Moody's Analytics

Actual:	4.13%
Previous: **	3.60%
Coverage:	2013Q3
Next Release:	01/30/2014
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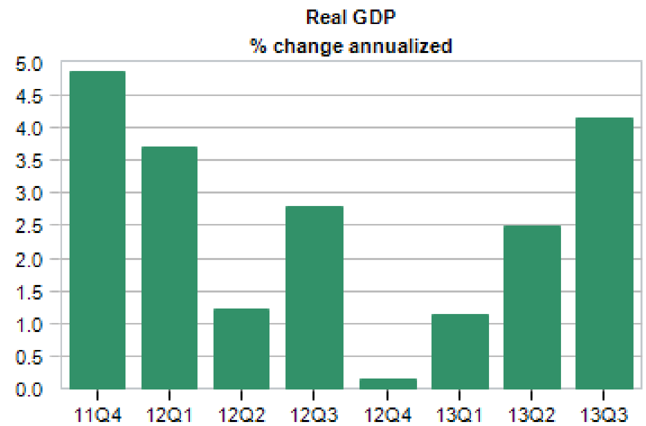
**Before any revisions



First Take

Real GDP grew in the third quarter by 4.1% (SAAR), according to the Bureau of Economic Analysis' third estimate. This was up from the second reading of 3.6% and a gain of 2.5% in the second quarter. The acceleration came from slower growth in imports and faster growth in state and local government spending but was dominated by inventory investment, which bodes ill for the fourth quarter. The revisions were largely from consumer spending. Corporate profits rose 1.9% in the quarter, down from 3.3% in the second quarter. Gross domestic income added only 1.8%, its slowest advance in a year. Inflation accelerated in the quarter, but real disposable income growth slowed. The saving rate increased modestly.

Gross Domestic Product	13Q3	13Q2	13Q1	12Q4	12Q3	12Q2	12Q1	11Q4
Annualized % change								
Real	4.13	2.48	1.15	0.14	2.78	1.2	3.71	4.87
Nominal	6.19	3.08	2.83	1.58	4.93	3	5.76	5.41
Implicit price deflator	1.97	0.58	1.67	1.43	2.09	1.77	1.97	0.51
Contributions to real GDP, annualized % change, ppt								
Consumption	1.36	1.24	1.54	1.13	1.15	1.28	1.98	1.65
Fixed investment	0.89	0.96	-0.23	1.63	0.39	0.68	1.21	1.39
Fixed residential investment	0.31	0.4	0.34	0.5	0.35	0.15	0.53	0.29
Fixed nonresidential investment	0.58	0.56	-0.57	1.13	0.04	0.53	0.68	1.1
Inventories	1.67	0.41	0.93	-2	0.6	-0.91	0.36	2.73
Net exports	0.14	-0.07	-0.28	0.68	-0.03	0.1	0.44	-0.6
Government	0.08	-0.07	-0.82	-1.31	0.67	0.05	-0.28	-0.31

Gross Domestic Income	13Q3	13Q2	13Q1	12Q4	12Q3	12Q2	12Q1	11Q4
Annualized % change								
Real	1.8	3.21	2.44	4.85	0.88	-0.62	5.44	2.58
Nominal	3.8	3.81	4.15	6.35	2.99	1.14	7.52	3.1

Corporate Profits	13Q3	13Q2	13Q1	12Q4	12Q3	12Q2	12Q1	11Q4
% change								
Total with IVA and CCA	1.88	3.31	-1.3	1.73	0.7	0.93	-0.68	5.26
Profits before tax	2.09	2.12	-1.63	0.95	2.25	-0.1	12.99	4.39
Profits after tax	2.6	2.05	-0.65	1.53	2.26	0.31	11.64	4.25

