • 161 Comments

In details and charts.

By Wolf Richter for WOLF STREET.

There has been a lot of confusion about that 1.4% quarter-over-quarter drop in "real" GDP. So let me just go through what didn't cause it, and then what caused it. What caused it was a freak event, and this freak event is likely to start unwinding in Q2. We're already seeing some evidence of it.

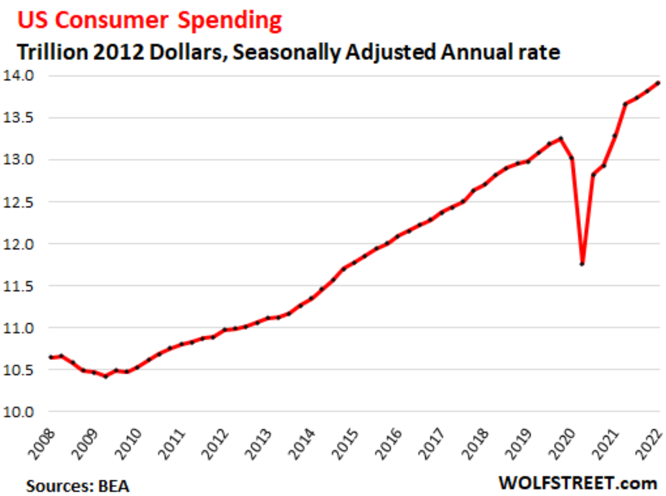
What didn't cause the drop in GDP:

Consumer spending rose by 2.7% in Q1, annual rate, adjusted for raging inflation. It accounted for 70.5% of GDP. This growth was in the middle of the range prevalent after the Great Recession until the pandemic (from 0.4% in Q2 2011 to 4.5% in Q4 2014).

However, there has been a pronounced shift from spending on goods to spending on services, especially discretionary services, where spending had collapsed during the pandemic. These

[Reserve](#)
[Housing Bubble 2](#)
[Inflation & Devaluation](#)
[Jobs](#)
[Trade](#)
[Transportation](#)

discretionary services include plane tickets, sports and entertainment venues, cruises, more or less discretionary healthcare services (such as dentists, elective surgeries, routine doctors' visits, etc.) I discussed this shift in consumer spending from goods to services in detail here. This shift in spending from goods to services will be important in a moment. The chart shows total consumer spending in the GDP data in inflation-adjusted dollars:



Gross private domestic investment rose by 2.3% annualized, following the spectacular spike in Q4. This measure includes investments in residential and nonresidential structures, equipment, intellectual property, etc., and it includes "change in private inventories" (more in a moment).

FRONT PAGE

Who Bought the Incredibly Spiking US Government Debt, Now $30.4 Trillion in Treasury Securities?
by Wolf Richter • May 19, 2022

A red-hot question in our iffy times.

As Supply Rises & Mortgage Rates Spike, US Home Sales Fall to Lowest since June 2020, Plunge in California's Coastal Metros
by Wolf Richter • May 19, 2022

Sales at the Top are strong. Bottom falls out in rest of market. "Rising interest rates and higher home prices depressed housing demand."

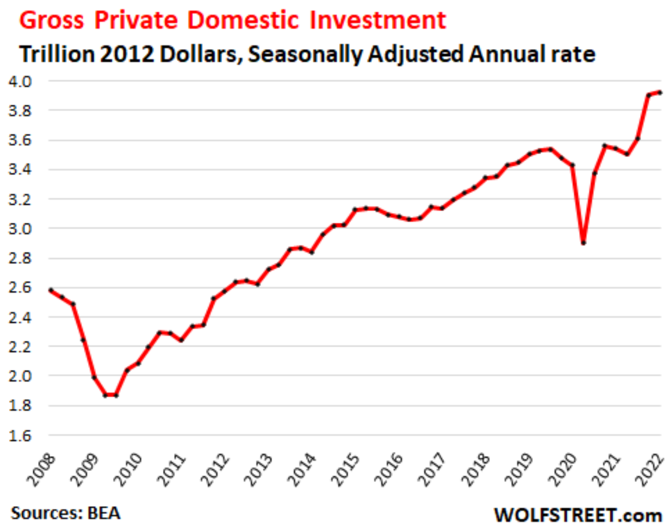
Bad Breath of Inflation Sinks Target, Walmart, Other Retailers on Surging Costs of Products, Labor, and Transportation
by Wolf Richter • May 18, 2022

Not a revenue-shocker (they were up even from stimulus-miracle a year ago), but a cost-shocker. Unable to pass on all the cost increases, their margins got squeezed.

Housing Bubble Getting Ready to Pop: Mortgage Applications Plunge amid Holy-Moly Mortgage Rates, Croaking Stocks, Ridiculous Home Prices
by Wolf Richter • May 18, 2022

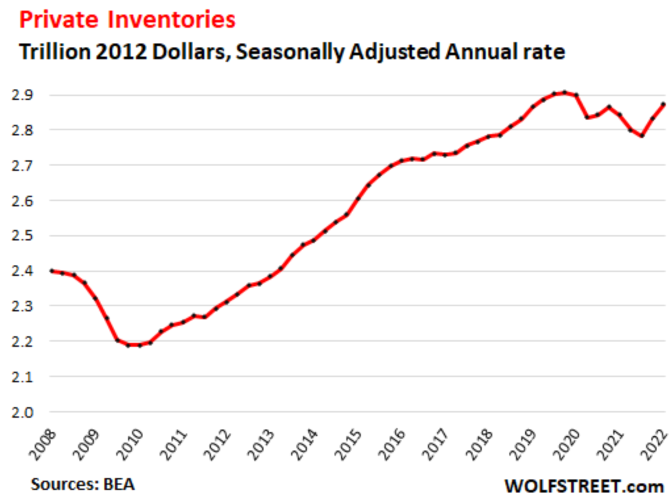
"Recent stock market volatility" catches some of the blame.

Americans Are in a Sour Mood, But it Didn't



Private inventories rose by 5.7% in Q1, after the 7.1% jump in Q4, annualized and adjusted for raging inflation. There has been a boom in sales of goods, particularly durable goods in 2020 and 2021 that triggered all kinds of supply chain issues, and shortages, and US companies depleted their inventories in many goods categories. They have been scrambling to catch up, and some of the supply chain issues improved later last year and earlier this year.

