

GDP and the Economy

Final Estimates for the Fourth Quarter of 2005

REAL gross domestic product (GDP) increased 1.7 percent in the fourth quarter of 2005 after increasing 4.1 percent in the third quarter, according to the “final” estimates of the national income and product accounts (NIPAs) (table 1 and chart 1).¹ The final estimate of real GDP growth was 0.1 percentage point more than the “preliminary” estimate released in February; it reflected an upward revision to inventory investment (page 3).

The deceleration in real GDP growth reflected a deceleration in consumer spending, an acceleration in imports, a downturn in Federal Government spending, and decelerations in equipment and software and in residential fixed investment.

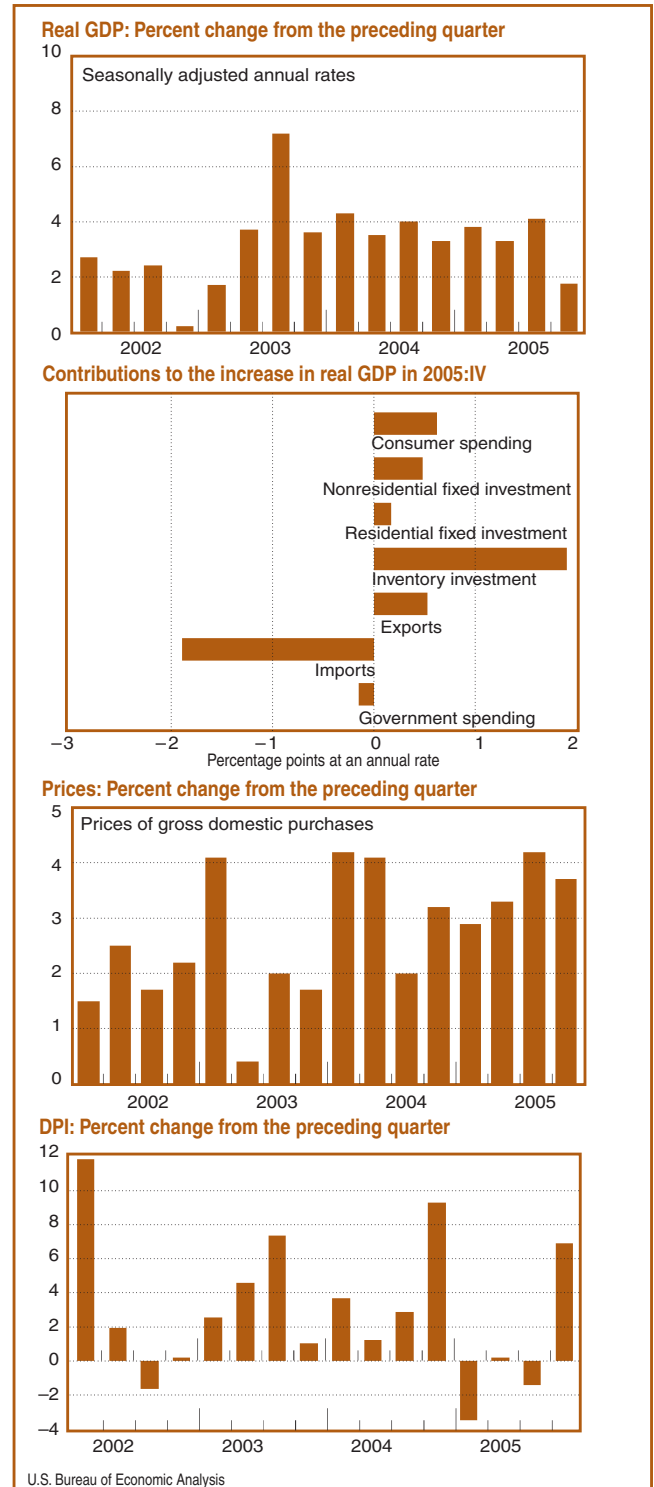
- Corporate profits increased \$185.8 billion (14.4 percent at a quarterly rate) in the fourth quarter after decreasing \$54.4 billion (4.0 percent) in the third quarter (page 4).
- Prices of goods and services bought by U.S. residents increased 3.7 percent, 0.1 percentage point more than the preliminary estimate. In the third quarter, prices increased 4.2 percent. Energy prices decelerated, and food prices accelerated. Excluding food and energy, gross domestic purchases prices increased 3.2 percent after increasing 2.5 percent.
- Real disposable personal income (DPI) increased 6.7 percent, 0.4 percentage point less than in the preliminary estimate. Real DPI decreased 1.4 percent in the third quarter.
- Real gross national product (GNP) increased 0.7 percent after increasing 4.4 percent.² The fourth-quarter increase is 1.0 percentage point less than the increase in real GDP, reflecting a decrease in net receipts of income from the rest of the world.

