ECONOMIC UPDATE

REGIONS

January 29, 2016

Q4 2015 Real GDP: Consumers, Housing The Only Bright Spots In A Dim Q4

- The BEA's initial estimate shows annualized real GDP growth of 0.7 percent in Q4 2015. Real GDP grew by 2.4 percent for all of 2015.
- Consumer spending and residential investment were the main supports for Q4 growth; inventories and trade were the main drags on growth.

The BEA's initial estimate pegs real GDP growth at an annualized rate of 0.7 percent in Q4 2015. As is the case in any given quarter, the BEA's initial estimate of GDP is based on highly incomplete source data and, as such, subject to what can be large revisions. That said, there are no revisions that will save Q4 from going down as a quarter to forget. For all of 2015, the U.S. economy grew by 2.4 percent, based on the preliminary data, matching 2014's growth rate.

Real consumer spending grew at an annualized rate of 2.2 percent in Q4, with spending on consumer durables rising at a 4.3 percent pace. Real spending on motor vehicles and parts is reported to have declined at an annual rate of 4.9 percent in Q4 despite modestly higher unit motor vehicle sales. This simply reflects the weak pricing environment in the goods sector of the economy. Still, the decline in real spending on motor vehicles was more than offset by double-digit growth in spending on recreational goods and vehicles and solid growth in spending on home furnishings, appliances, and other household equipment. Real spending on nondurable goods rose at an annual rate of 1.5 percent in Q4, but this comes after two quarters of growth of better than four percent and some slowdown was inevitable.

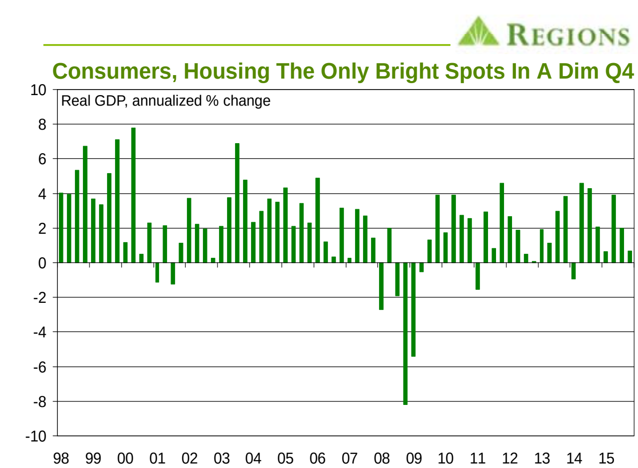
Spending on household services, which accounts for roughly two-thirds of all consumer spending, grew at an annual rate of 2.0 percent in Q4. Spending on recreational services, food services, lodging, and health care drove growth in overall services spending, while unseasonably warm weather held down spending on utilities. We will caution that this is one element of the GDP data subject to potentially large revision – it will not be until the Q4 Survey of Services is released on March 10 that BEA will have a final tally on Q4 services spending which will be reflected in their third estimate of Q4 real GDP due on March 25.

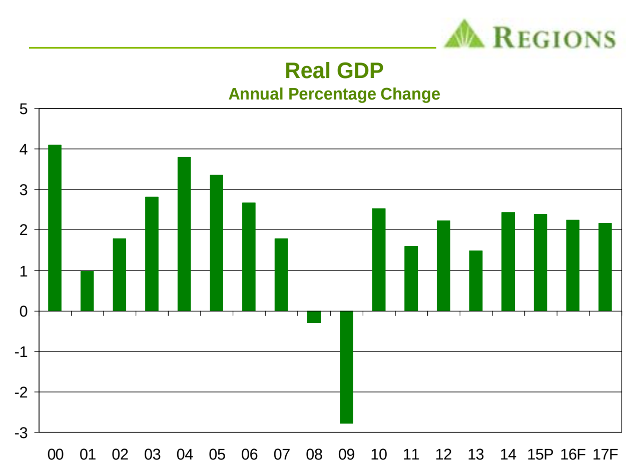
Fixed investment was a neutral factor in Q4 real GDP growth, with growth in residential investment being offset by a decline in business investment. Total real residential investment grew at an annualized rate of 8.2 percent in Q4, with solid growth in both single family and multi-family investment. In contrast, business fixed investment declined at an annual rate of 1.8 percent, the first such decline since Q3 2012. In Q4 firms cut spending on equipment and structures, while spending on intellectual property products rose by just 1.6 percent following a decline in Q3. There was a notable slowdown in the rate of inventory accumulation in the nonfarm business sector, which alone took 0.45 percentage points off of top-line real GDP growth.

Trade was another sizeable drag on Q4 growth, taking 0.47 percentage points off of top-line growth. Real exports of U.S. goods fell at an annual rate of 5.4 percent while real imports of goods rose at a 0.6 percent pace. The total real trade deficit widened to $566.5 billion (annualized) in Q4 from $546.1 billion in Q3.

As noted earlier today's first pass at the Q4 GDP data will be revised two more times as more complete source data become available. But, don't count on those revisions making Q4 look any better. Indeed, we expect business fixed investment to be revised lower and also look for the trade gap, when all is said and done, to be at least marginally wider than the estimate incorporated into today's release. More significantly, we were surprised by the estimate of inventory accumulation in today's release. We, and almost every other analyst, had built in a much more pronounced slowdown in the rate of inventory accumulation in Q4 than BEA reports. This means one of two things – either the BEA will lower their estimate of Q4 inventory accumulation, and in turn Q4 real GDP growth, or the inventory drawdown in Q1 will be more pronounced than we expected, posing a downside risk to Q1 real GDP growth.

It is starting to seem that Q1 2016 may not look all that different than Q4 2015. Consumer spending and housing will be the main drivers of growth, with a modest assist from government spending, but business investment, trade, and inventories are again likely to weigh on growth. The net result will likely be another quarter of the same 2.0 to 2.5 percent we've come to know but not necessarily love since the end of the 2007-09 recession.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com