In addition, consumers switched spending from goods, where spending has been dropping, to services, where spending has been surging. Goods require inventories. And the reduced demand for goods took some pressure off inventories. But inventories remain far below the levels needed for a smoothly running economy:



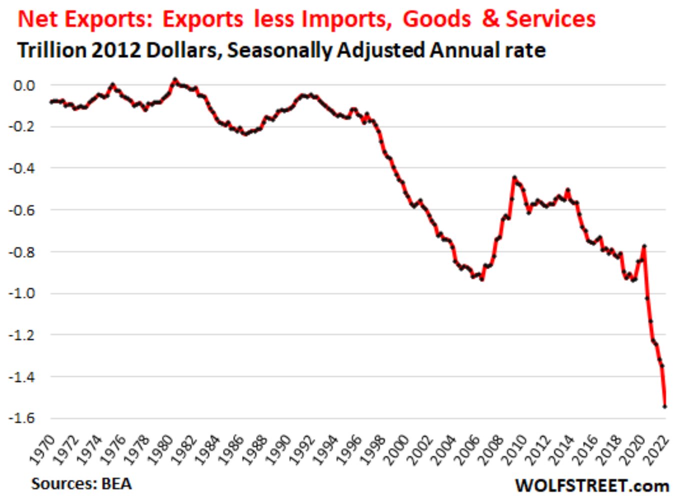
The Freak event that caused GDP to drop in Q1:

The Trade Deficit in goods & services exploded by $192 billion in Q1, annualized and adjusted for inflation, the second-worst ever drop in dollar terms, behind only Q3 2020.

Exports are added to GDP, imports are subtracted from GDP. With exports rising moderately but imports soaring, "Net Exports" (exports minus imports) have been a negative on GDP for decades. During the pandemic, stimulus-fuelled consumers spent huge record amounts on goods, many of them imported, and the trade deficit surged.

But what happened last quarter, the super-spike in the trade deficit, was extra-ordinary. As supply chains improved somewhat and as businesses were able to build inventories, imports of goods surged in a historic manner, causing the brutal worsening of the trade deficit in goods.

And this brutal worsening of the trade deficit reduced GDP by $192 billion annualized. But overall GDP fell by only $70 billion! A decline of half the size, which would have still been huge, would have produced a positive GDP reading:

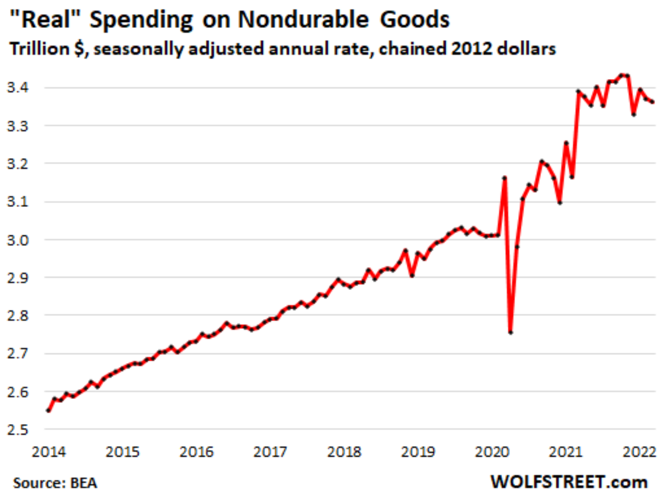


Why this freak trade deficit figure will start unwinding in Q2

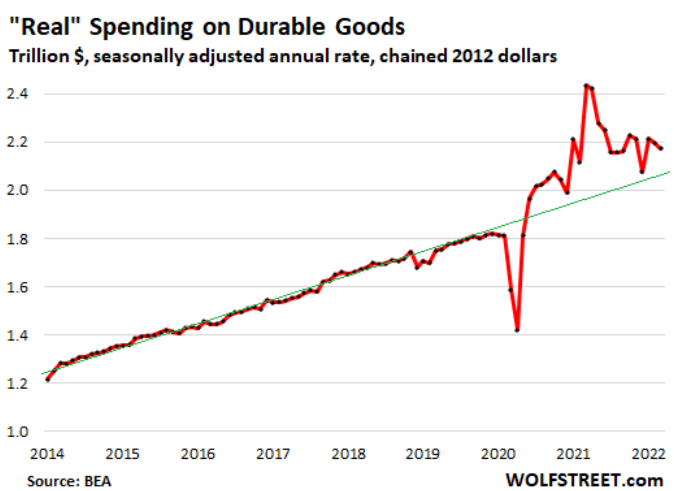
For the next quarter or two, the trade deficit will get smaller than the freak show in Q1, and it will be a smaller drag on GDP. Why? Because…

Consumer spending has been switching to services on a large scale, from goods (all adjusted for inflation).

Spending on nondurable goods fell again in March, seasonally and inflation adjusted. It has been falling since November last year, and was down 0.8% from a year ago. But it still remains very high, up by 13% from 2019, and will likely ease further in Q2. Nondurable goods are mostly food, fuel, and household supplies.



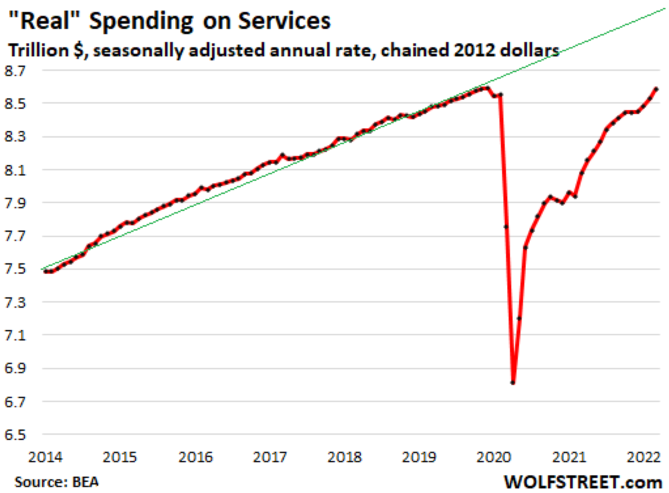
Spending on durable goods has fallen sharply since March 2021 (-10.7%, adjusted for inflation). But it remained very high, up 24% from March 2019, and will likely fall further, regressing toward the pre-pandemic mean, as consumers switch their spending back to services:



Many of these goods are imported, and a decrease in spending on goods will lower imports from the freak-show levels last year and in Q1 this year. This isn't to say that magically, the trade deficit will disappear, but it will shift from abysmally horrible to just horrible, and the trade deficit will get smaller and be much less of a drag on GDP.

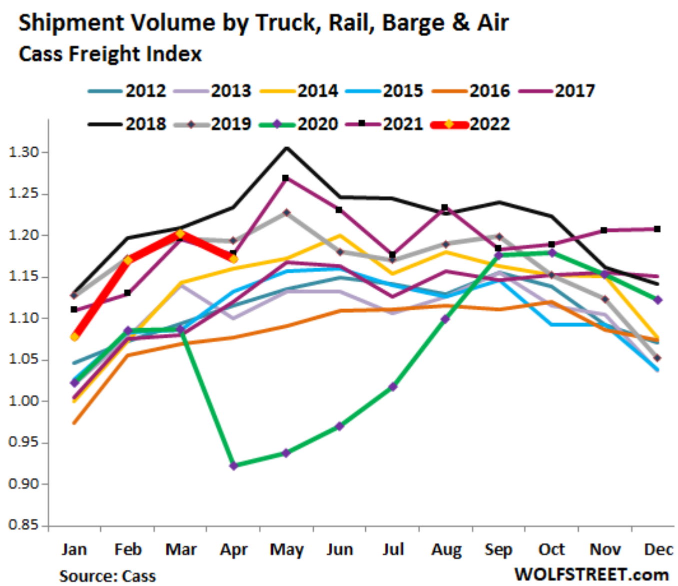
Meanwhile, spending on services is surging. Even when adjusted for inflation, it jumped by 0.6% in

March, and by 6.3% year-over-year. But it remains below pre-pandemic trend and has a long way to go with higher-than-normal growth to get back to normalish levels, and we'll see more of this normalization in Q2:



Sudden pullback in freight shows slower demand for goods in Q2.

