GDP and the Economy

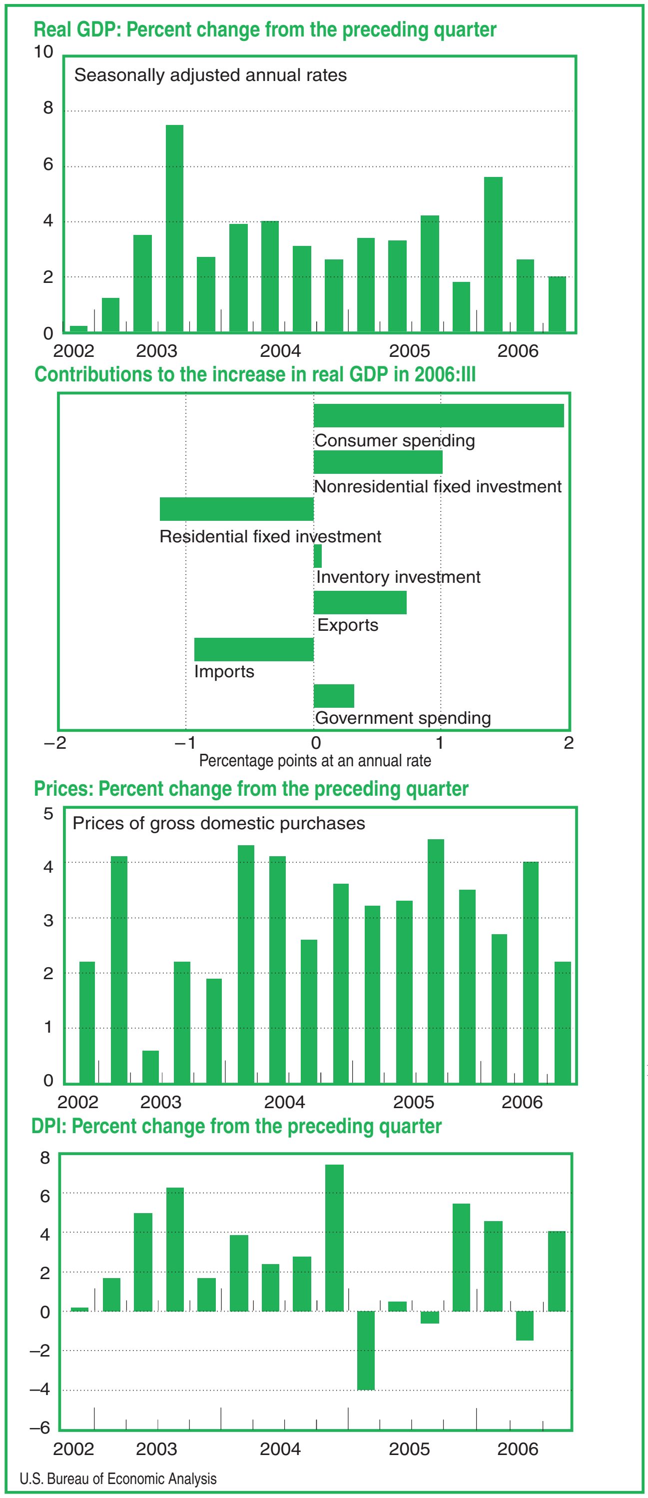
Final Estimates for the Third Quarter of 2006

ECONOMIC growth slowed in the third quarter of 2006, according to the "final" estimates of the national income and product accounts (NIPAs).[1] Real gross domestic product (GDP) increased 2.0 percent, revised down 0.2 percentage point from the "preliminary" estimate. In the second quarter, GDP increased 2.6 percent (chart 1 and table 1).[2]

The slowdown reflected an acceleration in imports (a subtraction in the GDP calculation), a larger decrease in residential investment, and decelerations in consumer spending for services, in inventory investment, and in state and local government spending.[3] The slowdown was moderated by upturns in equipment and software investment, consumer spending for durable goods, and Federal Government spending.

