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Economy was hit harder by severe winter than initially feared

BY JIM PUZZANGHERA - May 30, 2014

The economy stumbled badly during the severe winter, much more than first estimated, according to a government report, and stalled a recovery that appeared poised to take off this year.

Economists, however, see the quarterly drop more as a delay in the nation's long revival from the Great Recession. Other recent data indicate economic growth has picked up significantly this spring, putting the recovery back on a slowly improving track.

Total economic output shrank at an annual rate of 1% from January through March, the first quarterly contraction in three years and just the second since the recession ended nearly five years ago, the Commerce Department said Thursday.

The department's revised figure for what is known as gross domestic product was far worse than the 0.1% growth initially reported last month. And the revision was steeper than the 0.5% contraction economists had anticipated.

The new reading also makes it unlikely that the economy will expand this year at the 3% rate economists previously projected.

"We've got to climb out of that hole" in the first quarter, said Brian Bethune, chief economist at consulting firm Alpha Economic Foresights. "You can think of it as a temporary setback, but it is going to pull down growth projections for this year."

Investors shrugged off the report. The Dow Jones industrial average rose 65.56 points, or 0.4%, to 16,698.74.

It typically takes two straight quarters of contraction to signal a recession, and projections are for growth to return in the second quarter. The economy expanded at a 2.6% annual rate in the fourth quarter last year. And heading into this year, the recovery appeared ready to reach what economists call takeoff velocity, which has been an elusive pace in the recovery.

"If the economy can demonstrate it can grow better than 3% on a sustained basis, it will motivate many more companies to accelerate business capital spending and also increase the pace of hiring," said **Bernard Baumohl, chief global economist at the Economic Outlook Group.**

This winter, bitter cold and heavier-than-normal snowfall swept across much of the nation, chilling economic activity.

The big factor in the contraction was a larger decline than originally estimated in how much businesses spent to restock their shelves.

Companies increased their stockpiles of goods by just $49 billion in the first quarter, down sharply from $111.7 billion in the fourth quarter. The falloff shaved first-quarter economic growth by 1.62 percentage points.

The weather didn't slow down consumers much. Their spending was revised up slightly to 3.1% Thursday, though still down from 3.3% in the fourth quarter. Even so, spending was strong, which bodes well for the rest of the year.

But it wasn't enough to boost first-quarter growth.

"Companies were not able to generate more inventory to offset that consumption because trucks were stuck on the road and employees couldn't get back to the factories," **Baumohl** said.

Still, what he called the "historically harsh winter" didn't alter the improving fundamentals of the recovery.

Baumohl forecast growth of 3.5% to 4% in the second quarter as businesses rebuild inventories. And he projects 3% growth in the second half of the year.

Alan MacEachin, corporate economist at Navy Federal Credit Union, also is expecting a "decent snapback" in growth this quarter. He's forecasting 3.7% annualized growth, with the economy then "back on track for 3% going forward."

Economists point to improving economic data in recent weeks to bolster their view that the first quarter was a weather-related anomaly.

Orders for airplanes, motor vehicles, computers and other durable goods, a key indicator of future factory output, rose in April for the third straight month, the Commerce Department said this week.

And on Thursday, the Labor Department reported that initial jobless claims dropped last week by 27,000 to 300,000. The figure was near the lowest level in seven years.

In addition, the number of people receiving unemployment benefits for the week that ended May 17, the most recent data available, fell to 2.6 million, the lowest level since November 2007.

And the robust gain of 288,000 net new jobs in April indicated that the labor market was rebounding after a winter slowdown.

But caution flags are still out on the recovery.

As bad as the winter was, it wasn't the only cause for the first-quarter contraction. Higher mortgage rates, for instance, contributed to the slowdown in the housing market. And a weaker global economy resulted in fewer exports.

Lindsey Piegza, chief economist at brokerage Sterne Agee, anticipates only 1.5% growth in the second quarter and about 2% for the latter half of the year. She cited the housing slowdown and weak wage growth for workers.

"It's more of the same," Piegza said of the economy, which has struggled to grow at much more than a 2% annual rate since the recession ended.

On Thursday, the Commerce Department also reported a big drop in corporate profits in the first quarter. Earnings fell by $213.4 billion to $1.96 trillion. In the fourth quarter, profits had increased $47.1 billion.

"When corporate profits drop by that order of magnitude, businesses are going to restrain their investment and hiring," Bethune said.

Although many fundamental aspects of the recovery remain strong, a slow global economy and an iffy housing market mean the economy still has a ways to go to get back to normal, he said.

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