1. Three sequential GDP estimates for each quarter are prepared: Advance, preliminary, and final estimates. Each incorporates more comprehensive and improved source data. Quarterly estimates in the NIPAs are expressed at seasonally adjusted annual rates, unless otherwise specified. Quarter-to-quarter dollar changes are differences between these published estimates. More information can be found on BEA’s Web site at <www.bea.gov/bea/about/infoqual.htm> and at <www.bea.gov/bea/faq/national/gdp_accuracy.htm>.

2. GNP is a measure of the goods and services produced by labor and property supplied by U.S. residents, regardless of their location. In contrast, GDP is a measure of the goods and services produced by labor and property in the United States, regardless of nationality. GNP equals GDP *plus* income receipts from the rest of the world *minus* income payments to the rest of the world.

Christopher Swann prepared this article.

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



Real GDP Overview

Table 1. Real Gross Domestic Product and Components

[Seasonally adjusted at annual rates]

	Change from preceding period (percent)				Contribution to percent change in real GDP (percentage points)				Share of current-dollar GDP (percent)
	2005				2005				2005
	I	II	III	IV	I	II	III	IV	IV
Gross domestic product.....	3.8	3.3	4.1	1.7	3.8	3.3	4.1	1.7	100.0
Personal consumption expenditures.....	3.5	3.4	4.1	0.9	2.44	2.35	2.85	0.62	69.9
Durable goods.....	2.6	7.9	9.3	-16.6	0.22	0.64	0.76	-1.47	7.8
Nondurable goods.....	5.3	3.6	3.5	5.0	1.07	0.74	0.73	1.02	20.7
Services.....	2.8	2.3	3.3	2.6	1.15	0.97	1.36	1.08	41.4
Gross private domestic investment.....	8.6	-3.7	5.3	16.1	1.42	-0.63	0.87	2.54	17.3
Fixed investment.....	7.0	9.5	8.0	3.9	1.12	1.51	1.31	0.65	17.0
Nonresidential.....	5.7	8.8	8.5	4.5	0.58	0.90	0.88	0.48	10.8
Structures.....	-2.0	2.7	2.2	3.1	-0.05	0.07	0.06	0.09	2.8
Equipment and software.....	8.3	10.9	10.6	5.0	0.64	0.83	0.82	0.39	8.0
Residential.....	9.5	10.8	7.3	2.8	0.54	0.62	0.43	0.17	6.2
Change in private inventories.....					0.29	-2.14	-0.43	1.89	0.3
Net exports of goods and services.....					-0.40	1.11	-0.12	-1.36	-6.2
Exports.....	7.5	10.7	2.5	5.1	0.74	1.07	0.26	0.52	10.5
Goods.....	5.3	16.0	3.2	8.0	0.37	1.08	0.23	0.56	7.3
Services.....	12.5	-0.4	1.0	-1.4	0.37	-0.01	0.03	-0.05	3.2
Imports.....	7.4	-0.3	2.4	12.1	-1.14	0.04	-0.38	-1.88	16.7
Goods.....	8.2	-1.1	3.5	13.5	-1.05	0.15	-0.46	-1.76	14.1
Services.....	3.7	4.4	-3.2	4.8	-0.10	-0.11	0.09	-0.12	2.6
Government consumption expenditures and gross investment.....	1.9	2.5	2.9	-0.8	0.35	0.47	0.54	-0.15	19.0
Federal.....	2.4	2.4	7.4	-2.6	0.17	0.17	0.52	-0.18	7.0
National defense.....	3.0	3.7	10.0	-8.9	0.14	0.17	0.46	-0.44	4.6
Nondefense.....	1.1	-0.2	2.4	11.7	0.03	-0.01	0.06	0.26	2.3
State and local.....	1.6	2.6	0.2	0.2	0.19	0.31	0.03	0.03	12.0
Addenda:									
Final sales of domestic product.....	3.5	5.6	4.6	-0.2	3.51	5.45	4.58	-0.24	
Gross domestic purchases price index.....	2.9	3.3	4.2	3.7					
GDP price index.....	3.1	2.6	3.3	3.5					