- Prices of goods and services purchased by U.S. residents increased 2.2 percent, 0.1 percentage point more than the "preliminary" estimate, following a 4.0-percent increase. Energy prices decelerated sharply, while food prices accelerated.
- Real disposable personal income (DPI) increased 4.1 percent, 0.4 percentage point more than the "preliminary" estimate; it decreased 1.5 percent in the second quarter.
- Corporate profits increased $61.5 billion (3.9 percent at a quarterly rate) after increasing $22.7 billion (1.4 percent) in the second quarter. See the box "Corporate Profits and the Economy" (page 6).
- The personal saving rate, personal saving as a percentage of current-dollar DPI, was –1.2 percent; in the second quarter, it was –1.4 percent.
- Real gross national product (GNP) increased 1.8 percent, compared with a 2.3-percent increase.

Chart 1. GDP, Prices, Disposable Personal Income (DPI)



1. Each GDP estimate for a quarter (advance, preliminary, and final) incorporates increasingly comprehensive and improved source data. More information can be found at <www.bea.gov/bea/about/infoqual.htm> and <www.bea.gov/bea/faq/national/gdp_accuracy.htm>. Quarterly estimates are expressed at seasonally adjusted annual rates, which show the value of an activity if the quarterly rate were maintained for a year.

2. "Real" estimates are in chained (2000) dollars, and price indexes are chain-type measures.

3. In this article, "consumer spending" refers to the NIPA series "personal consumption expenditures," "inventory investment" refers to "change in private inventories," "Federal Government spending" refers to "Federal Government consumption expenditures and gross investment," and "state and local government spending" refers to "state and local government consumption expenditures and gross investment."

Christopher Swann prepared this article.

Real GDP Overview

Table 1. Real Gross Domestic Product and Components

[Seasonally adjusted at annual rates]

	Share of current-dollar GDP (percent)	Change from preceding period (percent)				Contribution to percent change in real GDP (percentage points)			
	2006	2005	2006			2005	2006		
	III	IV	I	II	III	IV	I	II	III
Gross domestic product[1]	**100.0**	**1.8**	**5.6**	**2.6**	**2.0**	**1.8**	**5.6**	**2.6**	**2.0**
Personal consumption expenditures	**70.2**	**0.8**	**4.8**	**2.6**	**2.8**	**0.53**	**3.38**	**1.81**	**1.96**
Durable goods	8.1	–12.3	19.8	–0.1	6.4	–1.08	1.50	–0.01	0.50
Nondurable goods	20.6	3.9	5.9	1.4	1.5	0.79	1.20	0.30	0.32
Services	41.5	2.0	1.6	3.7	2.8	0.83	0.67	1.52	1.14
Gross private domestic investment	**16.8**	**16.2**	**7.8**	**1.0**	**–0.8**	**2.51**	**1.31**	**0.17**	**–0.13**
Fixed investment	16.3	2.8	8.2	–1.6	–1.2	0.46	1.34	–0.27	–0.19
Nonresidential	10.7	5.2	13.7	4.4	10.0	0.52	1.36	0.45	1.01
Structures	3.2	12.0	8.7	20.3	15.7	0.31	0.25	0.56	0.46
Equipment and software	7.5	2.8	15.6	–1.4	7.7	0.21	1.11	–0.10	0.55
Residential	5.6	–0.9	–0.3	–11.1	–18.7	–0.06	–0.02	–0.72	–1.20
Change in private inventories	0.5	....	....	....	....	2.05	–0.03	0.44	0.06
Net exports of goods and services	**–6.0**	....	....	....	....	**–1.07**	**–0.04**	**0.42**	**–0.19**
Exports	11.2	9.6	14.0	6.2	6.8	0.97	1.41	0.66	0.73
Goods	7.9	11.5	17.3	6.0	9.4	0.80	1.20	0.45	0.71
Services	3.2	5.5	6.7	6.7	0.8	0.17	0.21	0.21	0.03
Imports	17.2	13.2	9.1	1.4	5.6	–2.04	–1.46	–0.24	–0.93
Goods	14.6	14.1	9.4	–0.1	7.1	–1.84	–1.27	0.01	–1.00
Services	2.6	8.3	7.4	9.9	–2.6	–0.20	–0.19	–0.25	0.07
Government consumption expenditures and gross investment	**19.1**	**–1.1**	**4.9**	**0.8**	**1.7**	**–0.21**	**0.94**	**0.16**	**0.32**
Federal	7.0	–4.6	8.8	–4.5	1.3	–0.33	0.61	–0.32	0.09
National defense	4.6	–9.9	8.9	–2.0	–1.2	–0.49	0.41	–0.09	–0.06
Nondefense	2.3	7.1	8.5	–9.3	6.5	0.16	0.20	–0.23	0.15
State and local	12.1	1.0	2.7	4.0	1.9	0.13	0.33	0.48	0.23
Addenda:									
Final sales of domestic product	....	–0.3	5.6	2.1	1.9	–0.28	5.61	2.11	1.90
Gross domestic purchases price index	....	3.5	2.7	4.0	2.2	....	....	....	....
GDP price index	....	3.3	3.3	3.3	1.9	....	....	....	....

