Economic News and Insights

Seacoast NATIONAL BANK

Economic Perspectives

Revised Fourth Quarter Gross Domestic Product

GDP Revised Down to Negative 6.2%

Steepest Decline Since Q1 1982

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The Commerce Department reported Friday in its revised estimate of GDP that the nation's economy contracted in the fourth quarter much more severely than originally thought. GDP (Gross Domestic Product) declined at an annual rate of 6.2% in the fourth quarter of 2008 as compared to the advance estimate of –3.8% issued a month ago. The revised estimate is based on more complete data.

The GDP is the "top line" measure of the nation's economy and the broadest measure of goods and services produced in the nation. The negative 6.2% growth rate is the poorest showing since the first quarter of 1982 when the economy contracted at 6.4%. The current contraction is largely the product of shrinking business inventories, exports and consumer spending although most major components revealed a worse showing than originally thought.

The advance estimate last month showed that business inventories rose an estimated $6.2 Billion — a figure that surprised many economists. We opined at that time that inventories were high in relation to sales and that high inventories would set the stage for a larger GDP decline going forward. Friday's revised estimate however, shows that inventories actually shrank $19.9 Billion in the fourth quarter thereby confirming our expectation.

Exports were a significant support to the nation's GDP in 2007 and part of 2008 however real exports of goods and services decreased 23.6% in the fourth quarter. That is in stark contrast to a modest decline of 3.0% in the third quarter. The decline is a clear reaction to the softening global economy where many U.S. trading partners, such as Great Britain, the Euro Zone, Eastern Europe and the Far East are either in recession or on the edge.

Real personal consumption expenditures fell 4.3% in the fourth quarter as compared to a decrease of 3.8% in the third. At the end of the year, consumers cut back spending the most in 28 years. Durable goods (those expected to last at least three years) including cars, appliances and furniture were the hardest hit although consumers have clearly cut back on non-durable goods, especially discretionary items.

Businesses have now cut back severely as well. Non residential fixed investment decreased 21.1% compared to a decrease of only 1.7% a quarter earlier. Investment in non-residential structures decreased 5.9% compared to an increase of 9.7%. Equipment and software purchases decreased 28.8% — over three times the rate of the previous quarter.

Residential investment has been a drag on the GDP for three full years. In the fourth quarter investment fell 22.2% and subtracted 0.82% from the GDP. That was the 12th consecutive decline and the third largest single quarter decline on record. Residential investment now contributes about 2.9% to GDP which is an all time low. The cycle high was 5.5%. The contribution to residential investment will remain low as long as builders are forced to cut construction starts to reduce inventories.

Looking forward, we expect the first quarter of 2009 to decline 5% with some modest improvement late in the year. When the books close on 2009 they will probably show that the economy contracted 3.5±% for the year.

Quarter	GDP Growth
Q4 2008	-6.2% Preliminary
Q3 2008	-0.5%
Q2 2008	2.8%
Q1 2008	0.87%
Q4 2007	-0.17%
Q3 2007	4.67%
Q2 2007	4.71%
Q1 2007	0.05%

The **Bureau of Labor Statistics** of the Commerce Department continually revises the GDP as more data become available. The first release is the "advance" release. That is followed about 30 days later by the "preliminary" release and in another 30 days by the "final" release.

The estimates are probably never truly final but evolve over time. Each July the Commerce Department releases annual revisions that could date back several years. Additionally, a significant revision occurs every five years. The next will be in July 2009.

How is GDP Calculated?

The formula is surprisingly simple (although the inputs are not).

Income (Household Consumption)
+
Investment (Business, Household & Government)
+
Government Consumption (Goods and Services)
+
Net Trade (Exports minus imports)
=
GDP

Questions, comments, observations, suggestions or additional information?
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