NOTE: Percent changes are from NIPA table 1.1.1, and contributions to percent change are from NIPA table 1.1.2. Shares are from NIPA table 1.1.10.

Growth in consumer spending fell to 0.9 percent from 4.1 percent, contributing 0.62 percentage point to real GDP compared with 2.85 percentage points. Spending for durable goods, mainly motor vehicles and parts, turned down. Spending for nondurable goods accelerated, reflecting an acceleration in spending for clothing and shoes and an upturn in spending for gasoline, fuel oil, and other energy goods.

Fixed investment decelerated. Investment in equipment and software decelerated, reflecting downturns in investment in transportation equipment and in "other" information processing equipment.

Inventory investment turned up and contributed 1.89 percentage points to real GDP growth after subtracting 0.43 percentage point. Inventory investment of retail automobile dealers, other retail stores, and nondurable-goods manufacturing turned up.

Goods exports accelerated partly because of an acceleration in nonautomotive capital goods, which in turn reflected an acceleration in "other" nonautomotive capital goods and an upturn in civilian aircraft, engines, and parts.

Real imports accelerated, subtracting 1.88 percentage points from GDP growth after subtracting 0.38 percentage point. Goods imports accelerated; petroleum and products, nonpetroleum industrial supplies, and nonautomotive consumer goods all turned up.

Federal Government spending decreased 2.6 percent after increasing 7.4 percent, reflecting a downturn in defense spending. Nondefense spending accelerated.

Real final sales of domestic product—real GDP less the change in private inventories—turned down.

Measuring Saving

The gross saving rate (saving from all sources as a percentage of gross national income) was 13.6 percent in the fourth quarter, unchanged from the third quarter.

Net saving, which excludes the consumption of fixed capital, is a measure of the saving that is available for augmenting the stock of fixed assets. The net saving rate was 1.7 percent in the fourth quarter, compared with -1.2 percent in the third quarter. The negative saving rate in the third quarter reflected the destruction of assets from the hurricanes.

Personal saving is defined as disposable personal income less consumer spending, interest paid by persons, and per-

sonal transfer payments to the rest of the world. The personal saving rate, which measures personal saving as a percentage of disposable personal income, was -0.2 percent in the fourth quarter. The rate has been negative for the last three quarters and has been declining steadily since the 1980s.

For more information, see Marshall Reinsdorf, "Saving, Wealth, Investment, and the Current-Account Deficit," SURVEY OF CURRENT BUSINESS 85 (April 2005): 3. Compare personal saving in the NIPAs with personal saving in the Federal Reserve Board's flow of funds accounts at <www.bea.gov/bea/dn/nipaweb/Nipa-Frb.asp>.

