August 1, 2016, GDP Review: Context for Last Friday's GDP Report

First Estimate of Second Quarter Data

Last Friday, the Bureau of Economic Analysis (BEA) reported real gross domestic product (GDP) growth of 1.2% in the second quarter of 2016, for a 1.0% average real GDP growth rate for 2016 thus far. First quarter real GDP growth was 0.8% after the annual revision. The 1.2% was far below expectations: Atlanta Fed's GDPNow forecast was 1.8%, the *Wall Street Journal* survey of economists expected 2.5%, and Wells Fargo expected 2.6%.

Second Quarter Data	
Real GDP (billions)	$16,575.1
Quarterly % Change Annualized	1.2%
Current Recovery Average	2.1%
Post-1960 Recovery Average*	3.7%

Second Quarter Forecasts	
Atlanta Fed GDPNow	1.8%
Blue Chip Consensus	2.5%
Wells Fargo Economics Group	2.6%

Sources: BEA, Haver Analytics, Atlanta Fed, Blue Chip, Wells Fargo Economics Group.
*Calculated from recoveries following recessions lasting longer than 6 months and excludes the current recovery.

In December 2015, the Federal Open Market Committee (FOMC) forecasted 2.4% growth for Q2 of 2016. In March, it revised this to 2.2%, and in June, it lowered its forecast to 2.0%. The FOMC also lowered its 2017 estimate from 2.1% to 2.0%.

Annual Revisions

The BEA also released its annual revisions to the National Income and Product Accounts (NIPAs) which affect GDP estimates back to the first quarter of 2013. Last year, real GDP grew 2.6% annualized, compared to the previous estimate of 2.4%. However, when measured from the fourth quarter of 2014 through the fourth quarter of 2015 (this measure is preferred by the FOMC), real GDP growth for 2015 was revised downward to 1.9% from 2.0%.

Overall, the average annual growth rate for real GDP from the fourth quarter of 2012 through the first quarter of 2016 remained the same at 2.2%. A deeper revision of the numbers to account for any seasonal adjustment corrections back to 2005 is not expected until 2018.

Context

Major drags on GDP growth occurred in private domestic investment, including nonresidential and residential investment, as well as private inventories. As in the first quarter, consumer spending largely propped up growth in the second quarter.

- Consumer spending rose in the second quarter after sluggish first-quarter growth. Recent retail sales data, which increased 0.6% in June, also points to stronger consumer spending.
- Any potential impact on imports and exports from Brexit missed most of this quarter, as the vote occurred at the end of the second quarter, but is expected to show up in the following quarter, most likely affecting exports.
- Businesses continue to hire modestly, but are investing less. Durable goods orders have remained weak this year, and fell 4% in June, the largest drop in nearly two years. Furthermore, fixed investment fell for the third consecutive quarter, down 3.2% in the second quarter.

Second quarter data still has two revisions to go before arriving at a final estimate. For the previous first quarter annualized real GDP growth, the first estimate of 0.5% was revised upward for a second estimate of 0.8% and was ultimately revised to 1.1% in the third and final estimate. However, due to annual revisions, first quarter real GDP growth was ultimately revised back down to 0.8%.

The Bigger Picture

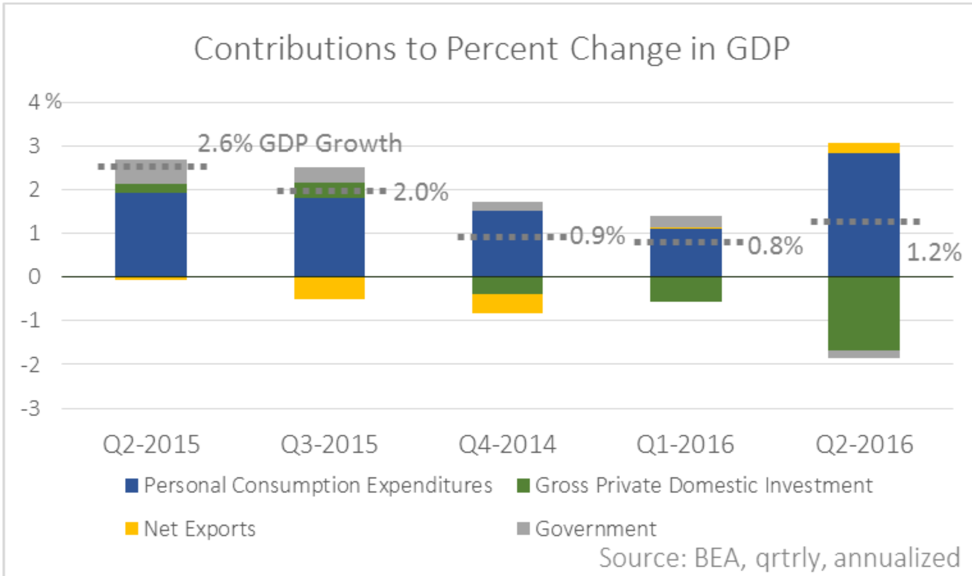
Even now, more than seven years after the recession ended, the recovery continues to be uneven across the country. Nearly two-thirds of 381 U.S. metro areas are reported to have fully recovered employment levels, according to a report for the U.S. Conference of Mayors. However, measuring by county, based on Census Bureau data, the Economic Innovation Group finds 20 counties account for half of new businesses (this is less than 1% of over 3,000 counties nationwide). In addition, just 73 counties accounted for half of job growth from 2010 to 2014. Meanwhile, recent Labor Department data indicate that business dynamism continues to decline.

