

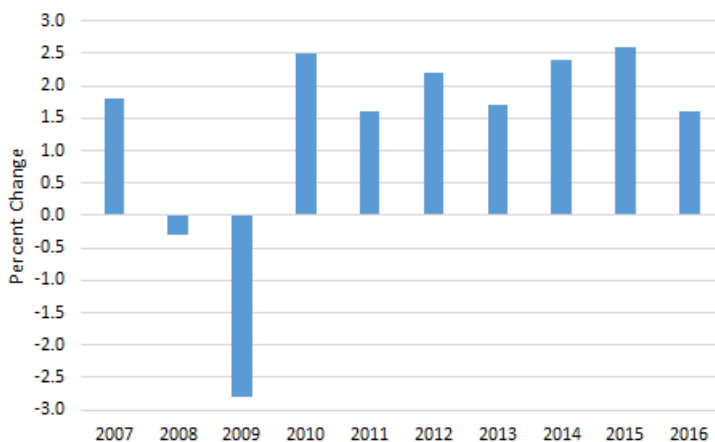
U.S. ECONOMY WATCH: GROWING PAINS

Kevin Flanagan — Head of Fixed Income Strategy
02/01/2017

We're only a little more than a week into the Trump administration, and investors are already beginning to see [volatility](#) in the money and bond markets. Indeed, the flurry of executive order signings and comments from the president last week elicited varying responses depending on their tenor or content. In our opinion, fixed income investors are just beginning to see what could potentially lie ahead in terms of [U.S. Treasury \(UST\)](#) volatility, as the market digests the various twists and turns the upcoming [fiscal policy](#) debate may take.

There's no doubt we are just in the early innings of this fiscal policy saga. As the headlines play out, it will be important to consider the fundamental backdrop of the U.S. economy leading into any potential forthcoming stimulus. In other words, what is the starting point for growth? The latest report from the Bureau of Economic Analysis (BEA) outlined the fact that the U.S. economy is still suffering from growing pains.

U.S. Real GDP



Source: Bureau of Economic Analysis, as of 1/27/2017. Past performance is not indicative of future results.

The above chart clearly illustrates the point that real GDP has experienced difficulties trying to break out from the great recession and has failed to grow beyond +2.6% in any calendar year since the economic downturn ended in 2009. In fact, overall growth has been only +2.1% over this 7½-year period. For the past calendar year, real GDP came in at +1.6%, the weakest annual showing in five years. In fact, the 2011 and 2016 performances were the lowest post-[recession](#) growth rates. As is often the case, the annual figure can mask what transpires on a quarterly basis. This was definitely the case in 2016, when growth got off to an anemic start of only +0.8% in Q1 and then topped out at +3.5% in Q3.

The BEA report also revealed that 2016 did not end on an overly robust note either, as real GDP came in at +1.9%, or 1.6 percentage points below the Q3 rate. Personal consumption continued to be a positive contributor during the period, while the next export component acted as a noticeable drag, reversing the pattern in trade seen for Q3. An interesting aspect to the GDP data came from the inventories grouping. This component added a full percentage point to growth in Q4, which prompts the question: Is this a sign of strength or potential weakness? Inventories can essentially increase for

two reasons: 1) businesses voluntarily increase their positions because they foresee an increase in demand that will need to be met (a positive); or 2) positions were involuntarily increased because demand declined (a negative). Typically, an increase in inventories of the magnitude that was witnessed in Q4 tends to get reversed to some degree during the subsequent quarter. If this pattern holds true for the first quarter of this year, real GDP will already have a headwind to overcome.

Conclusion

In two out of the last three years, Q1 growth numbers have tended to come in on the soft side. With the calendar now turning to February, investors will start to receive data for the month of January, and the UST market will begin formulating an opinion of where overall growth stood to begin the new year. This will be an important consideration in the context of potential fiscal stimulus later this year and what that could mean for [inflation](#) expectations, interest rates and Fed policy as a result: was the economy “hot” or “cold” on an underlying, pre-stimulus basis? Stay tuned...

Unless otherwise noted, source is the Bureau of Economic Analysis, as of 1/27/2017.

For more investing insights, check out our [Economic & Market Outlook](#)

View the online version of this article [here](#).

IMPORTANT INFORMATION

U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

There are risks involved with investing, including possible loss of principal. Foreign investing involves currency, political and economic risk. Funds focusing on a single country, sector and/or funds that emphasize investments in smaller companies may experience greater price volatility. Investments in emerging markets, currency, fixed income and alternative investments include additional risks. Please see prospectus for discussion of risks.

Past performance is not indicative of future results. This material contains the opinions of the author, which are subject to change, and should not to be considered or interpreted as a recommendation to participate in any particular trading strategy, or deemed to be an offer or sale of any investment product and it should not be relied on as such. There is no guarantee that any strategies discussed will work under all market conditions. This material represents an assessment of the market environment at a specific time and is not intended to be a forecast of future events or a guarantee of future results. This material should not be relied upon as research or investment advice regarding any security in particular. The user of this information assumes the entire risk of any use made of the information provided herein. Neither WisdomTree nor its affiliates, nor Foreside Fund Services, LLC, or its affiliates provide tax or legal advice. Investors seeking tax or legal advice should consult their tax or legal advisor. Unless expressly stated otherwise the opinions, interpretations or findings expressed herein do not necessarily represent the views of WisdomTree or any of its affiliates.

The MSCI information may only be used for your internal use, may not be reproduced or re-disseminated in any form and may not be used as a basis for or component of any financial instruments or products or indexes. None of the MSCI information is intended to constitute investment advice or a recommendation to make (or refrain from making) any kind of investment decision and may not be relied on as such. Historical data and analysis should not be taken as an indication or guarantee of any future performance analysis, forecast or prediction. The MSCI information is provided on an "as is" basis and the user of this information assumes the entire risk of any use made of this information. MSCI, each of its affiliates and each entity involved in compiling, computing or creating any MSCI information (collectively, the "MSCI Parties") expressly disclaims all warranties. With respect to this information, in no event shall any MSCI Party have any liability for any direct, indirect, special, incidental, punitive, consequential (including loss profits) or any other damages (www.msci.com)

Jonathan Steinberg, Jeremy Schwartz, Rick Harper, Christopher Gannatti, Bradley Krom, Tripp Zimmerman, Michael Barrer, Anita Rausch, Kevin Flanagan, Brendan Loftus, Joseph Tenaglia, Jeff Weniger, Matt Wagner, Alejandro Saltiel, Ryan Krystopowicz, Kara Marciscano, Jianing Wu and Brian Manby are registered representatives of Foreside Fund Services, LLC.

WisdomTree Funds are distributed by Foreside Fund Services, LLC, in the U.S. only.

You cannot invest directly in an index.

DEFINITIONS

Volatility : A measure of the dispersion of actual returns around a particular average level. nbsp;.

Treasury : Debt obligation issued by the U.S. government with payments of principal and interest backed by the full faith and credit of the U.S. government.

Fiscal Policy : Government spending policies that influence macroeconomic conditions. These policies affect tax rates, interest rates and government spending, in an effort to control the economy.

Real growth : Refers to the rate of economic growth with the inflation rate subtracted from it.

Recession : two consecutive quarters of negative GDP growth, characterized generally by a slowing economy and higher unemployment.

Inflation : Characterized by rising price levels.