Source: Bureau of Economic Analysis

The Numbers

- This was the BEA's third estimate of GDP for the third quarter. It reported that the economy rose 4.1% on an annualized basis, above the 2.5% addition in the prior quarter. The initial release had growth at 2.8% and the second estimate was 3.6%.
- Growth was dominated by inventory investment. It contributed 1.7 percentage points, more than 40% of the total increase. This is a negative for the outlook for the fourth quarter.
- Consumer spending contributed 1.4 percentage points to growth, slightly more than in the second quarter, but 0.4 percentage point more than previously reported, accounting for the bulk of the upward revision. Services, especially healthcare and recreation, led the revision, although nondurable goods, mainly energy goods, also contributed.
- Fixed investment was also a driver of growth, although its contribution was marginally smaller than in the second quarter. Trade made a small positive contribution after being a minor drag in the second quarter. The slowing in spending gains was due to weaker service spending.
- Government made its first positive contribution in a year, thanks to expanding state and local government spending. The federal government remained a drag.
- The Personal Consumption Expenditures index showed faster inflation than in the second quarter. It rose 1.9% in the quarter, marginally below the 2% reported last month and well above the 0.1% decline in the second quarter. Excluding food and energy, inflation rose from 0.6% to 1.4%, also revised down marginally. Inflation remains low enough to encourage the Federal Reserve to maintain loose monetary policy.
- Real disposable income increased 3%, down from a 4.1% gain in the prior quarter. Since income growth outpaced that of spending, the saving rate rose from 4.7% to 4.9% (previously reported as 5%).
- Corporate profits rose 1.9% (not annualized) in the third quarter, down from growth of 3.3% in the second quarter. This number was initially reported as a 1.8% increase last month. The gain was led by domestic industries, although profits for foreign industries improved from the second quarter. Domestically, profits rose more for nonfinancial industries.
- Gross domestic income, an alternative measure of the size of the economy, grew an upwardly revised 1.8% after adding 3.2% in the second quarter. This was the slowest advance in one year and the first time growth in gross domestic income lagged GDP growth over the same interval.

Behind the Numbers

Economic growth accelerated in the third quarter, and even more than previously reported. However, more than three quarters of the acceleration came from faster inventory accumulation and is, therefore, a negative for the outlook in the next few quarters. Growth in real final sales of domestic product, GDP minus inventory accumulation, accelerated only to 2.5% in the third quarter from 2.1% in the second quarter.

The quarter covers the period before the government shutdown, and during most of the quarter, it was widely thought Congress would reach an agreement avoiding the shutdown. Hence, the modest growth in final sales and gross domestic income show that the economy was feeling the effects of intense fiscal headwinds even before the shutdown and rising inventories call into question whether businesses were fully prepared for the impact. Tax increases and government spending reductions, of which the across-the-board cuts from budget sequestration are only a part, hit the economy hard this year. Fiscal austerity has been more intense this year than at any time since the U.S. was demobilized after World War II.

Real GDP rose 2% over the four quarters ending with the third quarter, up from 1.6% in the second quarter. However, excluding inventory investment, year-ago gains in final sales remained at 1.7% for the third straight quarter and were the weakest since the third quarter of 2010. A year earlier, year-over-year growth was nearly 3% by either measure. Residential investment is strongly leading, with government spending declines, especially for federal defense spending, the largest drag. Consumer spending is increasing at about the same pace as overall GDP. Forward-looking indicators are mixed; rapid inventory accumulation are a drag, but expectations for faster consumer spending and continued advances in residential investment are still positives. Hence, the outlook for faster growth next year remains intact.

Preconditions are in place for much stronger economic expansion in 2014. Evidence of this underlying strength is clearest in the job market. Payroll employment gains have accelerated to around 200,000 net new jobs per month and are increasingly broad-based across industries and pay levels. The problems and imbalances that developed during the housing bubble nearly a decade ago have largely been corrected. Households have significantly reduced their debt burdens. The banking system is well-capitalized and highly liquid. The financial health of nonfinancial businesses is strong.

The main missing ingredient for stronger growth is confidence. The nightmare of the Great Recession weighs heavily on the collective psyche, and political brinkmanship and policy uncertainty have been hard to bear. But sentiment has improved with the budget deal and apparent reduction in brinkmanship in Washington. Investors are especially upbeat, as stock prices continue to hit record highs. With the reduction in fiscal drag and release of pent-up demand, 2014 could be a breakout year for the economy.