- Freedom House reports that freedom in the world is on the decline in the aftermath of the recent recession. The number of countries experiencing declining freedom reached 72 last year, the largest since the 10-year decline began. Only 43 countries saw increases.
- The International Monetary Fund's (IMF) latest downgrade to global growth in July also came with a warning of increased economic, political, and institutional uncertainty following Brexit. In addition, the IMF projects real GDP growth of only 1.8% for 2016 and 2017 in the United States.
- The Federal Reserve announced no policy changes in its July Federal Open Market Committee statement last week, but noted moderate job growth and economic activity. It also noted that near-term risks to the economic outlook "have diminished." The tone gave the possibility of a rate hike for September.
- Projections of slower economic growth over the next decade abound. The Federal Reserve Bank of St. Louis notes real GDP growth remains well below its pre-recession trend: It's about 19% below trend as of the final quarter of 2015, and is projected to fall to 26% below trend by the final quarter of 2024.

Second Quarter Details

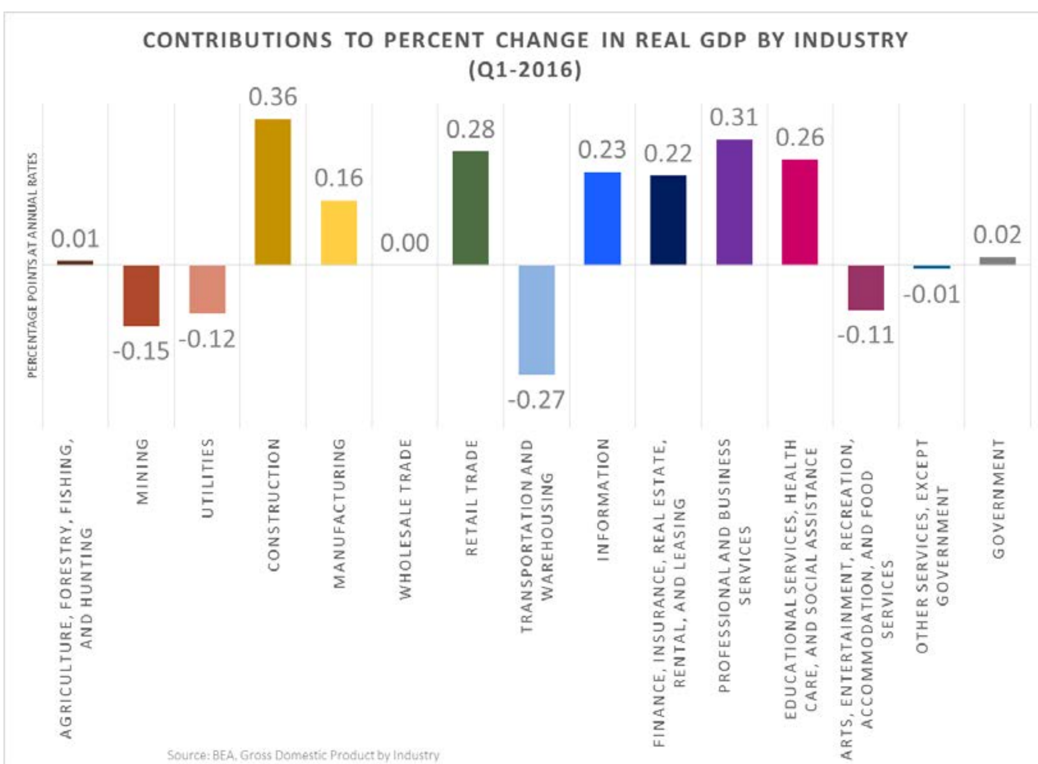
Among positive and negative contributions to GDP this quarter, the BEA release notes:

- The growth in GDP was primarily due to an acceleration in consumer spending, an upturn in exports, and a decrease in imports.
- Negative contributions resulted from declines in inventory investment, nonresidential fixed investment, and state and local government spending.



Last Thursday, the BEA release for [first quarter 2016 data for GDP by industry]() found:

- Construction, professional and business services, health care and social assistance, and retail trade led first quarter growth.
- In all, 11 of the 22 industry groups (including subgroups) contributed to the slow growth in the second quarter.



Economic Indicators

The data in the following table shows a sample of economic activity over the course of the second quarter. Forecast estimates for GDP growth are predicated upon these releases, as they reveal a little more about the economy with each month of new data. For some indicators, June data has not yet been released.

2nd Quarter Economic Indicators	April	May	June
ISM Manufacturing Index (>50 = expansion)	50.8	51.3	53.2
ISM Non-Manufacturing Index	55.7	52.9	56.5
U.S. Trade Deficit (Millions)	$(37,383)	$(41,144)	
Retail Sales	1.2%	0.2%	0.6%
Business Inventory-to-Sales Ratio	1.40	1.40	
Housing Starts	3.8%	-1.7%	4.8%
Durable Goods Orders	3.2%	-2.8%	-4.0%
Personal Income	0.5%	0.2%	
Personal Outlays	0.0%	0.4%	
Nonfarm Payroll Job Growth	144,000	11,000	287,000
Private Payroll Job Growth	147,000	(6,000)	265,000
PCE Inflation (12-mo. change)	1.1%	0.9%	
Core PCE Inflation (12-mo. change)	1.6%	1.6%	
Consumer Confidence	94.7	92.4	97.4

Source: Haver Analytics.

Upcoming Key Releases

- The annual revisions and June data for monthly Personal Income and Outlays follow on Tuesday, August 2nd, affecting data back to January 2013. Underlying detail will be released on August 5th.
- The second estimate for Q2 GDP data, based on more complete data, will be released August 26th at 8:30am. BEA will also report the estimates for gross domestic income (GDI), and the average of GDI and GDP.
- The third and final estimate for Q2 GDP data will be released on September 29th at 8:30am.