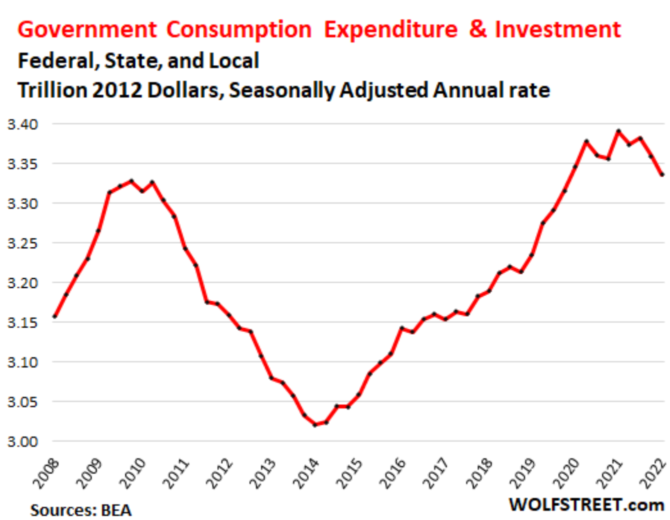
We're already seeing US transportation volume slowing down. And this is across the board. Shipment volume in the US by all modes of transportation, but excluding commodities, fell by 0.5% year-over-year in April and by 1.8% from April 2019, and by 5.0% from April 2018, according to the Cass Freight Index (my discussion: Signs of a Downshift in the Freight Cycle, Trucking, and Demand). See the bold red line:



Government consumption also fell in Q1.

Spending by federal, state, local government agencies on equipment, supplies, fuel, etc. (not salaries and social spending) fell in Q1, which also dragged down GDP.

I'm not going to make predictions about government consumption, but governments at all levels are floating in a sea of cash after the money-printing binge and the high tax revenues for 2021. And these governments are going to spend this money sooner or later, which will then boost GDP.



The GDP Decline in Q1 likely gets unwound in Q2.

Less-catastrophic imports, thereby a less-catastrophic trade deficit, will reduce the drag on GDP. Consumers are holding up for now. And there is still an unspeakably huge amount of money floating around out there among consumers, businesses, and governments at the state and local levels, after the $11 trillion in stimulus in two years – $4.7 trillion from the Fed's money-printer and about $6 trillion in government deficit spending. And some of this money will get spent over the next few quarters.

Yes, there will be a recession some day because sooner or later there always is, because recessions are part of the business cycle. But so far in the data, there is no recession being outlined. Consumer spending on durable goods has backed off from the crazy highs during the pandemic, as spending shifts to services, and overall spending growth is reverting from the spike during the pandemic to pre-pandemic normal. This normalization is happening, and that's a good thing.

However, in terms of asset prices, there's a rug-pull going on: The Fed has embarked on rate hikes and will soon embark on quantitative tightening, after interest-rate repression and QE have inflated nearly all asset prices to often ridiculous levels. So that's where the action will continue to be.

Would you like to be notified via email when WOLF STREET publishes a new article? Sign up here.

Email to a friend

161 comments for "That Q1 GDP Drop Was a Freak Event that'll Get Unwound in Q2"

.ike
May 15, 2022 at 9:58 pm

Wow I think this was a non pessimistic / non bearish article. 👍good news.

Housing Bubble Getting Ready to Pop: Mortgage Applications Plunge amid Holy-Moly Mortgage Rates, Croaking Stocks, Ridiculous Home Prices

by Wolf Richter • May 18, 2022 • 250 Comments

"Recent stock market volatility" catches some of the blame.

By Wolf Richter for WOLF STREET.

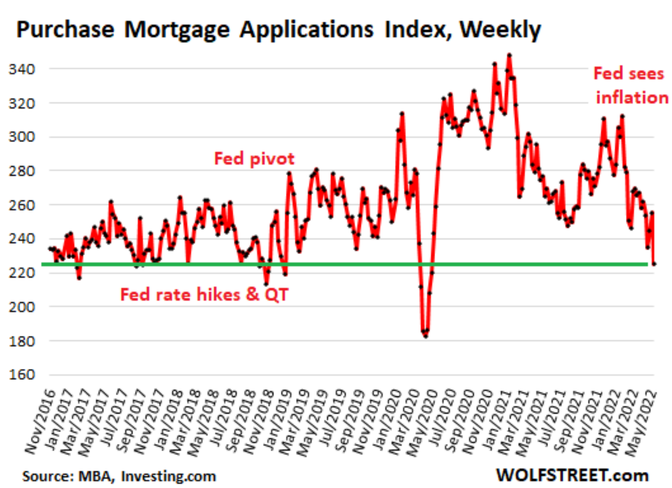
Pieces of evidence are lining up in increasing density. The number of potential future homebuyers that need a mortgage has been thinning out for months. Today, another milestone: Applications for mortgages to purchase a home dropped 12% from the prior week and were down 15% from a year ago.

In its report, the Mortgage Bankers Association today added that "prospective homebuyers have been put off by higher rates and worsening affordability conditions" – namely the ridiculous spike in home prices over the past 18 months, on top of the surge in prior years, combined with

[Reserve](#)
[Housing Bubble 2](#)
[Inflation & Devaluation](#)
[Jobs](#)
[Trade](#)
[Transportation](#)

mortgage rates returning to what would have been still very low rates a couple of decades ago.

The MBA's Purchase Mortgage Applications Index dropped to the lows of late 2018. Back then, the Fed had been hiking rates, and its QT had pushed mortgage rates to a hair over 5%, volume was drying up, and prices had started to wobble and were coming down in some markets. But inflation was below the Fed's target, and Trump had been keelhauling Powell on a daily basis. Powell caved, mortgage rates dropped again, and volume and prices took off again. Now raging inflation is the dominant economic concern, and the Fed is determined to get it under control (data via Investing.com):



Holy-Moly Mortgage Rates.

FRONT PAGE

Who Bought the Incredibly Spiking US Government Debt, Now $30.4 Trillion in Treasury Securities?

by Wolf Richter • May 19, 2022

A red-hot question in our iffy times.

As Supply Rises & Mortgage Rates Spike, US Home Sales Fall to Lowest since June 2020, Plunge in California's Coastal Metros

by Wolf Richter • May 19, 2022

Sales at the Top are strong. Bottom falls out in rest of market. "Rising interest rates and higher home prices depressed housing demand."