1. The estimates of GDP under the contribution columns are also percent changes.

NOTE. Percent changes are from NIPA table 1.1.1, contributions are from NIPA table 1.1.2, and shares are from NIPA table 1.1.10.

Consumer spending accelerated slightly in the third quarter, contributing 1.96 percentage points to real GDP growth. Durable-goods spending turned up, reflecting an upturn in motor vehicles and parts, especially light trucks. Nondurable-goods spending accelerated, as clothing and shoes turned up.

Nonresidential fixed investment picked; equipment and software spending turned up.

The decrease in residential investment was larger than in the previous quarter for the second straight quarter and was the largest since the first quarter of 1991. The larger third-quarter decrease reflected a larger decrease in single-family structures and a downturn in "other" structures.

Inventory investment slowed, reflecting downturns in mining, utilities, and construction, in manufacturing, and in "other" industries.

Exports stepped up. Goods exports accelerated, as automotive vehicles, engines, and parts turned up. Service exports decelerated.

Imports accelerated. Petroleum and products and "nonpetroleum industrial supplies and materials" turned up; nonautomotive consumer goods accelerated. Imports of services turned down.

Federal Government spending turned up, primarily reflecting an upturn in nondefense spending.

Real final sales of domestic product (real GDP less inventory investment) slowed, increasing 1.9 percent after increasing 2.1 percent.

GDP and Gross Domestic Purchases

In addition to gross domestic product (GDP), another related measure of economic growth—gross domestic purchases—is included in the national income and product accounts (NIPAs).

GDP measures the market value of final goods and services produced by labor and property in the United States, including the goods that are added to, or subtracted from, inventories. GDP is defined as the sum of consumer spending, business and residential investment, inventory investment, government spending, and exports less imports.

Gross domestic purchases is defined as GDP less exports plus imports. It measures domestic demand for goods and services regardless of their origin. Exports represent foreign demand for U.S. goods and services. Subtracting exports from GDP yields a measure of expenditures that focuses on domestic buyers. Imports can be viewed as the value of goods and services that exceed the domestic supply and that expand the consumption and investment alternatives for domestic purchasers.

Differences between GDP and gross domestic purchases reflect patterns in imports less exports: As imports exceed exports, gross domestic purchases exceeds GDP.

For annual and quarterly estimates of these measures, see NIPA tables 1.4.1 and 1.4.3–1.4.6.

For more information on GDP and gross domestic purchases, see also "A Guide to the National Income and Product Accounts of the United States" on BEA's Web site at <www.bea.gov/bea/an/nipaguid.pdf>.

Revisions to GDP

Table 2. Preliminary and Final Estimates for the Third Quarter of 2006

[Seasonally adjusted at annual rates]

