Economic Research Department

BBVA

GDP Observatory

April 29, 2009

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1Q09 GDP Growth

- **GDP decreased at a slower rate than in 4Q09**
- **PCE's increase could indicate a bottom in the downward trend**
- **Investment and international trade present risks to recovery**

GDP in 1Q09 declined 6.1%, a slightly slower rate than the 6.3% drop in 4Q08, but still more than expected due to a surprisingly large adjustment in inventories. In contrast, PCE rebounded 2.2% following two consecutive quarterly declines. Even though both durable and non-durable goods bounced back, the increase in durable goods was the main driver due to a 20.5% jump in spending on motor vehicles after declining for six consecutive quarters. These results are a positive signal that the downward trend in PCE may have reached a bottom.

As expected, the decline in non-residential investment was sharper than in 4Q08. The steep 44.2% plunge in structures is noteworthy because it is the lowest decrease on record (1947). On top of the commercial sector, which has been leading the decline, the mining sector had a significant contribution. Equipment and software also fell sharply by 33.8%, the greatest rate since 1Q58. This result, however, was widely expected according to high frequency indicators such as industrial production of high tech goods, capital goods orders, etc. Overall, non-residential investment subtracted 4.68pp from GDP growth, the largest negative contribution on record.

Despite some stabilization in monthly indicators, residential investment decreased further by 38.0%, the highest rate since 3Q80, subtracting 1.4pp from GDP. The change in private inventories also subtracted 2.8pp.

Both exports and imports declined by 30.0% and 34.1% respectively, primarily due to falling demand for goods both at home and abroad. The sharp decrease in both components resulted in a positive contribution of net exports to GDP.

Lastly, government spending fell for the first time since 4Q05 due to lower spending on national defense (-6.4%). State and local government spending also dropped by 3.9%, which reflects the increasing stress on their finances due to the ongoing recession.

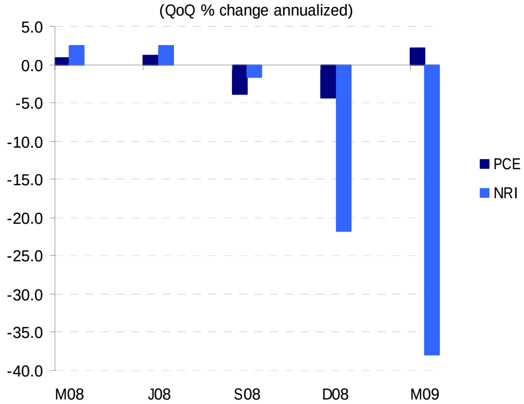
Bottom-line: The economic contraction in the first quarter came in below our expectations. The positive PCE results indicate that the worst could be over for consumer spending since the next quarters could be boosted by the fiscal stimulus package, low interest rates and further discounts on autos. Despite positive PCE readings, the outlook for investment and international trade remains gloomy and imposes downward risks to an eventual recovery. So far, monthly indicators have not shown signs of a rebound in the high-tech industry. Corporate profits are down and both domestic and external demand remains weak. These trends could exacerbate job losses and drag down GDP even further. Lastly, there is the risk that net exports could turn negative again as the economic recovery of the US's top trading partners is expected to happen later, which will drive down exports for an extended period.

1Q09 GDP Growth
Advance: -6.1%
Preliminary: May 29, 2009
Final: June 25, 2009

Gross Domestic Product (qoq annualized % change)

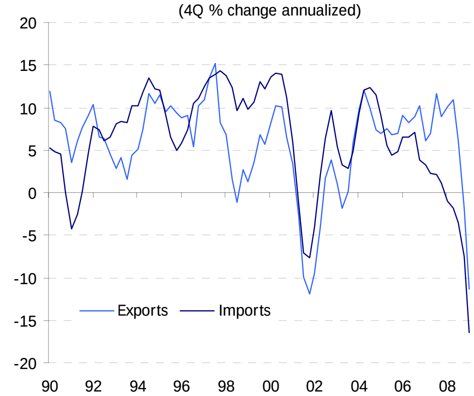
	Actual	Expected	Difference
Total	-6.1	-4.7	1.4
PCE	2.2	-1.4	-3.6
Non-resdidential Investment	-37.9	-24.5	13.4
Residential Investment	-33.8	-18.5	15.3
Exports	-30.0	-32.5	-2.5
Imports	-34.1	-22.9	11.2
Government Spending	-3.9	8.2	12.1

PCE and Non-Residential Investment
(QoQ % change annualized)



Source: BEA

Imports and Exports
(4Q % change annualized)



Source: BEA