

Consumer Metrics Institute News

January 30, 2015: BEA Estimates 4th Quarter 2014 GDP Growth to be 2.64%

(Web page version is [here](#))

In their first estimate of the US GDP for the fourth quarter of 2014, the Bureau of Economic Analysis (BEA) reported an annualized rate, down -2.32% from the much celebrated +4.96% growth rate reported for the prior quarter.

The growth was nearly halved by substantial changes in a number of its components: imports took -1.55% from the quarter, government consumption took another -0.24% from the number, contracting governmental spending took another -1.20% off the top, and plunging fixed investment took another -1.20% off the headline.

Inventories and consumer spending were the only bright spots. Inventory growth added +0.85% to the headline. Increased government spending added 0.52% to the headline number, while spending on household services added 0.52% to the headline.

The increased consumer spending came from both improved disposable income and reduced savings. Households had a 0.5% increase in real per capita disposable income (now reported to be \$37,775 per annum). This is still down \$94 per year from the 4th quarter of 2013. Savings dropped another -0.1% for the quarter to 4.6%.

As mentioned last quarter, plunging energy prices are likely playing havoc with many of the numbers in this report. The headline number is down quarter-to-quarter -- pushing all consumer oriented inflation indexes firmly into negative territory. During the fourth quarter (ending in December) the seasonally adjusted CPI-U index published by the Bureau of Labor Statistics (BLS) was solidly dis-inflationary, dropping -0.2% from the prior quarter. The price index reported by the Billion Prices Project (BPP -- which arguably more fully reflected the "at the pump" inflation) was significantly more dis-inflationary, dropping a full -2.14% quarter-to-quarter (an astounding -8.30% annualized rate over the prior year).

Yet for this report the BEA still assumed a very mildly dis-inflationary annualized deflator of only -0.09%. The discrepancy between the "deflators" raises some serious consistency issues. Over reported inflation (or under reported dis-inflation) will result in distorted real numbers. BEA's "nominal" numbers were corrected for inflation using the line-item appropriate BLS CPI-U and PPI indexes, but the correction was at an implausibly high 7.17% annualized rate. Clearly the BEA's deflator is troubling, but using the more reasonable BLS deflators and growth rates when applied to the BEA's nominal data -- suggesting that the BEA's initial nominal data may be more correct than the deflators can handle.

Among the notable items in the report :

-- The headline contribution from consumer expenditures for goods was +1.20% (up +0.14% from the prior quarter).

-- The contribution made by consumer services spending to the headline surged to +1.67% (up +0.52% from the last quarter). Recreational services provided the boost, while a drop in non-profit spending provided a partial offset. The combined contribution of consumer services to the headline number by consumers was 2.87%, up +0.66% from the prior quarter.

-- Commercial private fixed investments provided only +0.37% of the headline number (down -0.84% from the 1.21% of the prior quarter). All in heavy equipment (industrial and transportation). The reported growth came almost entirely from IT spending.

-- Inventories contributed +0.82% to the headline number (up a full +0.85% from the prior quarter). This line item is the only one that shows a gain, and this gain can be expected to reverse over the coming quarters.

-- As we expected, governmental spending removed -0.40% from the headline (down -1.20% from the 3rd quarter). This was in fact entirely spurious: spending pulled forward from the 4th quarter as a result of fiscal year-end budgetary maneuvers. Opaque "seasonal adjustments," they seem to completely fail to correct for seasonal anomalies caused by Federal fiscal year-end "cynics might point out that the failure to seasonally adjust for those shenanigans consistently provides spurious growth that is reversed out until after the subsequent "State of the Union" address).

-- Exports are now reported to be contributing +0.37% to the headline growth rate (down -0.24% from the third quarter).

-- Imports subtracted -1.39% from the headline number (down -1.55% from the prior quarter). The prior quarter's imports were most susceptible to price related distortions.

-- The annualized growth rate for the "real final sales of domestic product" is now reported to be only +1.82% (down from 2.99% in BEA's "bottom line" measurement of the economy, and that "bottom line" rate lost nearly two-thirds of its prior quarter).

-- And as mentioned above, real per-capita annual disposable income was reported to have grown by \$279 per year. This is a growth rate of 3.01%. Real disposable income is still down -\$94 per year from the fourth quarter of 2012 (before the recession). This is a 2.99% in total since the second quarter of 2008 -- a pathetic 0.45% annualized growth rate over the past 6 and a half years.