Revisions to GDP

Table 2. Final and Preliminary Estimates for the Fourth Quarter of 2005
 [Seasonally adjusted at annual rates]

	Percent change from preceding quarter			Contribution to percent change in real GDP		
	Final	Preliminary	Final minus preliminary	Final	Preliminary	Final minus preliminary
Gross domestic product (GDP)	1.7	1.6	0.1	1.7	1.6	0.1
Personal consumption expenditures	0.9	1.2	-0.3	0.62	0.81	-0.19
Durable goods.....	-16.6	-16.6	0.0	-1.47	-1.47	0.00
Nondurable goods.....	5.0	5.1	-0.1	1.02	1.04	-0.02
Services.....	2.6	3.0	-0.4	1.08	1.24	-0.16
Gross private domestic investment	16.1	14.8	1.3	2.54	2.35	0.19
Fixed investment.....	3.9	4.4	-0.5	0.65	0.73	-0.08
Nonresidential.....	4.5	5.4	-0.9	0.48	0.57	-0.09
Structures.....	3.1	3.3	-0.2	0.09	0.09	0.00
Equipment and software.....	5.0	6.2	-1.2	0.39	0.48	-0.09
Residential.....	2.8	2.6	0.2	0.17	0.16	0.01
Change in private inventories.....	.....	.....	.....	1.89	1.62	0.27
Net exports of goods and services.....	.....	.....	.....	-1.36	-1.40	0.04
Exports.....	5.1	5.7	-0.6	0.52	0.58	-0.06
Goods.....	8.0	7.7	0.3	0.56	0.54	0.02
Services.....	-1.4	1.2	-2.6	-0.05	0.04	-0.09
Imports.....	12.1	12.8	-0.7	-1.88	-1.98	0.10
Goods.....	13.5	14.0	-0.5	-1.76	-1.82	0.06
Services.....	4.8	6.3	-1.5	-0.12	-0.16	0.04
Government consumption expenditures and gross investment	-0.8	-0.7	-0.1	-0.15	-0.13	-0.02
Federal.....	-2.6	-2.6	0.0	-0.18	-0.18	0.00
National defense.....	-8.9	-9.0	0.1	-0.44	-0.44	0.00
Nondefense.....	11.7	11.9	-0.2	0.26	0.26	0.00
State and local.....	0.2	0.4	-0.2	0.03	0.05	-0.02
Addenda:						
Final sales of domestic product.....	-0.2	0.0	-0.2	-0.24	0.01	-0.25
Gross domestic purchases price index.....	3.7	3.6	0.1	.....	.....	.....
GDP price index.....	3.5	3.3	0.2	.....	.....	.....

Consumer spending on services was revised down, reflecting newly available Energy Information Administration data on electricity sales for December and newly available Securities and Exchange Commission data on brokerage commissions for the fourth quarter.

Inventory investment was revised up, reflecting revised Census Bureau data for December on manufacturing and trade inventories and newly available Energy Information Administration data on utility inventories for November and December.

Source Data for the Final Estimates

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

Personal consumption expenditures: Retail sales for December (revised). Electricity and natural gas sales to residential consumers for December (new).

Nonresidential fixed investment: Construction put-in-place data for November and December (revised) and manufacturers' shipments of machinery and equipment for December (revised).

Residential investment: Construction put-in-place data for November and December (revised).

Change in private inventories: Manufacturers and trade inventories for December (revised). Coal and petroleum stocks of electric utilities for November (new) and net addition of natural gas for December (new).

Exports and imports of goods and services: International transactions accounts for October through December (revised).

Government consumption expenditures and gross investment: State and local government construction put-in-place data for November and December (revised).

Wages, salaries, and compensation: Employment, average hourly earnings, and average weekly hours for December (revised) and data on employer costs for employee compensation for the fourth quarter (new).