	Change from preceding quarter (percent)			Contribution to percent change in real GDP (percentage points)		
	Prelim-inary	Final	Final minus prelim-inary	Prelim-inary	Final	Final minus prelim-inary
Gross domestic product (GDP) [1]	**2.2**	**2.0**	**–0.2**	**2.2**	**2.0**	**–0.2**
Personal consumption expenditures	**2.9**	**2.8**	**–0.1**	**1.99**	**1.96**	**–0.03**
Durable goods	6.0	6.4	0.4	0.47	0.50	0.03
Nondurable goods	1.1	1.5	0.4	0.23	0.32	0.09
Services	3.1	2.8	–0.3	1.29	1.14	–0.15
Gross private domestic investment	**0.0**	**–0.8**	**–0.8**	**0.01**	**–0.13**	**–0.14**
Fixed investment	–0.9	–1.2	–0.3	–0.15	–0.19	–0.04
Nonresidential	10.0	10.0	0.0	1.01	1.01	0.00
Structures	16.7	15.7	–1.0	0.49	0.46	–0.03
Equipment and software	7.2	7.7	0.5	0.52	0.55	0.03
Residential	–18.0	–18.7	–0.7	–1.16	–1.20	–0.04
Change in private inventories	....	....	....	0.16	0.06	–0.10
Net exports of goods and services	....	....	....	**–0.21**	**–0.19**	**0.02**
Exports	6.3	6.8	0.5	0.68	0.73	0.05
Goods	9.4	9.4	0.0	0.71	0.71	0.00
Services	–1.0	0.8	1.8	–0.03	0.03	0.06
Imports	5.3	5.6	0.3	–0.89	–0.93	–0.04
Goods	6.9	7.1	0.2	–0.96	–1.00	–0.04
Services	–2.7	–2.6	0.1	0.07	0.07	0.00
Government consumption expenditures and gross investment	**2.2**	**1.7**	**–0.5**	**0.42**	**0.32**	**–0.10**
Federal	1.5	1.3	–0.2	0.10	0.09	–0.01
National defense	–1.1	–1.2	–0.1	–0.05	–0.06	–0.01
Nondefense	6.8	6.5	–0.3	0.15	0.15	0.00
State and local	2.6	1.9	–0.7	0.32	0.23	–0.09
Addenda:						
Final sales of domestic product	2.1	1.9	–0.2	2.06	1.90	–0.16
Gross domestic purchases price index	2.1	2.2	0.1	....	....	....
GDP price index	1.8	1.9	0.1	....	....	....

1. The estimates of GDP under the contribution columns are also percent changes.

The final estimate of a 2.0-percent increase in real GDP growth is 0.2 percentage point less than the preliminary estimate. The revised growth rate reflects a downward revision to consumer spending for services, which contributed 0.15 percentage point less to GDP growth than previously estimated. For 1978–2005, the revisions to GDP growth, without regard to sign, averaged 0.3 percentage point from the preliminary to the final estimates.

The downward revision to consumer spending for services primarily reflected revisions to medical care services, specifically hospitals and nursing homes.

Inventory investment was also revised down, reflecting revisions to wholesale trade and manufacturing.

State and local government spending was revised down, primarily reflecting a revision to structures investment.

Source Data for the Final Estimates

The final estimates of gross domestic product for the third quarter of 2006 incorporated the following source data.

Personal consumption expenditures: Retail sales for August and September (revised). Quarterly services survey for the third quarter (new).

Nonresidential fixed investment: Construction put in place for August and September (revised).

Residential fixed investment: Construction put in place for August and September (revised).

Change in private inventories: Manufacturers' and trade inventories for September (revised).

Exports and imports of goods and services: International transactions accounts data for the second and third quarters (revised) and goods data for September (revised).

Government consumption expenditures and gross investment: State and local government construction put in place for August and September (revised).

GDP prices: Export and import prices for July, August, and September (revised), unit value index for petroleum imports for June (revised), and prices of single-family houses under construction for the third quarter (revised).

Corporate Profits

Table 3. Corporate Profits

[Seasonally adjusted]

	Billions of dollars (annual rate)					Percent change from preceding quarter (quarterly rate)			
	Level	Change from preceding quarter							
	2006	2005	2006			2005	2006		
	III	IV	I	II	III	IV	I	II	III
Current production measures:									
Corporate profits	1,653.3	127.2	175.6	22.7	61.5	10.0	12.6	1.4	3.9
Domestic industries	1,418.7	154.3	145.8	8.9	66.8	14.8	12.2	0.7	4.9
Financial	474.8	94.7	51.4	41.7	–9.1	32.0	13.1	9.4	–1.9
Nonfinancial	943.9	59.6	94.5	–32.8	75.8	8.0	11.7	–3.6	8.7
Rest of the world	234.6	–27.1	29.8	13.8	–5.3	–12.1	15.2	6.1	–2.2
Receipts from the rest of the world	408.9	16.6	15.7	25.7	6.9	4.8	4.4	6.8	1.7
Less: Payments to the rest of the world	174.2	43.7	–14.0	11.9	12.1	36.3	–8.5	7.9	7.5
Less: Taxes on corporate income	490.6	45.7	32.3	19.2	14.5	12.1	7.6	4.2	3.0
Equals: Profits after tax	1,162.7	81.4	143.2	3.6	47.0	9.2	14.8	0.3	4.2
Net dividends	650.4	17.0	14.7	15.4	19.3	2.9	2.5	2.5	3.1
Undistributed profits from current production	512.4	64.4	128.5	–11.8	27.8	21.2	34.9	–2.4	5.7
Net cash flow	1,380.5	–6.8	125.3	1.1	30.2	–0.5	10.2	0.1	2.2

Note. Levels of these and other profits series are shown in NIPA tables 1.12, 1.14, 1.15, and 6.16D.

