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Economic Watch

US

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Economic Analysis

US
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Changing Dynamics in GDP Growth

A Look at Growth Contributions, New Classifications, and the Significance of GDP Data

- **Annual revisions to GDP data change past figures, not future outlook**
- **Intellectual property launch an important milestone in GDP accounting**
- **High expectations for nonresidential investment and exports post-2013**

Gross domestic product (GDP) is the primary measure of economic activity across the globe, accounting for both public and private investment and consumption. The indicator rests on the top of the list when it comes to important macroeconomic variables, yet it is often surprising how much emphasis is placed on the data. Quarterly GDP estimates are lagged at least three months, with the final report lagged six months, and by that point short-term economic data are already suggestive of whether or not activity is moving in a positive direction. Furthermore, the Bureau of Economic Analysis releases annual revisions to GDP data in the U.S. that often result in significant changes to the previously known figures. Various changes in the composition and classification of GDP over time seem to be much more indicative of economic growth than what we see on the surface. With this in mind, it is important to take a step back and reflect on the significance of GDP data and what it means for future economic analysis.

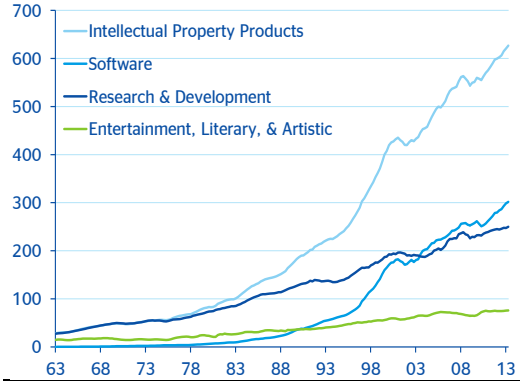
Annual Revisions and New Classifications

The BEA's growth estimates are re-examined to account for the changing economy. Recently, the BEA released its annual revisions to GDP data (dating back to 1947), along with a new classification for intellectual property products. The revisions appeared to be significant for some periods – the latest recession was somewhat less severe than previously estimated, while a strong upward revision to 1Q12 growth pushed the annual figure from 2.2% to 2.8% for 2012. At the same time, GDP growth for 1Q13 was revised down from its "final" estimate of 1.8% just a month before to a mere 1.1% on a QoQ SAAR basis. So, did these revisions really change the way we see economic activity during those times, and does the updated data significantly impact our views of the future? Despite these changes to the data, we have maintained our baseline GDP forecasts for 2013 and beyond (see our latest U.S. Outlook).

Chart 1
Real GDP Growth, Pre- & Post-Revisions (QoQ % Change, SAAR)

Source: BEA & BBVA Research

Chart 2
Intellectual Property Products (Real $Bn, SAAR)



Source: BEA & BBVA Research

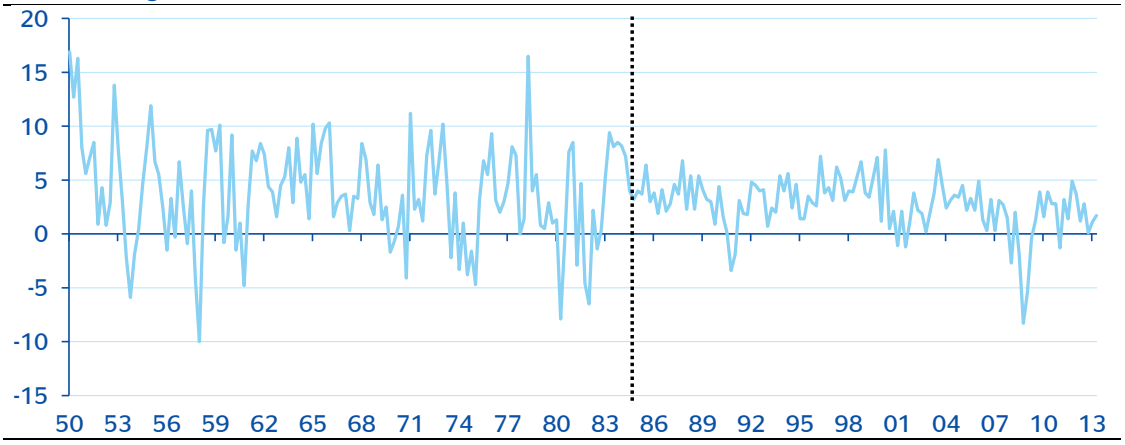
More telling, then, is the introduction of intellectual property as its own fixed investment contribution to GDP. This new classification includes software, research and development, and entertainment, literary, and artistic investments, creating a more modern relevance of the GDP measurement to the changing economic environment. Intellectual property has increasingly become a driving factor of economic activity in the U.S., whether it is related to software innovation, R&D, or the entertainment industry. The latter, in particular, is not quite up to par with the others in terms of investment volume, but it is surely an important sector to measure moving forward. Ultimately, this introduction of a new GDP classification shows that the U.S. is taking the first step in adapting to changes in society, and we expect that other countries will follow suit as the significance of intellectual property investment continues to rise.

