1Q21 Economic Summary

2021 is off to a promising start as a faster-than-expected vaccine rollout coupled with another round of fiscal stimulus kicked the US economic recovery into high gear. After some initial hiccups, the pace of US vaccinations accelerated during the first quarter. By the end of March, the US was administering 2.75 million vaccines per day and approximately 30% of Americans had received at least one dose. As COVID case numbers, hospitalizations and death rates declined, more states began to relax restrictions and reopen, resulting in a rebound in economic growth. Despite the advances made on the health front and the improvements in the economic outlook, the Biden administration continued to believe that more fiscal support was necessary to sustain the recovery and mitigate the losses caused by a year of economic restrictions. Thus, on March 11, President Biden signed the $1.9 trillion American Rescue Plan into law. The bill extends pandemic support for the unemployed, provides aid for state and local governments, and funds additional COVID-19 testing and vaccines. In addition, most Americans received up to $1,400 in direct payments under the plan. Given the massive fiscal injection, market expectations for stronger growth and higher inflation increased, pushing Treasury yields to post-pandemic highs. The surge in yields caused some volatility in stock prices, but markets remained resilient and equity indices were back near all-time highs by the end of the quarter.

With the economy starting to fire on all cylinders, US economic data surprised to the upside during the first quarter. Both manufacturing and services sectors surged as household and business demand accelerated. Increased vaccinations, fewer restrictions, and fiscal relief gave consumers the confidence to go out and spend. Retail sales soared in March, recording the second-largest monthly increase on record. Consumers spent their recently received stimulus checks on areas hit hardest by the pandemic, including bars, restaurants and apparel. As demand boomed, employers picked up the pace of hiring. The US added 1.6 million jobs during the quarter and the unemployment rate fell to 6.0% in March. Employment gains were widespread across industries, signaling that the economic recovery is broad-based and should continue to pick-up momentum as more restrictions are lifted. Improving labor market conditions continued to support strong housing demand; however, the pace of home sales declined during the quarter due to record-low inventory levels. The severe lack of supply drove up home prices, which coupled with higher mortgage rates, started to crimp affordability. While homebuilders did their part to increase supply, their progress was impeded by rising material prices, supply chain backlogs, and persistent labor shortages. All of which contributed to the increase in home prices. Overall, US first quarter growth was quite strong, with some economists estimating that US GDP had fully recovered its pandemic-related losses by quarter-end.

Not all countries started the year as strongly as the US. China's economic recovery continued during the first quarter thanks to increased exports and growing consumer demand. However, the pace of GDP growth slowed relative to the fourth quarter as China's post-COVID rebound continued to level off. In Europe, economic growth is expected to have contracted during the first quarter as a resurgence in the coronavirus pandemic triggered renewed restrictions. Japan also experienced another COVID wave, which caused the country to declare a state of emergency. The tighter restrictions on daily life led to a pull back in business and consumer spending, likely resulting in a slight contraction in first quarter GDP. Despite these setbacks, the IMF recently revised up its 2021 global growth forecast to reflect expectations of stronger growth in the second half of the year as lockdown restrictions are eased. The organization credited the latest round of fiscal stimulus in the US along with worldwide progress on vaccine rollouts as reasons for the improved outlook. The IMF warned that there remains a high degree of uncertainty surroundings its projections, with much still dependent on the race between the virus and vaccines. As such, the IMF expects central banks to keep monetary policy accommodative and tighten only gradually when it is evident that the recovery has taken hold and economic slack has decreased.

The Federal Reserve acknowledged the improved US growth outlook at the March FOMC meeting but agreed with the IMF that much more progress is needed before ending easy monetary policy. Despite accelerating economic activity and the aggressive vaccine effort, "participants agreed that the economy remained far from the Committee's longer-run goals and that the path ahead remained highly uncertain." As such, the FOMC voted to keep the target range of the fed funds rate unchanged at 0.00-0.25% and to continue buying at least $120 billion in bonds each month. Given the run-up in yields during the quarter, some market participants expected the Fed might alter the duration of its bond purchases to tamp down long-term rates; however, the Fed announced no changes to the tenure of its asset purchases. Chair Powell said he was not concerned with the recent rise in rates, viewing it as a statement of confidence in the economy, not an indication of mounting inflation pressure. The Fed anticipates that inflation measures will run above its 2% target in the coming months due to production bottlenecks and supply constraints, but it views these factors as transitory and expects inflation will stabilize once supply disruptions dissipate.

A year into the global coronavirus pandemic, the US appears poised to turn its economic recovery into economic expansion thanks to consumer resilience and unprecedented monetary and fiscal stimulus. While there is light at the end of the COVID tunnel, continued progress on overcoming the virus remains key to making the rosy outlook a reality.