Bad Breath of Inflation Sinks Target, Walmart, Other Retailers on Surging Costs of Products, Labor, and Transportation

by Wolf Richter • May 18, 2022

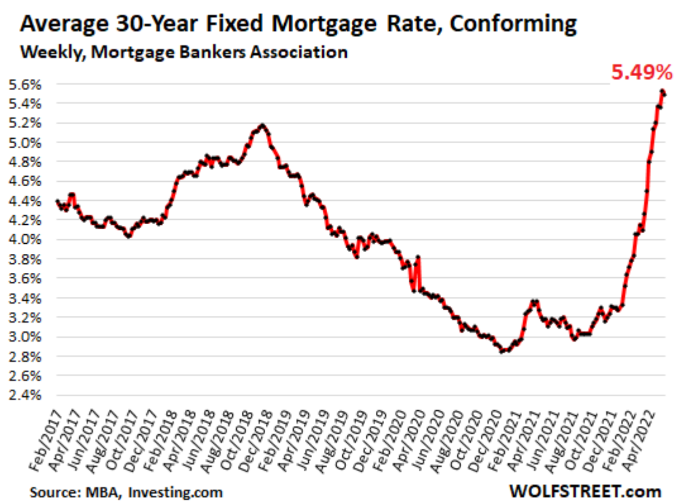
Not a revenue-shocker (they were up even from stimulus-miracle a year ago), but a cost-shocker. Unable to pass on all the cost increases, their margins got squeezed.

Americans Are in a Sour Mood, But it Didn't Dampen their Spending: Splurging at Retailers, Especially Some Retailers

by Wolf Richter • May 17, 2022

Retail Therapy at Bars & Restaurants, Cannabis Stores, and Ecommerce? Other retailers not so lucky.

The average 30-year fixed mortgage rate with conforming balances and 20% down this week eased a tiny bit to 5.49%, according to the MBA today, from the prior week's 5.53%, both the highest holy-moly mortgage rates since 2009 (data via Investing.com):



Croaking stocks get blamed.

And it's not just mortgage rates: The MBA added that "general uncertainty about the near-term economic outlook, as well as recent stock market volatility, may be causing some households to delay their home search."

In this context, "volatility" always means sagging stock prices, because no one complains about upward volatility, and stocks are croaking. I mean, not every day, because we've had some sharp bear-market rallies, but they don't last long, and then stocks skid to lower lows. It's unnerving for people who've come to expect eternal and easy riches from stocks, and had built their whole future on this theory.

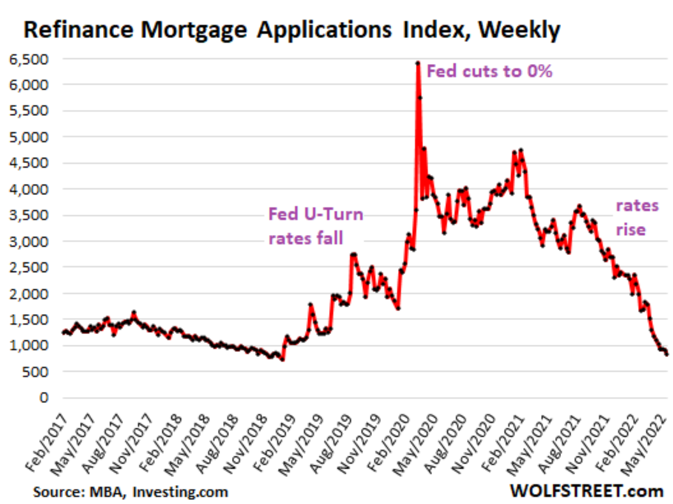
If you were going to borrow your down-payment by taking out a margin loan against your soaring stocks, you may now have second thoughts, that's for sure. I mean, look at the sh*tshow going today, with the Nasdaq down 4% at the moment, subject to change.

Cryptos were not mentioned by the MBA, and that's a good thing because they're just gambling tokens. But some bigger cryptos have already collapsed to essentially zero. Others are on the way. Bitcoin has plunged about 58% from November, and is down 25% from a year ago.

And that's not confidence-inspiring for people who'd expected to use their crypto gambling wins to buy a house with. Those that got out early, made it. And those that believe in HODL ("hold on for dear life"), well, they're going to have to keep believing.

Refi applications have collapsed for months.

Applications for mortgages to refinance an existing mortgage dropped further, having plunged all year amid these holy-moly mortgage rates, with the MBA's Refinance Mortgage Applications Index hitting the lowest point since the end of 2018.



Cash-Out Refi vs. No Cash-Out Refi.

But there is a split between cash-out refi, where needy homeowners are still feeding at the trough of the home-price spike, and no-cash-out refis, where homeowners are trying to lower their monthly payment by getting a new mortgage with a lower rate.

The AEI Housing Center tracks this split, using a different methodology than the MBA to account for mortgage applications.

Cash out refis are motivated by the need to take a big chunk of cash out of the home, and mortgage rates are a secondary issue. So cash out refis are continuing, but have dropped by 42% year-over-year, to the lows of early 2019, according to the AEI's Housing Center.

The share of cash-out refi mortgages insured by the FHA – includes subprime mortgages and low down-payment mortgages – rose to 27% of all cash-out refi mortgages, up from a share of 10% at the beginning of the year.

"This indicates that higher risk borrowers are experiencing more stress due to inflation – not a healthy trend," the AEI said. They're doing cash-out refis with holy-moly mortgage rates to pay for inflation? Oh boy… Thank god that only the taxpayer is on the hook here from get-go, and not the banks, which means that the Fed can let this one rip.

No cash-out refis are motivated by lower mortgage rates to reduce the mortgage payment and save money every month. And those lower mortgage rates are now history. In the current reporting week, no cash-out refis have collapsed by 93% year-over year.

This means the end of the monthly savings from lower mortgage payments, and the end of these savings getting spent on goods and services, and thereby another pillar of support under consumer spending has been kicked out from under it.

Enjoy reading WOLF STREET and want to support it? Using ad blockers – I totally get why – but want to support the site? You can donate. I appreciate it immensely. Click on the beer and iced-tea mug to find out how:

Would you like to be notified via email when WOLF STREET publishes a new article? [Sign up here](#).

[Email to a friend](#)

250 comments for "Housing Bubble Getting Ready to Pop: Mortgage Applications Plunge amid

The Most Splendid Housing Bubbles in America, April Update: Raging Mania on the Eve of the Spike in Mortgage Rates

by Wolf Richter • Apr 26, 2022 • 148 Comments

At the time rate locks were issued for those deals, mortgage rates were still around 3.2%.

By Wolf Richter for WOLF STREET.

Home prices spiked in crazy leaps – including by about 30% or more in Phoenix, Tampa, and Miami year-over-year – according to the S&P CoreLogic Case-Shiller Home Price Index today. But this raging mania took place with mortgage rates of late *last year*, given the long lag the Case-Shiller Index.

