

## U.S. NATIONAL GDP ACCOUNTS JANUARY 27, 2011

### U.S. Q4 GDP rose an annualized 2.8% in Q4 on inventory gain

#### Implications

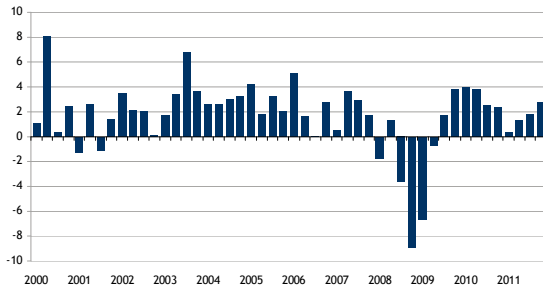
The advance estimate of U.S. Q4 GDP growth was 2.8%, up from 1.8% and 1.3% increases in the third and second quarters, respectively, although slightly below market expectations for a 3.0% increase. The main contributor to the acceleration in growth in Q4 was a sizeable 1.9 percentage point (ppt) add from inventories that more-than-reversed a 1.4 ppt drag in Q3. Consumer spending growth accelerated modestly to a 2.0% rate in the fourth quarter, up from a 1.7% gain in Q3 that was already stronger than the disappointing 0.7% Q2 increase. Residential investment rose a solid 10.9% in Q4, marking the third consecutive quarterly increase following 1.2% and 4.2% increases in Q3 and Q2, respectively.

Providing the main source of offset to stronger activity elsewhere, government spending plunged 4.6% in Q4, led by a 12.5% decline in defense spending. The drop in defense spending itself subtracted 0.7 ppts from quarterly GDP growth. As well, growth in business investment slowed to a 1.7% rate from an outsized 15.7% gain in Q3. Net exports subtracted 0.1 ppts from GDP growth after adding 0.4 ppts in Q3.

The rise in GDP in Q4 leaves the average annualized pace of growth over the second half of 2011 at 2.3% which, while still modest for this point in an economic recovery, marks an encouraging acceleration from the first half of the year when growth averaged less than a 1% per quarter. Much of the strength in Q4 reflected a sizeable add to growth from inventories that is not likely to be repeated. This suggests some downside risk to our forecast for GDP growth early in 2012; however recent strengthening in labour markets, including a slowing trend in layoffs, bodes well for consumer spending to continue to grow. As well, early indications of improving business confidence and a sharp rise in capital equipment orders in December points to a return to stronger growth in business investment and the sharp decline in government defense spending in Q4 is also unlikely to be repeated. Potential spillover from events in Europe, in addition to ongoing domestic fiscal retrenchment, also continue to provide sources of downside risk; however, the flow of data available to this point remains broadly consistent with GDP growth remaining close to the 2.8% Q4 rate in the current quarter.

Real GDP: U.S.

Annualized quarter-over-quarter % change



Source: Bureau of Economic Analysis, RBC Economics

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## Data details

- U.S. GDP rose an annualized 2.8% in Q4, up from a 1.8% increase in Q3 and a 1.3% Q2 gain. Market expectations were for a slightly stronger 3.0% increase in Q4.
- Much of the gain in GDP growth in Q4 was the result of an outsized 1.9 percentage point (ppt) add to growth from inventory investment that more than retraced a 1.4 ppt subtraction in Q3. Stronger growth in consumer spending (2.0% vs. a 1.7% Q3 gain) and a 10.9% rise in residential investment also contributed to the improvement.
- The main factors preventing stronger GDP growth were a sizeable 4.6% drop in government spending, much of which reflected an outsized 12.5% drop in defense spending that on its own subtracted 0.7 ppts from GDP growth, along a moderation in growth in business investment.
- The pace of GDP growth remains historically modest for this point in the recovery; however the acceleration to an average 2.3% rate in the second half of 2011 after disappointing growth of less than 1% in the first half of the year is encouraging, particularly given the impact that the European debt crisis had on confidence over the summer and fall. The strength in inventories implies some downside risk to growth in the current quarter though a rebound in defense spending will provide some offset. We expect this will keep Q1 growth close to the 2.8% Q4 rate reported today.

## Q4 national accounts – first estimate

Annualized % change from previous quarter

	Q4-10	Q1-11	Q2-11	Q3-11	Q4-11
Consumer Spending	3.6	2.1	0.7	1.7	2.0
Durables	17.2	11.8	-5.3	5.7	14.8
Non-Durables	4.3	1.6	0.2	-0.6	1.6
Services	1.3	0.8	1.9	1.9	0.2
Business Fixed Investment	7.5	1.2	9.2	13.0	3.3
Residential	2.5	-2.5	4.2	1.2	10.9
Non-residential Structures	10.6	-14.4	22.6	14.4	-7.2
Equipment and Software	8.0	8.7	6.3	16.2	5.2
Government Spending	-2.8	-5.9	-0.9	-0.1	-4.6
Inventory Change (\$ bn)	38.3	49.1	39.1	-2.0	56.0
Final domestic demand	2.7	0.4	1.3	2.7	0.9
Exports of Goods and Services	7.8	7.9	3.6	4.7	4.6
Imports of Goods and Services	-2.3	8.3	1.4	1.2	4.4
<b>Real GDP</b>	<b>2.3</b>	<b>0.4</b>	<b>1.3</b>	<b>1.8</b>	<b>2.8</b>

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