Corporate profits from current production increased \$61.5 billion, or 3.9 percent at a quarterly rate, after increasing \$22.7 billion, or 1.4 percent.

Profits of financial corporations decreased \$9.1 billion, or 1.9 percent, following an increase of \$41.7 billion, or 9.4 percent, in the second quarter.

Profits of nonfinancial corporations increased \$75.8 billion, or 8.7 percent, after decreasing \$32.8 billion, or 3.6 percent.

Taxes on corporate income increased \$14.5 billion, or 3.0 percent.

After-tax profits increased \$47.0 billion, or 4.2 percent.

Undistributed corporate profits (a measure of net saving that equals after-tax profits less dividends) increased \$27.8 billion, or 5.7 percent.

Net cash flow with inventory valuation and capital consumption adjustments (a profits-related measure of internally generated funds available for investment) increased \$30.2 billion, or 2.2 percent.

Corporate Profits by Industry

Table 4. Corporate Profits by Industry

[Seasonally adjusted]

	Billions of dollars (annual rate)					Percent change from preceding quarter (quarterly rate)			
	Level	Change from preceding quarter							
	2006	2005	2006			2005	2006		
	III	IV	I	II	III	IV	I	II	III
Industry profits:									
Profits with IVA	1,815.8	114.2	158.6	34.9	63.2	7.9	10.2	2.0	3.6
Domestic industries	1,581.1	141.3	128.8	21.1	68.4	11.6	9.5	1.4	4.5
Financial	500.1	95.9	50.6	44.3	–8.1	30.2	12.2	9.5	–1.6
Nonfinancial	1,081.0	45.3	78.3	–23.2	76.5	5.0	8.2	–2.3	7.6
Utilities	52.8	15.9	1.4	7.1	6.0	71.4	3.7	17.7	12.8
Manufacturing	331.9	–1.8	41.8	–10.8	42.0	–0.7	16.1	–3.6	14.5
Wholesale trade	125.1	11.8	1.3	–8.9	26.8	12.5	1.1	–8.3	27.2
Retail trade	131.3	13.2	–6.1	–1.8	10.1	11.3	–4.7	–1.4	8.3
Transportation and warehousing	39.6	–4.1	8.3	11.3	1.0	–17.8	43.4	41.4	2.7
Information	83.3	5.8	6.2	–3.9	–2.6	7.5	7.4	–4.4	–3.0
Other nonfinancial	317.1	4.5	25.5	–16.2	–6.8	1.4	8.1	–4.7	–2.1
Rest of the world	234.6	–27.1	29.8	13.8	–5.3	–12.1	15.2	6.1	–2.2
Addenda:									
Profits before tax (without IVA and CCAdj)	1,854.0	122.5	142.3	70.9	42.5	8.3	8.9	4.1	2.3
Profits after tax (without IVA and CCAdj)	1,363.4	76.8	110.0	51.7	28.0	7.0	9.4	4.0	2.1
IVA	–38.2	–8.3	16.3	–36.0	20.7	....	....	....	....
CCAdj	–162.4	13.0	17.0	–12.2	–1.6	....	....	....	....

NOTE. Levels of these and other profits series are shown in NIPA tables 1.12, 1.14, 1.15, and 6.16D.
IVA Inventory valuation adjustment CCAdj Capital consumption adjustment

Industry profits with inventory valuation adjustment increased $63.2 billion, or 3.6 percent at a quarterly rate. This increase is larger than the increase in profits from current production ($61.5 billion) because it excludes the capital consumption adjustment, which decreased $1.6 billion.

Profits of domestic financial industries turned down, decreasing $8.1 billion, or 1.6 percent.

Profits of domestic nonfinancial industries turned up, increasing $76.5 billion, or 7.6 percent.