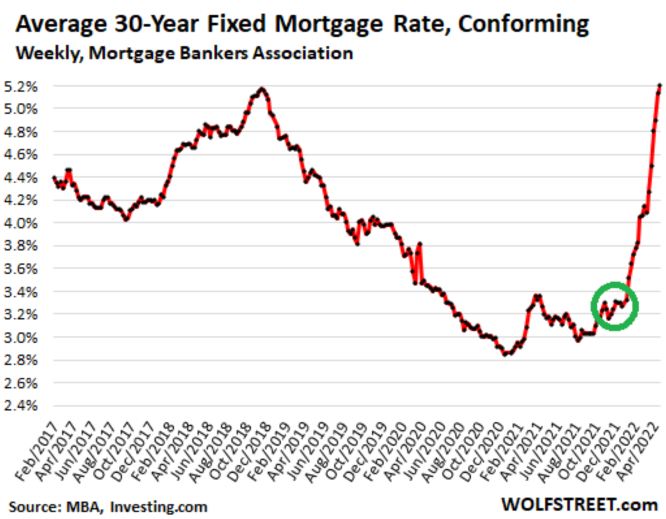
The long lag of the Case-Shiller Home Price Index.

The home price data released today was called "February" and represents the three-month average of closed sales that were *entered into public records* in December, January, February, reflecting deals that were agreed to a few weeks

[Reserve](#)
[Housing Bubble 2](#)
[Inflation & Devaluation](#)
[Jobs](#)
[Trade](#)
[Transportation](#)

earlier, roughly in November, December, and January.

But wait… Many of these homebuyers were pre-approved and had rate locks from prior weeks and months. In November and December last year, the average 30-year fixed rate hovered at around 3.2%, according to Mortgage Bankers Association data, which is when homebuyers got the rate locks for most of these deals in today's data (green circle in the chart):



The home price data in the charts below does not yet reflect any part of the spike in mortgage rates that commenced in January. But it reflects the crazed run-up beforehand when buyers were desperately trying to buy a home with their still low rate locks.

FRONT PAGE

Who Bought the Incredibly Spiking US Government Debt, Now $30.4 Trillion in Treasury Securities?

by Wolf Richter • May 19, 2022

A red-hot question in our iffy times.

As Supply Rises & Mortgage Rates Spike, US Home Sales Fall to Lowest since June 2020, Plunge in California's Coastal Metros

by Wolf Richter • May 19, 2022

Sales at the Top are strong. Bottom falls out in rest of market. "Rising interest rates and higher home prices depressed housing demand."

Bad Breath of Inflation Sinks Target, Walmart, Other Retailers on Surging Costs of Products, Labor, and Transportation

by Wolf Richter • May 18, 2022

Not a revenue-shocker (they were up even from stimulus-miracle a year ago), but a cost-shocker. Unable to pass on all the cost increases, their margins got squeezed.

Housing Bubble Getting Ready to Pop: Mortgage Applications Plunge amid Holy-Moly Mortgage Rates, Croaking Stocks, Ridiculous Home Prices

by Wolf Richter • May 18, 2022

"Recent stock market volatility" catches some of the blame.

Americans Are in a Sour Mood, But it Didn't

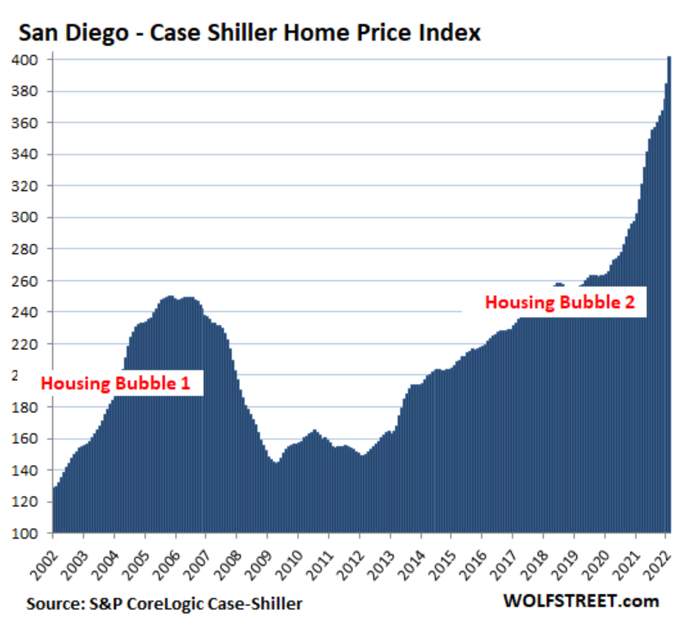
The mad scramble at the time.

During the time reflected in today's Case-Shiller home price data, there was a mad scramble to get the deals done before mortgage rates would rise, and this mad scramble is splendidly reflected here with some crazy spikes.

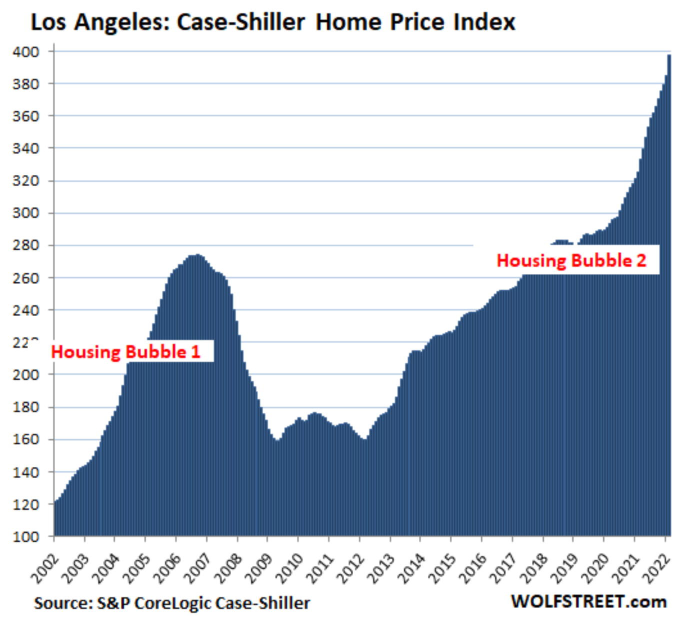
The overall National Case-Shiller Home Price Index for "February" (average of closed deals entered into public records in December, January, and February, and made in prior weeks and months) jumped 1.7% from the prior month and 19.8% year-over-year.

San Diego metro: Prices of single-family houses spiked by a holy-moly 4.5% in "February" from the prior month, and 29.1% year-over-year. The index value of 401 means that home prices exploded by 301% since January 2000, when the index was set at 100.

This price growth amounts to *4.3 times* the rate of CPI inflation (+70%) over the same period, crowning San Diego the Number 1 most splendid housing bubble on this list:



Los Angeles metro: The Case-Shiller index spiked by 3.2% in February from January and 22.1% year-over-year. With an index value of 397, house prices exploded by 297% since January 2000, crowning the Los Angeles metro as the Number 2 most splendid housing bubble on this list.