GDP prices: Export and import prices for October through December (revised), unit value index for petroleum imports for October through December (revised), and prices of single-family houses under construction for the fourth 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							
	2005	2005				2005			
	IV	I	II	III	IV	I	II	III	IV
Current production measures:									
Corporate profits	1,478.9	68.7	59.3	-54.4	185.8	5.6	4.6	-4.0	14.4
Domestic industries	1,270.3	53.9	55.5	-80.4	200.4	5.2	5.1	-7.0	18.7
Financial	383.7	36.0	-26.9	-71.9	104.9	10.6	-7.1	-20.5	37.6
Nonfinancial	886.6	17.8	82.5	-8.5	95.5	2.5	11.5	-1.1	12.1
Rest of the world	208.6	14.9	3.7	25.9	-14.5	8.3	1.9	13.1	-6.5
Receipts from the rest of the world	356.6	-19.1	14.7	10.1	18.3	-5.7	4.7	3.1	5.4
Less: Payments to the rest of the world	148.0	-33.9	10.9	-15.9	32.9	-22.0	9.1	-12.1	28.5
Less: Taxes on corporate income	417.1	69.6	9.9	-12.2	56.8	23.7	2.7	-3.3	15.8
Equals: Profits after tax	1,061.8	-0.8	49.4	-42.2	129.0	-0.1	5.3	-4.3	13.8
Net dividends	535.4	-94.4	11.4	13.8	15.3	-16.0	2.3	2.7	2.9
Undistributed profits from current production	526.4	93.5	38.0	-56.1	113.8	27.7	8.8	-12.0	27.6
Net cash flow	1,368.0	95.4	41.7	44.0	43.1	8.3	3.4	3.4	3.3

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

Corporate profits increased 14.4 percent in the fourth quarter after decreasing 4.0 percent in the third quarter. Fourth-quarter profits were reduced by \$22.9 billion because of Hurricane Wilma. Third-quarter profits were reduced by \$165.3 billion because of Hurricanes Katrina and Rita. BEA adjustments were based on the net benefits paid by domestic insurance companies and the uninsured losses of corporate property.

Profits of financial corporations increased 37.6 percent after decreasing 20.5 percent.

Profits of nonfinancial corporations increased 12.1 percent after decreasing 1.1 percent.

Taxes on corporate income increased 15.8 percent after decreasing 3.3 percent.

After-tax profits increased 13.8 percent after decreasing 4.3 percent.

Undistributed corporate profits (a measure of net saving that equals after-tax profits less dividends) increased 27.6 percent after decreasing 12.0 percent.

Net cash flow from current production, a profits-related measure of internally generated funds available for investment, increased \$43.1 billion (3.3 percent) in the fourth quarter after increasing \$44.0 billion (3.4 percent) in the third quarter.

Measuring Corporate Profits

Corporate profits is a widely followed economic indicator used to gauge corporate health, assess investment conditions, and analyze the effect on corporations of economic policies and conditions. In addition, corporate profits is an important component in key measures of income.

BEA's measure of corporate profits aims to capture the income earned by corporations from current production in a manner that is fully consistent with the national income and product accounts (NIPAs). The measure is defined as receipts arising from current production less associated expenses. Receipts exclude income in the form of dividends and capital gains, and expenses exclude bad debts, natural resource depletion, and capital losses.

Because direct estimates of NIPA-consistent corporate profits are unavailable, BEA derives these estimates. It does this in three steps.

First, BEA measures profits before taxes to reflect corporate income regardless of any redistributions of income through taxes. This measure is partly based on tax return

information from the Internal Revenue Service; BEA uses tax accounting measures as a source of information on profits for two reasons: They are based on well-specified accounting definitions, and they are comprehensive, covering all incorporated businesses—publicly traded and privately held—in all industries. BEA also uses other sources of information to estimate pretax profits, including information from the Census Bureau.

Second, 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 (IVA) that values inventories at current cost.

Third, to remove the effects of tax accounting on 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 the stock of assets due to wear and tear, obsolescence, accidental damage, and aging) and capital consumption allowances (tax return depreciation).