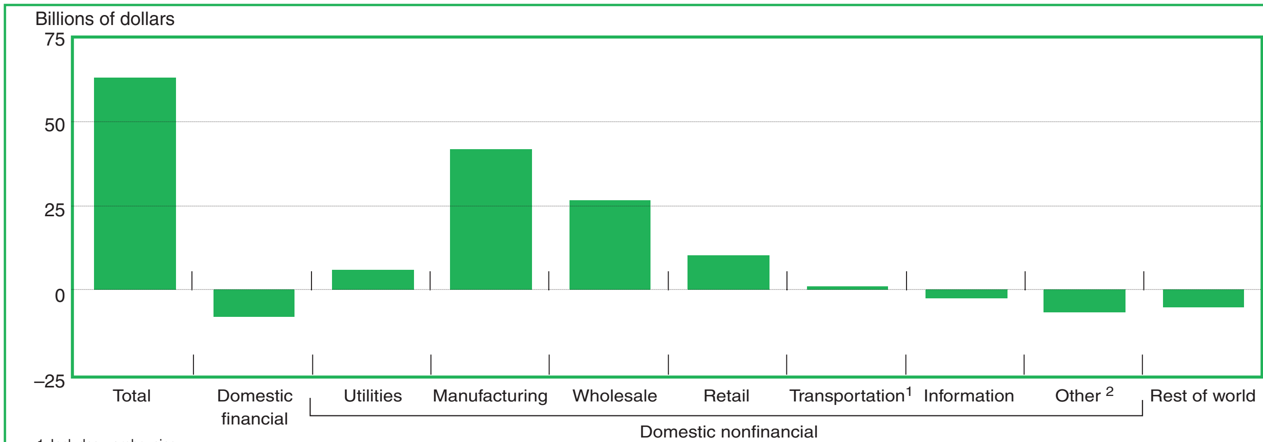
Profits of manufacturing industries turned up, increasing $42.0 billion, or 14.5 percent, reflecting an upturn in durable-goods manufacturing.

Profits of wholesale trade industries turned up, increasing $26.8 billion, or 27.2 percent.

Profits of retail trade industries turned up, increasing $10.1 billion, or 8.3 percent.

Profits from the rest of the world turned down, decreasing $5.3 billion, or 2.2 percent.

Chart 2. Corporate Profits With Inventory Valuation Adjustment: Change From the Preceding Quarter, 2006:III



1. Includes warehousing.
2. "Other" nonfinancial corporations include the agriculture, mining, construction, and services industries.
NOTE. Based on seasonally adjusted estimates.

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Corporate Profits by Industry

Industry profits are corporate profits by industry with inventory valuation adjustment (IVA). The IVA removes the effect of prices on inventories. The IVA is the difference between the cost of inventory withdrawals at acquisition cost and replacement cost. Ideally, BEA would also add the capital consumption adjustment (CCAdj) for each industry. However, estimates of the CCAdj are only available for two broad categories: Total financial industries and total nonfinancial industries. For more information about BEA's methodology, see "Corporate Profits: Profits Before Tax, Profits Tax Liability, and Dividends" at <www.bea.gov/bea/mp_national.htm>.

Corporate Profits and the Economy

Corporate profits gauge the general strength of the business sector. This widely followed statistic provides, among other things, an indication of future capital investment, a means to measure rates of return on investment, and a barometer that gauges the effect of policy changes on corporations.

Corporate profits in the national income and product accounts (NIPAs) measure profits earned by corporations from current production only. They do not include profits earned by corporations in other ways, such as profits associated with means of financing. The primary source data are data from the Internal Revenue Service. BEA also uses profits data based on company financial reports when tax-based data are not available.

BEA reports corporate profits on a current-dollar, seasonally adjusted, annualized basis. To ensure consistency with the NIPAs, BEA makes two adjustments. First, to remove the effects of price changes on inventories valued at historical cost and of tax accounting for inventory withdrawals, BEA adds an inventory valuation adjustment that values inventories at current cost. Second, to remove the effects of tax accounting rules on measured depreciation, BEA adds a capital consumption adjustment (CCAdj). CCAdj is defined as the difference between consumption of fixed capital (the decline in the value of assets due to wear and tear, obsolescence, accidental damage, and aging) and tax return depreciation.

Unlike other NIPA measures, changes in quarterly profits are reported at quarterly rates, not annual rates. Percent changes are reported in two ways: The change from the previous quarter and the change from the year-ago quarter.

