

# Business Situation

## Advance Estimates for the Fourth Quarter of 2005 and for 2005

IN the fourth quarter of 2005, real gross domestic product (GDP) decelerated sharply, increasing 1.1 percent—3.0 percentage points less than in the third quarter. Inflation also decelerated (chart 1).<sup>1</sup> In 2005, real GDP increased 3.5 percent; real GDP had increased 4.2 percent in 2004 (table 1).<sup>2</sup> Inflation accelerated in 2005, but excluding food and energy, the pace was about the same as in 2004. (See “Real GDP for 2005.”)

### The Fourth Quarter of 2005

The advance estimates for the fourth quarter of 2005 show the following:

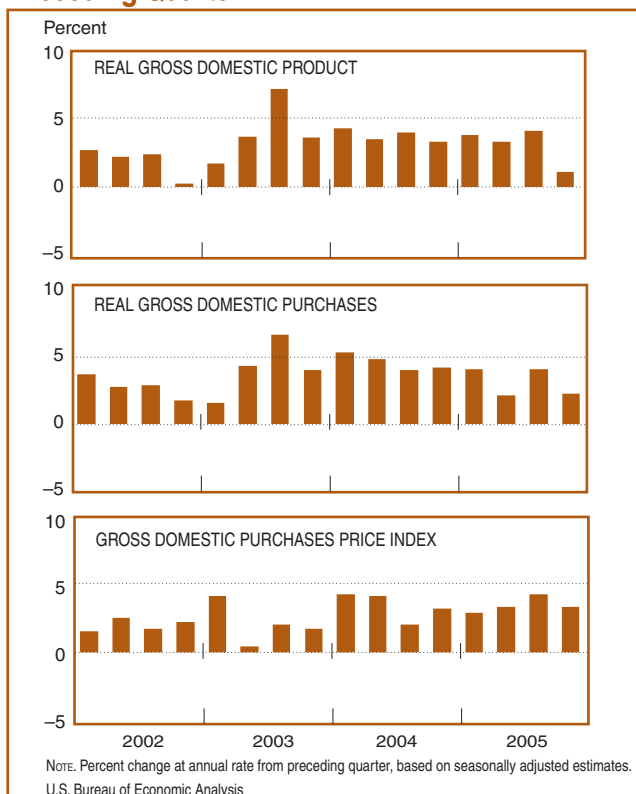
- Real GDP increased 1.1 percent after increasing 4.1 percent in the third quarter (table 1). The deceleration

1. Three sequential GDP estimates for each quarter are prepared—advance, preliminary, and final estimates. Each incorporates increasingly comprehensive and improved source data. Detailed information on BEA estimates, revisions, and accuracy can be found on BEA’s Web site at [www.bea.gov/bea/about/infoqual.htm](http://www.bea.gov/bea/about/infoqual.htm) and at [www.bea.gov/bea/faq/national/gdp\\_accuracy.htm](http://www.bea.gov/bea/faq/national/gdp_accuracy.htm). 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. Percent changes are calculated from unrounded data and annualized.

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

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**Chart 1. Selected Measures: Change From Preceding Quarter**