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							
	2005	2005				2005			
	IV	I	II	III	IV	I	II	III	IV
Industry profits:									
Profits IVA	1,529.7	259.5	54.1	-28.2	164.6	24.0	4.0	-2.0	12.1
Domestic industries.....	1321.1	244.6	50.4	-54.1	179.1	27.2	4.4	-4.5	15.7
Financial	382.7	57.8	-27.7	-70.8	104.0	18.1	-7.4	-20.3	37.3
Nonfinancial.....	938.3	186.8	78.1	16.7	75.0	32.1	10.2	2.0	8.7
Utilities.....	39.6	9.6	2.7	-6.7	19.9	68.3	11.4	-25.5	100.6
Manufacturing	238.3	15.5	34.5	13.9	19.7	10.0	20.3	6.8	9.0
Wholesale trade	100.6	14.5	16.7	-2.7	5.2	21.7	20.5	-2.7	5.4
Retail trade.....	130.4	16.9	4.5	7.8	13.5	19.4	4.2	7.2	11.5
Transportation and warehousing.....	29.1	21.2	5.0	5.0	-3.8	.....	.....	.....	.....
Information	54.0	25.7	6.8	-3.3	3.8	.....	.....	.....	.....
Other nonfinancial.....	346.4	83.3	8.0	2.7	16.8	35.4	2.5	0.8	5.1
Rest of the world	208.6	14.9	3.7	25.9	-14.5	8.3	1.9	13.1	-6.5
Addenda:									
Profits before tax (without IVA and CCAdj).....	1,570.1	254.2	33.9	-19.6	177.5	22.6	2.5	-1.4	12.7
Profits after tax (without IVA and CCAdj).....	1153.0	184.6	24.0	-7.4	120.7	22.2	2.4	-0.7	11.7
IVA.....	-40.4	5.3	20.2	-8.6	-12.9	.....	.....	.....	.....
CCAdj.....	-50.7	190.8	5.2	-26.3	21.4	.....	.....	.....	.....

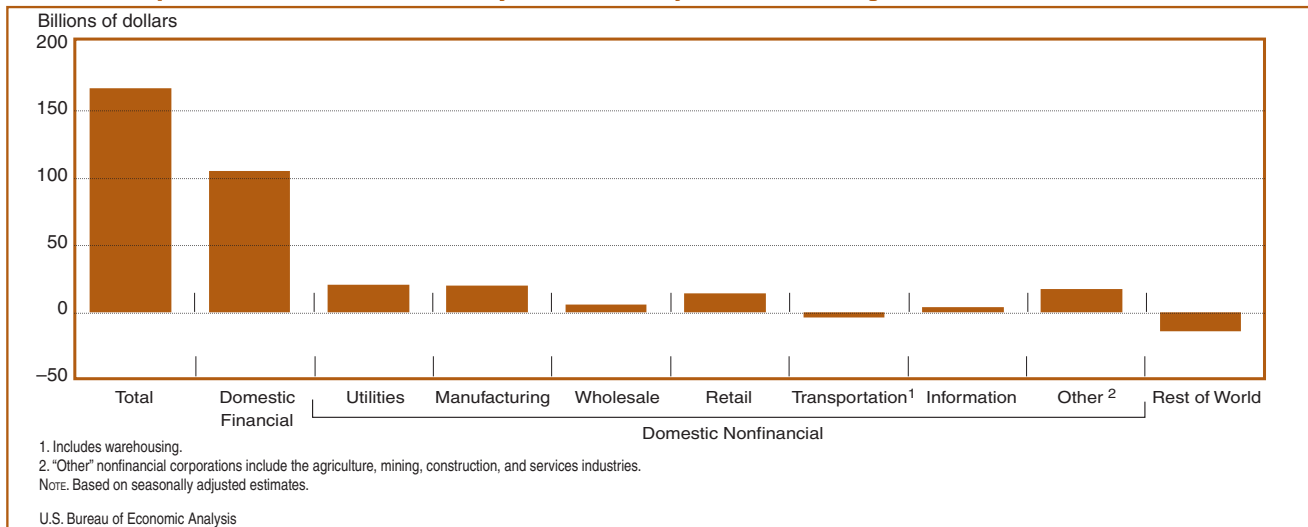
Industry profits with IVA increased \$164.6 billion after decreasing \$28.2 billion (chart 2). The increase in industry profits is smaller than the increase in profits from current production; profits from current production include the estimates of CCAdj, which increased \$21.4 billion in the fourth quarter after decreasing \$26.3 billion in the third.

Profits for domestic financial industries increased \$104.0 billion after decreasing \$70.8 billion.

Profits for domestic nonfinancial corporate profits increased \$75.0 billion after increasing \$16.7 billion.

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

Chart 2. Corporate Profits With Inventory Valuation Adjustment: Change From 2005:III to 2005:IV



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 indus-

try. 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>.