Quarter-to-quarter changes in profits are relatively volatile, and comparisons to year-ago quarters can be skewed by nonrecurring events. For example, profits in the third quarter of 2006 were 31 percent higher than in the third quarter of 2005; however, profits in the third quarter of 2005 were restrained by Hurricanes Katrina and Rita.

In the current economic expansion, profit growth has been strong:

- **Profits as a share of GDP.** Profits as a share of current-dollar GDP clearly shows the growth in profits over the current expansion. Profits as a share of GDP was 12.4 percent in the third quarter of 2006, up 5.4 percentage points from a trough in the third quarter of 2001 (chart 1).
- **Cash flow to fixed investment.** The ratio of cash flow to current-dollar nonresidential fixed investment is considered an indicator of businesses' ability to finance investment internally. The ratio has steadily increased to 0.97 in the third quarter of 2006 from a trough of 0.69 in the third quarter of 2000.
- **Profit per unit of real gross value added.** BEA estimates the price, costs, and residual profit per unit of real gross value added in the nonfinancial corporate sector (NIPA table 1.15). These data indicate how price changes flow to profits through unit labor and nonlabor costs (chart 2). Since 2000, unit prices have risen 13.4 percent, from just under $1 per unit to $1.12. Unit labor costs have risen mildly, about 5 cents, and unit nonlabor costs have been relatively flat, reflecting lower interest rate costs. Since 2003, profit per unit of sales has grown from about 10 cents, and an 8-percent share of the per unit price, to 15 cents and a 14-percent share.
- **Financial and nonfinancial corporate profits.** BEA reports profits for domestic financial and nonfinancial industries. Profit levels in the nonfinancial industries have nearly tripled since the previous low in the fourth quarter of 2001. Profits in the financial industries have turned up from levels affected by the hurricanes in the second and third quarters of 2005.

Chart 1. Profits as a Share of GDP

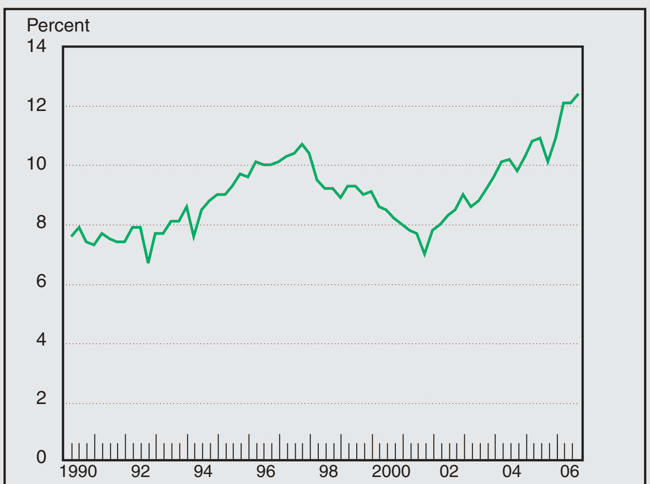

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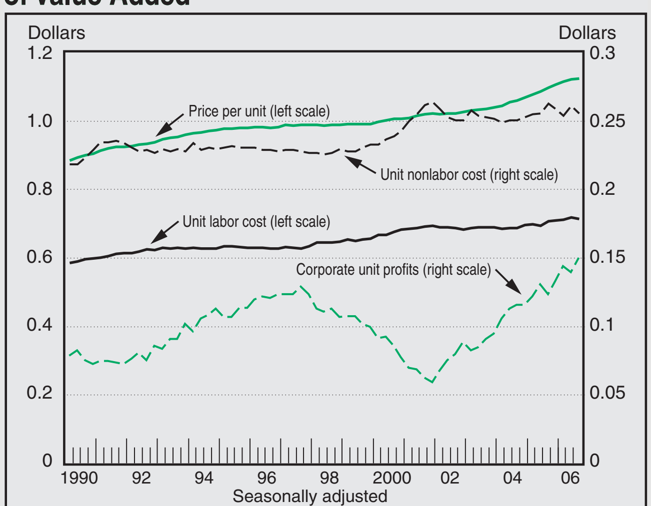
Chart 2. Price, Costs, and Profit Per Unit of Value Added



NOTE. Value added refers to gross value added of nonfinancial domestic corporate business.
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