
2019: THE ECONOMY IN THE YEAR AHEAD

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As the glow from the 2018 tax cuts fades in the U.S. in 2019, we expect the growth outlook to soften a bit from last year's pace.

Through Q3, real [GDP](#) was averaging +3.3%, and while forecasts for how economic activity finishes in 2018 vary, it seems likely that we will end the year around the +3.0% threshold. If this holds true when the data is released in the spring, it would mark our best annual performance since 2005.

For 2019, consensus forecasts revolve around +2.5%. While this pace of growth would represent some moderation from 2018, it would still be a modest improvement from the post-financial crisis/Great Recession level of +2.2%. In other words, a recession in 2019 does not seem likely.

Growth is also expected to slow on a global basis, but economic forecasts for this broader outlook also do not include any imminent downturns. For developed economies, consensus estimates look for GDP to drop 0.3 percentage points (pp) to +2.1% in 2019. Interestingly, the European Central Bank recently weighed in with its own projections. While its GDP estimate was revised downward by 0.1pp, the level of growth for 2019 is still pegged at +1.7%, essentially in line with the consensus.

Another key question to consider is this: Is [inflation](#) something to worry about? Through the first half of last year, inflation was essentially the "stealth" component. It was rising, but investors didn't appear to notice. Yes, inflation expectations rose appreciably from their mid-2017 lows to their recent peak in May. But from this high-water mark through October, break-even spreads were range bound. In other words, the bond market seemed to have discounted a rise in measures such as the [Consumer Price Index \(CPI\)](#) ahead of time, and then went to the sidelines. Since October, there has been a visible drop-off in expectations, with the lion's share of the widening in breakevens being reversed. This has coincided with CPI and core CPI (excluding food and energy) coming off their 2018 peaks. But current levels for both gauges still sit somewhat comfortably above the +2.0% threshold.

For 2019, investors should pay close attention to wages. For overall inflation, this had been the missing ingredient as far as the [Federal Reserve \(Fed\)](#) was concerned. But in three out of the last four months, the annualized increase for average hourly earnings has come in with a "3 handle"—the first such occurrence since 2009. If wages remain around the current +3.1% reading, we would not expect a meaningful increase in inflation expectations in 2019. But a move toward the +3.5% mark would probably create some heightened anxiety.

We'll be watching closely.

Read our full 2019 macro out look [here](#).

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DEFINITIONS

Gross domestic product (GDP) : The sum total of all goods and services produced across an economy.

Inflation : Characterized by rising price levels.

Consumer Price Index (CPI) : A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

Federal Reserve : The Federal Reserve System is the central banking system of the United States.