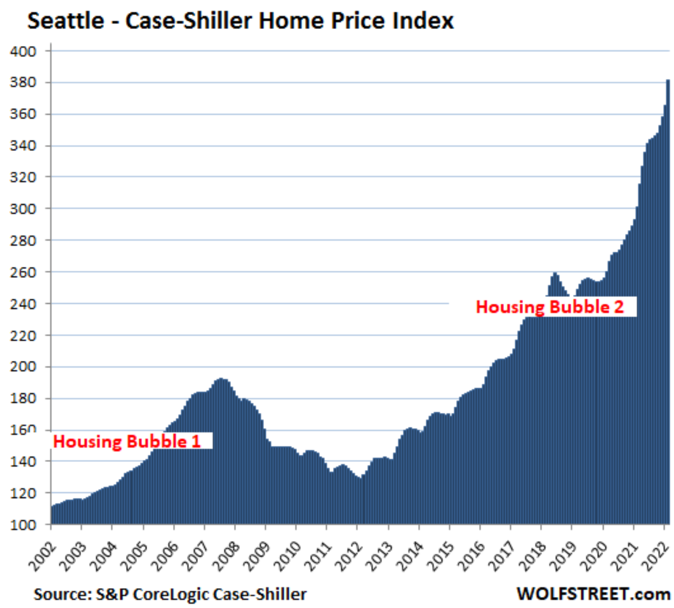
It's just house price inflation: dollar losing purchasing power.

The Case-Shiller Index's "sales pairs" method – comparing the price of a house when it sells in the current period to the price when it sold previously – tracks how many dollars it takes to buy the *same* house over time. The index includes adjustments for home improvements. By tracking the purchasing power of the dollar with regards to the same house, the index is a measure of house price inflation.

All charts here are on the same index scale, going just past 400.

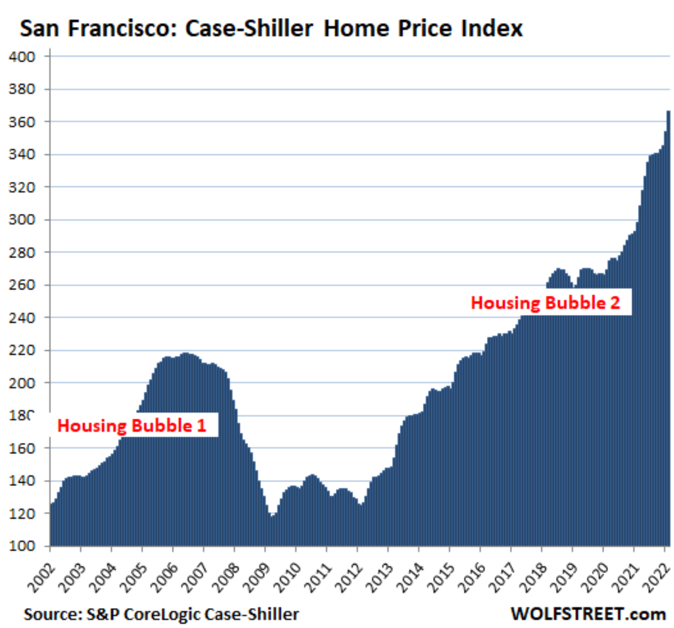
Seattle metro: House prices spiked a holy-moly 4.4% for the month, and 26.6% year-over-year. Since January 2000, house price inflation in the

Seattle metro amounts to 281%, *four times* the rate of CPI inflation:

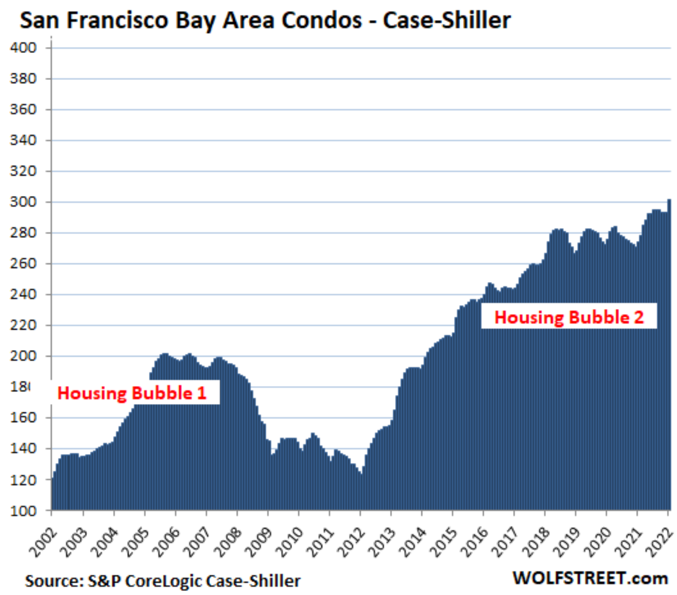


San Francisco Bay Area: Houses and condos have separated a few years ago, with condo prices lollygagging around, and house prices spiking. The Case-Shiller Index provides separate data for condos and houses for the five-county metro.

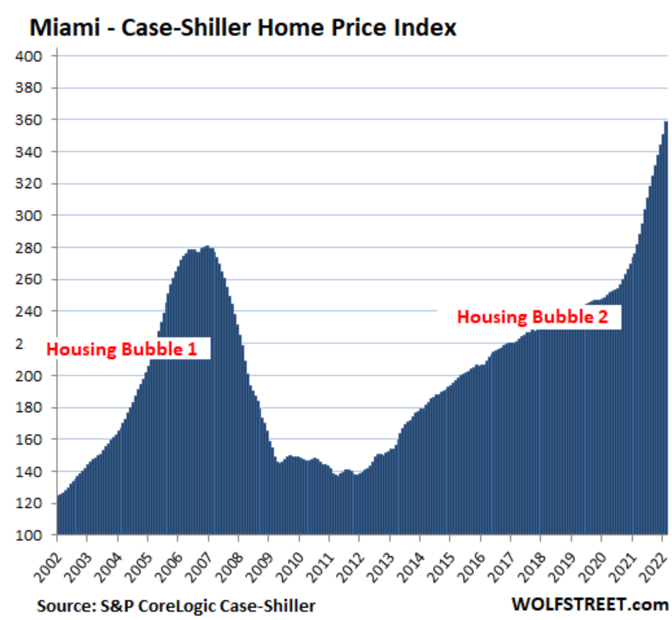
San Francisco Bay Area single-family house prices spiked 3.7% for the month, and by 22.9% year-over-year:



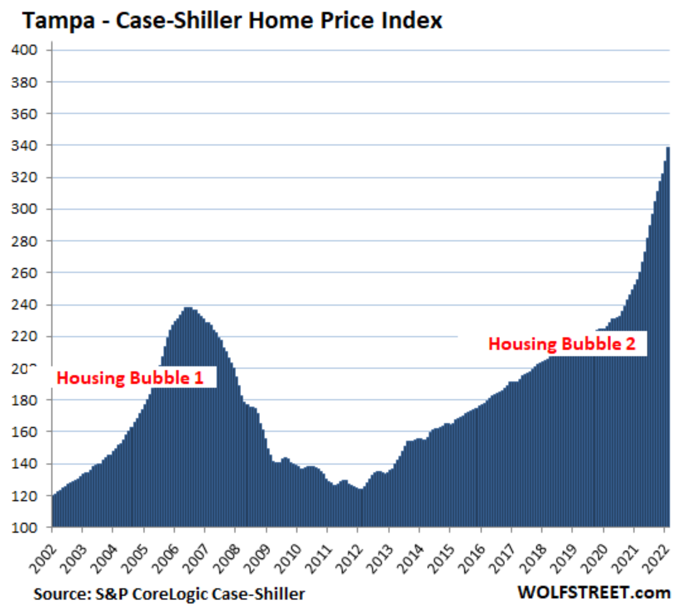
San Francisco Bay Area condo prices jumped by 2.6%, a big outlier, the little thingy sticking out on the right, after months of wobbling around and declining. The index is up 10% year-over-year. But since June 2018, condo prices have risen just 6.6%:



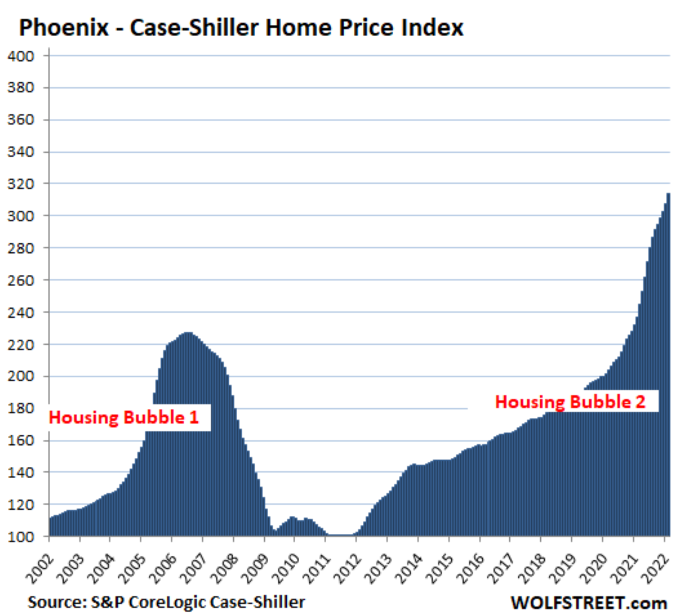
Miami metro: House prices spiked 2.3% for the month, and 29.7% year-over-year, the fastest since January 2006, on the eve of Miami's can-never-happen-here epic Housing Bust:



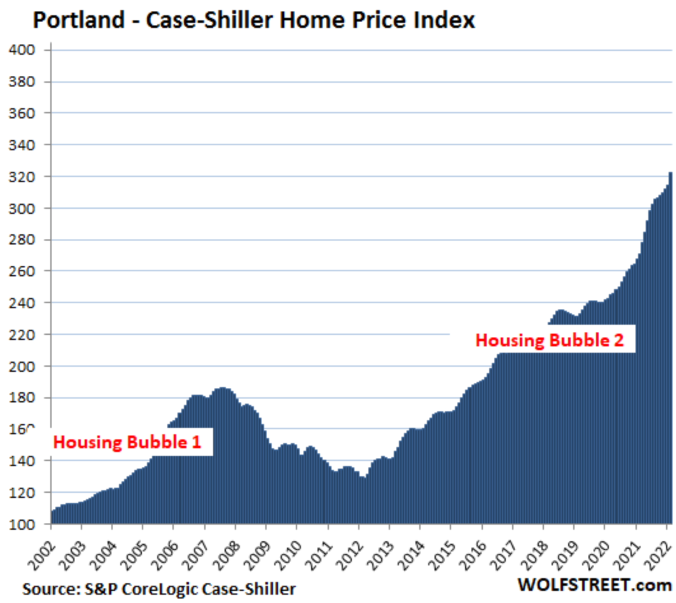
Tampa metro: House prices spiked by 2.7% for the month, and by 32.6% year-over-year, another record spike for the Tampa metro, wiping out the record spikes in the prior months, and out-spiking the crazy spikes on the eve of the housing bust:



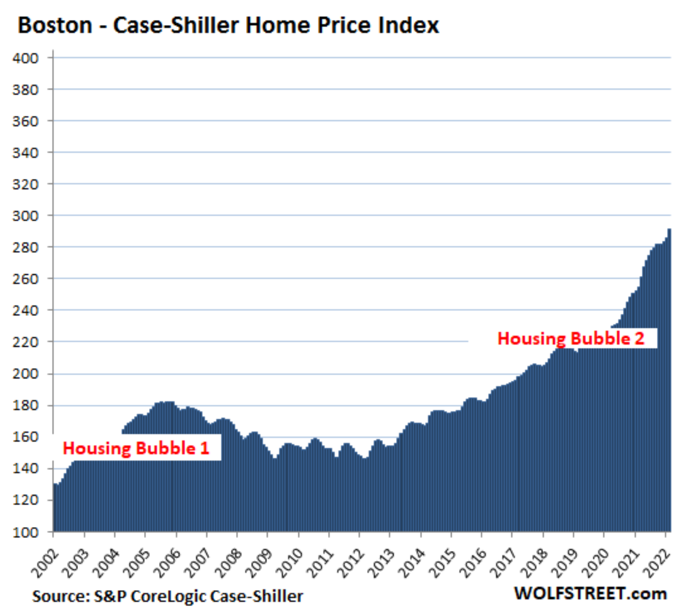
Phoenix metro: House prices spiked by 2.2% for the month, and by a record 32.9% year-over-year, the eighth month in a row of 30%+ year-over-year spikes:



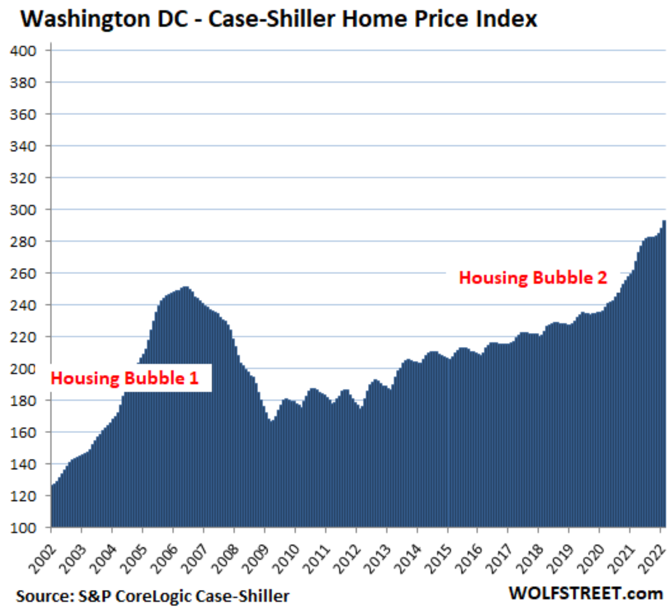
Portland metro: +2.5% for the month, and +19.0% year-over-year:



