U.S. Data Review

- Q3 GDP: robust growth led by consumer spending and inventory investment
- Inflation gauges: firm increase in the GDP price index, but moderate advance in the core PCE index

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Q3 GDP

- U.S. GDP surged 4.9 percent, annual rate, in the third quarter, brisker than the consensus expectation of a jump of 4.5 percent. The reading suggests a firm underlying performance in the economy, although a portion of the advance stems from factors that could reverse in coming quarters. Moreover, we still anticipate significant moderation in growth in Q4.

- Consumer spending led the advance in Q3 with a jump of 4.0 percent, annual rate (a contribution of 2.69 percentage points to growth). Outlays for goods rose 4.8 percent, rebounding from a paltry increase of 0.5 percent in Q2, while spending on services jumped 3.6 percent. Although the performance undoubtedly was strong, we remain cautious about the consumer sector. In particular, spending for services may have represented pent-up demand following previous COVID-related shutdowns. That is, a return to pre-pandemic normal allowed individuals to splurge on travel, live entertainment, and other events, which means slowing is likely after the initial burst. Perhaps more importantly, we strongly suspect that a depletion of excess pandemic-related savings and higher interest rates across all consumer loans will pose notable headwinds well into next year.

GDP and Related Items*

	23-Q1	23-Q2	23-Q3
Gross Domestic Product	2.2	2.1	4.9
Personal Consumption Expenditures	3.8	0.8	4.0
Nonresidential Fixed Investment	5.7	7.4	-0.1
Nonresidential Structures	30.3	16.1	1.6
Nonresidential Equipment	-4.1	7.7	-3.8
Intellectual Property Products	3.8	2.7	2.6
Change in Business Inventories (Contribution to GDP Growth)	-2.2	0.0	1.3
Residential Construction	-5.3	-2.2	3.9
Total Government Purchases	4.8	3.3	4.6
Federal Government Purchases	5.2	1.1	6.2
State and Local Govt. Purchases	4.6	4.7	3.7
Net Exports (Contribution to GDP Growth)	0.6	0.0	-0.1
Exports	6.8	-9.3	6.2
Imports	1.3	-7.6	5.7
Additional Items			
Final Sales	4.6	2.1	3.5
Final Sales to Domestic Purchasers	3.8	2.0	3.5
Gross Domestic Income	0.5	0.7	- -
Average of GDP & GDI	1.4	1.4	- -
GDP Chained Price Index	3.9	1.7	3.5
Core PCE Price Index	5.0	3.7	2.4

** Percent change SAAR, except as noted.*
Source: Bureau of Economic Analysis via Haver Analytics

- Government expenditures also were robust in Q3, increasing 4.6 percent, annual rate (a contribution of 0.79 percentage point to growth). Federal government outlays jumped 6.2 percent, while state and local spending advanced 3.7 percent. The brisk pace of federal government spending was influenced importantly by an increase of 8.0 percent in defense-related expenditures, which likely in part reflected support to Ukraine and other allies. The firm pace of spending at the state/local level is currently experiencing a tailwind from previously allocated COVID relief funds that are only now being deployed.

- Inventory investment made a large positive contribution of 1.32 percentage points to growth in Q3. However, the contribution to growth is likely to be transient in nature. A muddled demand outlook for next year, amid a concerted effort by the Federal Reserve to slow growth through restrictive monetary policy, raises the possibility of firms managing stocks cautiously in coming quarters (which likely will translate to drags from inventory investment).

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- Residential construction increased 3.9 percent, annual rate (a contribution of 0.15 percentage point to growth), but this followed declines in the preceding nine quarters and the outlook is unfavorable. The housing sector is one of the most interest rate sensitive areas of the economy; with elevated mortgage rates and tight lending standards pushing many potential homebuyers to the sidelines, builders are likely to curtail construction activity until conditions improve – an unlikely scenario in the near-term, as the Fed is likely to keep interest rates in restrictive territory for some time.

- Business fixed investment was unimpressive in Q3, slipping 0.1 percent (a contribution of 0.0 percentage point to GDP). Investment in intellectual property rose at a solid clip (2.6 percent), suggesting that research and development spending is being well maintained to facilitate future investment, but other areas were soft. Investment in structures rose 1.6 percent, decelerating sharply from increase of 16.1 percent and 30.3 percent in Q2 and Q1, respectively. The CHIPS Act and Inflation Reduction Act had spurred investment in production facilities for microprocessors and green energy initiatives, but the Q3 performance in investment suggests that the influence is fading. Equipment spending declined 3.8 percent, the third decline in the past four quarters.

- Net exports were a modest drag on GDP growth (-0.1 percent). Trade flows were firm, with exports increasing 6.2 percent and imports advancing 5.7 percent, but the larger dollar volume of imports led to the negative contribution to growth

- Inflation readings were mixed in Q3. The GDP price index rose 3.5 percent, annual rate, faster than the consensus view of 2.7 percent. However, the headline price index for personal consumption expenditures, the preferred inflation measure of Fed officials, increased 2.9 percent, annual rate, while the core index increased 2.4 percent – only moderately above the Fed's inflation target of 2.0 percent. The return to 2.0 percent inflation is not yet assured, and the path is unlikely to be linear, but price pressure is easing in response to restrictive monetary policy.