Historical Trends and Contributions to Growth

There have been various measurement changes from the BEA throughout history when it comes to best estimating economic growth. Back in 1991, the BEA changed its reporting standards to feature GDP as the primary measure of U.S. output rather than the previously used gross national product (GNP) – the difference being that GDP includes only production taking place within the U.S., not U.S. activity abroad, and is therefore more consistent with short-term indicators such as employment.

Historical trends show that GDP growth has seen its fair share of adjustments, and it is interesting to look at the series dating back to 1950. Growth was a lot more volatile prior to the 1990s, ranging from extreme highs above 15% on a QoQ SAAR basis in the early 1950s to extreme lows near -10% later in the decade. Since the mid-1980s, however, growth has remained within a smaller band to the upside, peaking at just under 8% around the turn of this century.

Chart 3
Real GDP Growth
(QoQ % Change, SAAR)



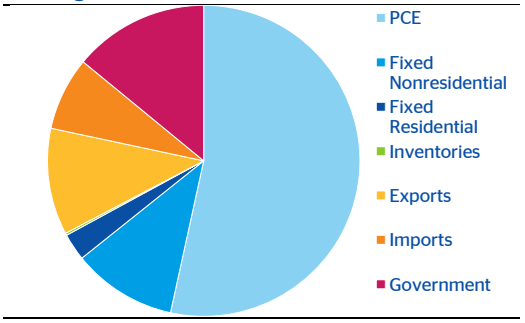
Source: BEA & BBVA Research

What happened to cause this change? This period is often referred to as the "great moderation", and the decline in volatility has been attributed to various factors including technological improvements (i.e. the internet), increased imports, and the end of high inflation rates in 1983. Whatever the reason may be, it is clear that the measurement of GDP has undergone some facelifts throughout history to account for a changing economic environment.

We see a similar story when looking at the specific contributions to growth. Contributions to GDP are always volatile quarter-quarter, but the trends are clear: in expansionary periods, personal consumption expenditures (PCE) have had the biggest contribution to real GDP growth. The share of PCE to total GDP has always dominated, rising from about 60% of total growth in the 1950s to almost 70% currently.

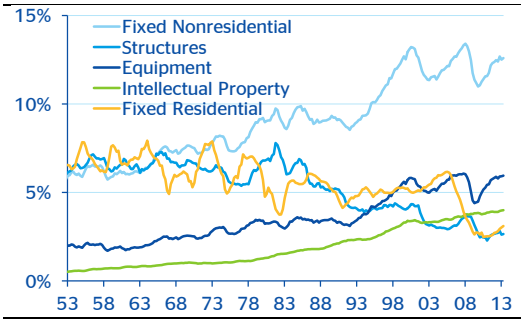
Over the next decade or so, we expect contributions to GDP to remain mostly consistent, though we do expect to see an increasing share of GDP for exports and fixed nonresidential investment (in large part due to the new accounting measure of intellectual property). In fact, we expect the share of exports as a percent of GDP to double throughout the next decade. The U.S. has brought a lot of manufacturing and other activities back from abroad, which should help reduce the dependence on imports for consumer-related goods. More importantly, continued energy exploration on U.S. soil will contribute to increased exports from the energy side. At the same time, we expect that the share of government consumption will continue to decline as fiscal austerity remains prominent.

Chart 4
Expected Shares of Real GDP, 2013-2017
(Average % of Real GDP)



Source: BEA & BBVA Research

Chart 5
Private Fixed Investment
(% of Real GDP)



Source: BEA & BBVA Research

Bottom Line: Ever-Changing GDP Measurements Boost Reflection of Economic Growth

GDP data has been held in the highest regards when it comes to economic analysis, but the estimates are not always the cream of the crop at face value. Many times it takes an in-depth analysis of the contributions and composition of GDP to get a better sense of true economic trends. Annual revisions to the data often change our perception of economic activity in the past, but not necessarily our outlook for future growth. More significant adjustments come when we see the BEA reclassifying data based on a changing economic environment, such as the introduction of a new investment category for intellectual property products. This variation in the measurement of GDP, among others, helps to support the indicator's reign as a comprehensive representation of economic growth.