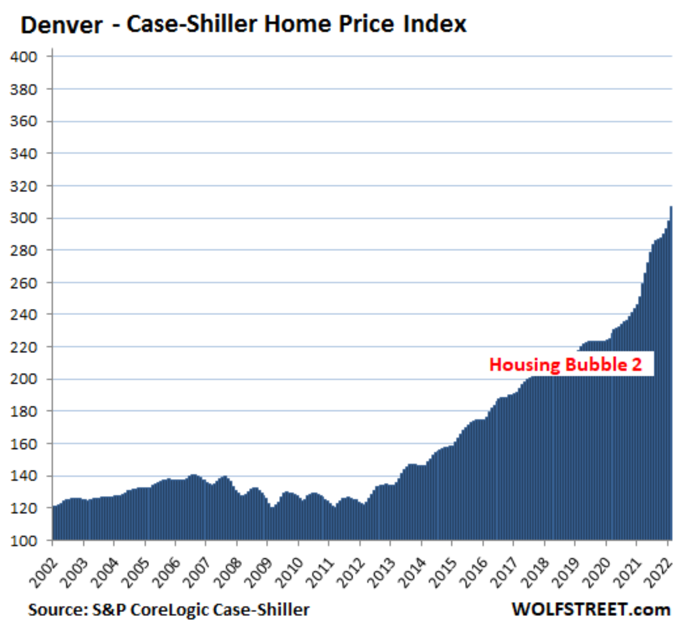
Boston metro: +2.1% for the month, and +14.6% year-over-year:



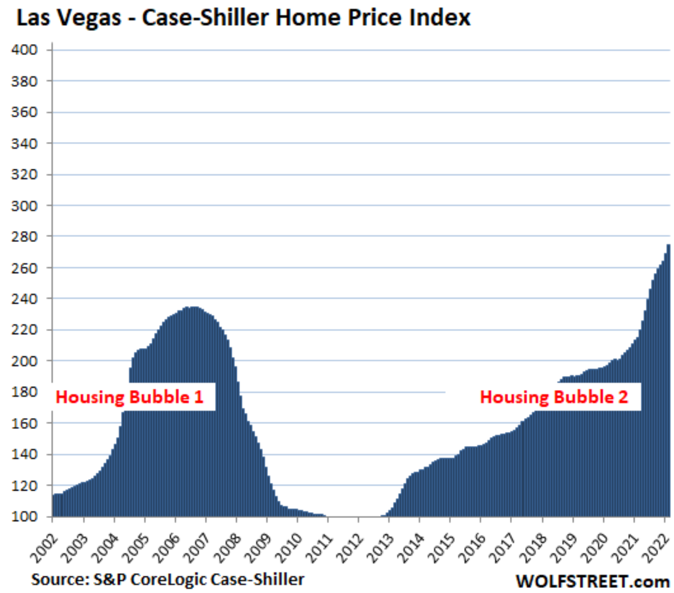
Washington D.C. metro: +1.7% for the month, and +11.9% year-over-year:



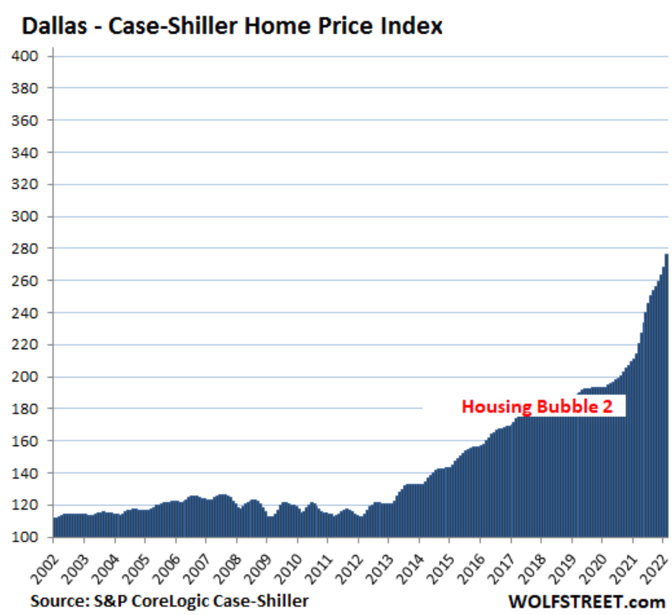
Denver metro: +3.1% for the month, and +22.3% year-over-year:



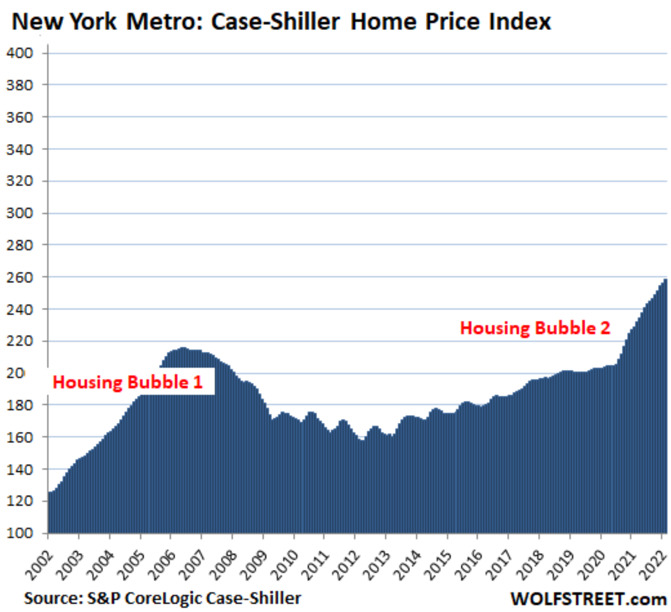
Las Vegas metro: +2.1% for the month, and +27.5% year-over-year:



Dallas metro: +2.9% for the month, and a record +28.8% year-over-year:



New York metro: +1.1% for the month, and +12.9% year-over-year. At an index value of 259, the metro has experienced 159% house price inflation since January 2000, compared to 70% CPI inflation.



The remaining metros in the 20-metro Case-Shiller Index – Atlanta, Charlotte, Chicago, Cleveland, Detroit, and Minneapolis – have experienced house price inflation since 2000 that doesn't measure up to these splendid housing bubbles here, and they therefore don't qualify yet to be included in this illustrious list.

Enjoy reading WOLF STREET and want to support it? Using ad blockers – I totally get why – but want to support the site? You can donate. I appreciate it immensely. Click on the beer and iced-tea mug to find out how:

Would you like to be notified via email when WOLF STREET publishes a new article? [Sign up here](#).