The Numbers

As a quick reminder, the classic definition of the GDP can be summarized with the following equation :

$$\text{GDP} = \text{private consumption} + \text{gross private investment} + \text{government spending} + (\text{exports} - \text{imports})$$

or, as it is commonly expressed in algebraic shorthand :

$$\text{GDP} = \text{C} + \text{I} + \text{G} + (\text{X}-\text{M})$$

In the new report the values for that equation (total dollars, percentage of the total GDP, and contribution to the final growth rate) are:

GDP Components Table

	Total GDP	=	C	+	I	+	G
Annual \$ (trillions)	\$17.7	=	\$12.1	+	\$3.0	+	\$3.2
% of GDP	100.0%	=	68.4%	+	16.7%	+	18.0%
Contribution to GDP Growth %	2.64%	=	2.87%	+	1.19%	+	-0.40%

The quarter-to-quarter changes in the contributions that various components make to the overall GDP can be best understood by looking out the component contributions in more detail and over time. In the table below we have split the "C" component into fixed investment and inventories, separated exports from imports, added a line for the BEA's "Real Final Sales of Domestic Products" and rearranged the columns with the most current to the left :

Quarterly Changes in % Contributions to GDP

	4Q-2014	3Q-2014	2Q-2014	1Q-2014	4Q-2013	3Q-2013	2Q-2013	1Q-2013	4Q-2012	3Q-2012	2Q-2012
Total GDP Growth	2.64%	4.96%	4.59%	-2.11%	3.50%	4.51%	1.77%	2.75%	0.06%	2.48%	1.62%
Consumer Goods	1.20%	1.06%	1.33%	0.23%	0.83%	0.80%	0.30%	1.35%	0.67%	0.74%	0.29%
Consumer Services	1.67%	1.15%	0.42%	0.60%	1.69%	0.59%	0.93%	1.11%	0.65%	0.58%	0.57%
Fixed Investment	0.37%	1.21%	1.45%	0.03%	0.95%	1.01%	0.74%	0.42%	0.96%	0.45%	0.61%
Inventories	0.82%	-0.03%	1.42%	-1.16%	-0.34%	1.49%	0.30%	0.70%	-1.80%	-0.19%	0.27%
Government	-0.40%	0.80%	0.31%	-0.15%	-0.71%	0.04%	0.04%	-0.75%	-1.20%	0.52%	-0.08%
Exports	0.37%	0.61%	1.43%	-1.30%	1.30%	0.67%	0.82%	-0.12%	0.19%	0.28%	0.64%
Imports	-1.39%	0.16%	-1.77%	-0.36%	-0.22%	-0.09%	-1.36%	0.04%	0.59%	0.10%	-0.68%
Real Final Sales	1.82%	4.99%	3.17%	-0.95%	3.84%	3.02%	1.47%	2.05%	1.86%	2.67%	1.35%

Summary and Commentary

Well, the 5% growth was nice while it lasted. And now we know why the Fed is disinclined to remove stimulus by "ramping up" the economy.

Among our take-aways from this report are:

-- For once, and at face value, the +1.82% "bottom line" Real Final Sales growth rate (corrected for inventory change) is a reasonable number for this economy.

-- Looking back, this reports tells us that the 5% growth in the third quarter probably had more than its share of smoke and mirrors. In the Federal fiscal year end shenanigans, the political gift that keeps on giving.

-- And we hate to get technical, but we are truly troubled by consistency and transparency issues raised by this report many times before, suspecting that under reported inflation was artificially boosting the headline numbers. Now that we know the BEA under reporting price DIS-inflation), we are even more troubled by an inability to derive meaningful or plausible real-world deflators. We understand that the BEA and BLS price tracking methodologies are vastly different, and comparing the two is an apples and oranges issue. Nevertheless, however correct and consistent the BEA's -0.09% quarterly deflator is from their methodology standpoint, from a real-world perspective. Unfortunately, that absurd deflator generates a reasonable growth number when applied against nominal data. The implication is that the nominal data is just as absurd as the -0.09% deflator.

Clearly something has been pulled out of a hat. We just can't tell what.

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