ECONOMIC UPDATE

REGIONS

July 30, 2015

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Q2 2015 Real GDP: Revised Data + New Methodology = Same Old Growth Rate

- The BEA's initial estimate shows real GDP expanded at an annualized rate of 2.3 percent in Q2 2015.
- Annual benchmark revisions show a slightly slower trend rate of real GDP growth over the 2012 – 2014 period

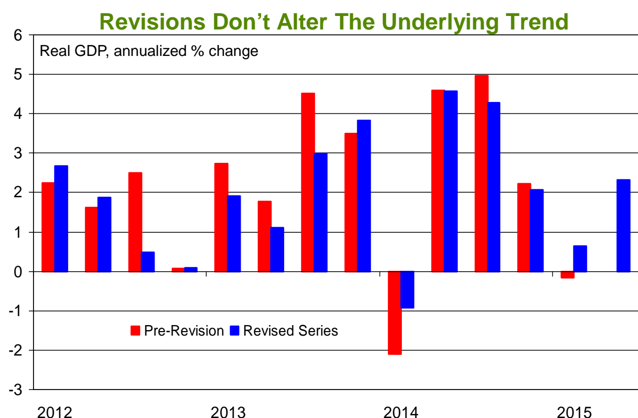
Today's release of the initial estimate of Q2 real GDP growth calls to mind the old adage "the more things change, the more they stay the same." Armed with revised source data and new methodology to remedy (at least partially) the seasonal adjustment issues that have in recent years clouded intra-year growth patterns, the BEA estimates real GDP expanded at an annualized rate of . . . 2.3 percent in Q2 2015. Which, for all the revised data and improved seasonal adjustment process, looks remarkably like the same old growth rate we've been stuck with for the past six years. As we do each and every quarter we will note the BEA's initial estimate of GDP in any given quarter is subject to incomplete source data and thus subject to what can be large revision, though some of the new methodology will at least in theory improve the accuracy of the BEA's initial estimate. That said, the first estimate of Q2 2015 came in below the consensus estimate of 2.7 percent and just a shade below our forecast of 2.4 percent growth.

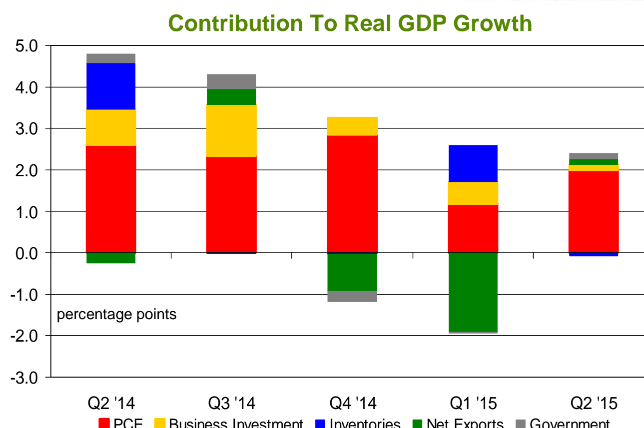
Consumer spending was the main support for top-line real GDP growth in Q2, with real consumer spending growing at an annualized rate of 2.9 percent (this added 1.99 points to top-line growth, as shown in the second chart below). Spending on motor vehicles was a key driver of overall growth in consumer spending, as annualized unit sales topped the 17 million mark in Q2 for the first time since 2005. Total inflation adjusted spending on consumer durables which, in addition to motor vehicles also includes items such as home furnishings and appliances, advanced at an annualized rate of 7.3 percent in Q2, while real spending on nondurable consumer goods grew by 3.6 percent and real spending on household services grew by 2.1 percent (these are annual rates).

Business fixed investment declined at an annualized rate of 0.6 percent in Q2 as spending on structures and equipment was down, though the sharp scaling back of investment in the energy sector acted as a significant drag in these categories in Q2. Our baseline forecast had called for energy to be less of a drag on business investment over 2H 2015 but the recent downturn in crude oil prices calls that into question. Spending on intellectual property products grew at an annual rate of 5.5 percent in Q2, continuing a nice string of advances which offers some hope for improved productivity growth in future quarters. Inventory accumulation in the nonfarm business sector was slower in Q2 than in Q1, resulting in inventories deducting slightly from top-line real GDP growth. As expected, the trade deficit narrowed a bit in Q2 which should be the last quarter for which the trade data are clouded by the West Coast port strike, leaving the focus on global growth and the stronger U.S. dollar in terms plotting the course of U.S. exports.

Methodological changes mainly revolve around correcting the residual seasonality (i.e., seasonal adjustment not fully correcting for seasonal patterns in the data) that has plagued the GDP data in recent years. This was clearly an issue with the data for Q1 of any given year, and note from the first chart below Q1 real GDP was revised higher in 2012 and 2014 but lower in 2013 (at present revisions only go back to Q1 2012), and time will tell whether residual seasonality has been fully corrected for. At the same time, since seasonal adjustment alters only the intra-year patterns of growth in any given year, upgrading Q1 means subsequent quarters by definition will be downgraded, and from the limited data we have today it looks like Q3 is the quarter that took the biggest hit. In the broader scheme, however, the trend rate of growth is now slightly lower – 2.1 percent as opposed to 2.4 percent for 2012-14 – than had been previously thought to be the case. This is perhaps the most disappointing element of the revisions, in the sense that many had been looking for growth to be revised higher, if only modestly, as a means of solving the puzzle of anemic labor productivity growth that has confounded analysts and policy makers over recent years. We were not looking for as much along these lines as were some others, but the bottom line is slow productivity growth remains an issue which must be dealt with but first has to be more fully understood than it now is.

All in all, today's report doesn't alter the broader view of the U.S. economy, with growth still in the steady though by no means satisfying range that has persisted since the end of the 2007-09 recession.





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