# ECONOMIC UPDATE

REGIONS

July 31, 2013



## Q2 2013 Real GDP: The Now Larger U.S. Economy Lumbers Along In 2013's First Half

- Real GDP grew at an annualized rate of 1.7 in Q2 2013 following (annualized) growth of 1.1 percent in Q1.
- The GDP Price Index rose at an annualized rate of 0.7 percent during Q2.
- Today's release incorporates comprehensive revisions to all historical GDP data and newly issued data on corporate R&D spending.

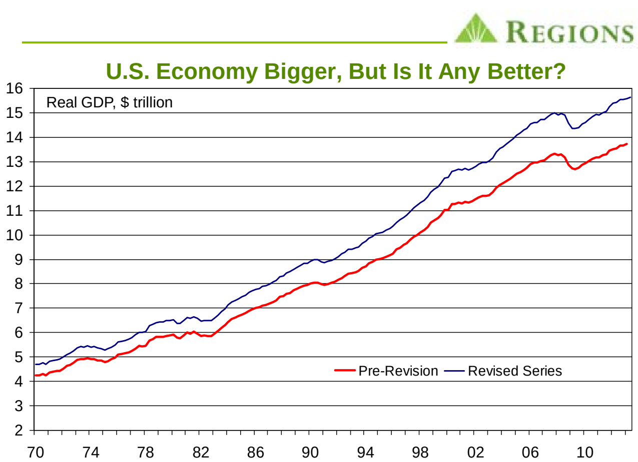
Bigger, yes. Better than ever, maybe not, and clearly not over the first half of 2013. That's the quick take on the BEA's release of revised historical GDP data along with the first estimate of Q2 real GDP growth. The BEA reports real GDP growth of 1.7 percent in Q2 2013, faster than had been anticipated but at the same time revised data show annualized growth of just 1.1 percent in Q1, slower than the previous estimate of 1.8 percent. All in all, the economy doesn't look much different over 2013's first half after accounting for the revised data.

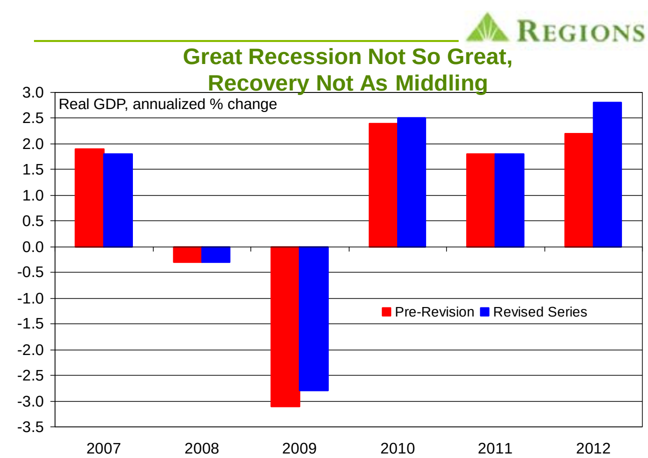
Today's release incorporates comprehensive revisions to the entire historical GDP database, with these revisions encompassing definitional changes, changes in how certain expenditures are classified, and statistical changes that include methodological changes, newly available source data, and revised source data. The most significant change is that research and development expenditures and original artistic productions will be accounted for in a new category – intellectual property products – to be included as a component of business fixed investment expenditures. We won't go into further detail on these revisions here but instead will discuss them in detail in the August edition of our *Monthly Economic Outlook* (don't worry, it will be more interesting than it sounds – really it will).

Real consumer spending grew at an annualized rate of 1.8 percent in Q2, down from growth of 2.3 percent during Q1. As has been the case over the life of the recovery, spending on consumer durable goods (such as motor vehicles and home furnishings/appliances) was far stronger than spending on household services and nondurable consumer goods. Business fixed investment grew at an annualized rate of 4.6 percent in Q2, bouncing back from a decline of 4.6 percent during Q1. After plunging by 25.7 percent (annualized) in Q1, real business spending on structures grew at a 6.3 percent annualized rate and real spending on equipment and software grew at an annualized rate of 4.1 percent. A faster build in nonfarm business inventories than seen in Q1 also supported top-line real GDP growth, as did a fourth consecutive double-digit increase in residential investment. Together, these four components added 2.56 percent to top-line real GDP growth, meaning Q2 continues the trend of private domestic demand growing at a faster rate than the overall economy.

On the flip side, a wider trade gap and further declines in consolidated government spending acted as drags on Q2 growth. Real exports of U.S. goods and services grew at an annualized rate of 5.4 percent in Q2 after an annualized decline of 1.3 percent in Q1 and better than expected given the shakier global growth environment during Q2. Real imports of goods and services, however, grew at an annualized rate of 9.5 percent, in part reflecting underlying strength of business and consumer spending. That growth in imports was so much stronger than growth in exports resulted in the wider trade gap. As expected, while real total government expenditures fell again in Q2, that decline was smaller than over previous quarters and concentrated on the federal government level as state and local government expenditures rose. The contraction in defense spending (0.5 percent) was much less severe than those seen in Q4 2012 (21.6 percent) and Q1 2013 (11.2 percent). What remains to be seen, however, is whether coming quarters bring a return of more severe cuts in defense spending, which we anticipate will be the case, or whether defense spending will be flat to only slightly lower. We do, on the other hand, expect to see continued growth in state and local government spending over coming quarters, reflecting improving budgetary conditions – though to be sure any such spending growth will remain on the moderate side.

Overall, the first half of 2013 doesn't look all that different even with the revised GDP data. The key question is whether the second half pick-up in growth that many analysts, us included, have been banking on will materialize. More significantly, the Fed has also been banking on such a pick-up, and today's GDP report is not likely to impact the timing of when the Fed begins to dial down the rate of its large-scale asset purchases, which we continue to expect to occur in September.

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