Signs of Faster Growth in 2017

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By the third quarter, we usually know enough about the current year to begin forecasting the next one. Not this time. With all the uncertainty around the presidential election and what it could mean for economic policy, the glass was too dark to see clearly. Now that the election results are in, we can finally start to look ahead into 2017.

No guarantees, but faster growth seems reasonable

Though solid, economic growth has been lagging, and many feared it would slow further after the election. Since then, however, data has shown that consumer confidence and spending continue to improve—a significant plus. One of the weak sectors, business, may also be poised for a turnaround, with the stock market's post-election bump clearly signaling that investors are feeling positive about the new administration.

There are real reasons for that:

- Infrastructure investment, one of Donald Trump's core policies, could help spur faster government spending growth.
- Tax cuts stand to further boost both consumer and business spending.
- The deregulatory trend expected from the Republican Congress—plus improving fundamentals, with company revenues and earnings increasing for the first time in several quarters—makes faster economic growth and a stronger stock market look quite possible.

In such an environment, we could see real growth of around 1.5 percent in 2016, which could increase to 2 percent or more in 2017. Similarly, we may well see faster revenue and earnings growth in the stock market, which could push returns above the mid-single digits that had been expected.

None of this is certain, of course. Potential roadblocks include the federal deficit, which would rise with lower taxes and higher spending. Will congressional Republicans sign off on this? Another headwind could be higher interest rates. With signs of growing inflation, the Fed may feel compelled to act faster than it is now signaling, and the bond vigilantes may decide to ride again.

Trade is also a factor. Depending on Trump's policies, exporters such as China, Japan, and Germany may run into significant economic challenges, which could create political risks around the world. Closer to home, Mexico may also be affected. International markets will likely face even greater hurdles this year than they did last year.

In short, things are looking up

Despite these very real constraints, further economic improvement is likely in the year to come. Much of this outlook is based on expectations, which are hard to quantify. Still, both the stock and bond markets are signaling that better times are ahead, and the outlook for 2017 is brighter than we thought only a couple of weeks ago. ■

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