**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)
	2004	2005	2005				2004	2005	2005				
			I	II	III	IV			I	II	III	IV	
<b>Gross domestic product (GDP)</b> .....	<b>4.2</b>	<b>3.5</b>	<b>3.8</b>	<b>3.3</b>	<b>4.1</b>	<b>1.1</b>	<b>4.2</b>	<b>3.5</b>	<b>3.8</b>	<b>3.3</b>	<b>4.1</b>	<b>1.1</b>	<b>100.0</b>
<b>Personal consumption expenditures</b> .....	<b>3.9</b>	<b>3.6</b>	<b>3.5</b>	<b>3.4</b>	<b>4.1</b>	<b>1.1</b>	<b>2.71</b>	<b>2.49</b>	<b>2.44</b>	<b>2.35</b>	<b>2.85</b>	<b>0.79</b>	<b>70.1</b>
Durable goods.....	6.0	4.4	2.6	7.9	9.3	-17.5	0.51	0.37	0.22	0.64	0.76	-1.56	7.8
Nondurable goods.....	4.7	4.4	5.3	3.6	3.5	5.1	0.94	0.90	1.07	0.74	0.73	1.04	20.7
Services.....	3.0	2.9	2.8	2.3	3.3	3.2	1.27	1.22	1.15	0.97	1.36	1.32	41.5
<b>Gross private domestic investment</b> .....	<b>11.9</b>	<b>5.8</b>	<b>8.6</b>	<b>-3.7</b>	<b>5.3</b>	<b>12.2</b>	<b>1.82</b>	<b>0.96</b>	<b>1.42</b>	<b>-0.63</b>	<b>0.87</b>	<b>1.95</b>	<b>17.2</b>
Fixed investment .....	9.7	8.0	7.0	9.5	8.0	3.0	1.47	1.28	1.12	1.51	1.31	0.51	17.0
Nonresidential .....	9.4	8.5	5.7	8.8	8.5	2.8	0.92	0.87	0.58	0.90	0.88	0.30	10.8
Structures .....	2.2	1.9	-2.0	2.7	2.2	0.7	0.06	0.05	-0.05	0.07	0.06	0.02	2.8
Equipment and software.....	11.9	10.8	8.3	10.9	10.6	3.5	0.86	0.82	0.64	0.83	0.82	0.28	8.0
Residential.....	10.3	7.2	9.5	10.8	7.3	3.5	0.55	0.42	0.54	0.62	0.43	0.21	6.2
Change in private inventories.....							0.35	-0.32	0.29	-2.14	-0.43	1.45	0.2
<b>Net exports of goods and services</b> .....							<b>-0.73</b>	<b>-0.28</b>	<b>-0.40</b>	<b>1.11</b>	<b>-0.12</b>	<b>-1.18</b>	<b>-6.2</b>
Exports.....	8.4	6.7	7.5	10.7	2.5	2.4	0.80	0.68	0.74	1.07	0.26	0.25	10.5
Goods.....	8.9	7.1	5.3	16.0	3.2	3.8	0.59	0.49	0.37	1.08	0.23	0.27	7.3
Services.....	7.4	6.0	12.5	-0.4	1.0	-0.9	0.22	0.18	0.37	-0.01	0.03	-0.03	3.2
Imports.....	10.7	6.2	7.4	-0.3	2.4	9.1	-1.53	-0.96	-1.14	0.04	-0.38	-1.42	16.6
Goods.....	11.0	6.7	8.2	-1.1	3.5	10.0	-1.30	-0.86	-1.05	0.15	-0.46	-1.32	14.0
Services.....	9.6	3.5	3.7	4.4	-3.2	4.2	-0.23	-0.09	-0.10	-0.11	0.09	-0.11	2.6
<b>Government consumption expenditures and gross investment</b> .....	<b>2.2</b>	<b>1.7</b>	<b>1.9</b>	<b>2.5</b>	<b>2.9</b>	<b>-2.4</b>	<b>0.41</b>	<b>0.32</b>	<b>0.35</b>	<b>0.47</b>	<b>0.54</b>	<b>-0.45</b>	<b>18.9</b>
Federal .....	5.2	2.0	2.4	2.4	7.4	-7.0	0.36	0.14	0.17	0.17	0.52	-0.50	6.9
National defense.....	7.0	2.3	3.0	3.7	10.0	-13.1	0.32	0.11	0.14	0.17	0.46	-0.66	4.6
Nondefense.....	1.8	1.6	1.1	-0.2	2.4	6.9	0.04	0.04	0.03	-0.01	0.06	0.15	2.3
State and local.....	0.4	1.5	1.6	2.6	0.2	0.4	0.05	0.18	0.19	0.31	0.03	0.05	12.0

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.

tion primarily reflected a deceleration in consumer spending, an acceleration in imports, a downturn in Federal Government spending, and decelerations in investment in equipment and software and in residential fixed investment that were partly offset by an upturn in inventory investment.<sup>3</sup>

- Prices of goods and services purchased by U.S. residents increased 3.3 percent after increasing 4.2 percent in the third quarter and 3.3 percent in the second quarter. The deceleration in the fourth quarter (and the acceleration in the third quarter)

3. In this article, "consumer spending" is shorthand for "personal consumption expenditures," "Federal government spending" is shorthand for "Federal government consumption expenditures and gross investment," and "inventory investment" is shorthand for the NIPA series "change in private inventories."

mainly reflected the quarterly pattern of energy prices.

- Real disposable personal income (DPI) increased 7.0 percent after decreasing 2.0 percent in the third quarter. The upturn primarily reflected a sharp acceleration in current-dollar DPI and a deceleration in the implicit price deflator for personal consumption expenditures used to deflate current-dollar DPI.

The hurricanes that struck the Gulf states in the third quarter and early in the fourth quarter, like other natural disasters, exacted economic losses that have had consequences for the national economy and for the economies of certain regions. (See "Effects of the hurricane.")

Among the contributors to the deceleration in real

#### Fourth-Quarter 2005 Advance NIPA Estimates: Source Data and Assumptions

The "advance" estimates for the fourth quarter are based on the following major source data; as more and better data become available, the estimates will be revised. (The number of months for which data were available is shown in parentheses.)

**Personal consumption expenditures:** Sales of retail stores (3), unit auto and truck sales (3), and consumers' shares of auto and truck sales (2);

**Nonresidential fixed investment:** Unit auto and truck sales (3), construction put in place (2), manufacturers' shipments of machinery and equipment other than aircraft (3), shipments of civilian aircraft (2), and exports and imports of machinery and equipment (2);

**Residential investment:** Construction put in place (2), single-family housing starts (3), sales of new homes (2), and sales of existing houses (3);

**Change in private inventories:** Trade and nondurable-goods manufacturing inventories (2), durable-goods manufacturing inventories (3), and unit auto and truck inventories (3);

**Net exports of goods and services:** Exports and imports of goods and services (2);

**Government consumption expenditures and gross investment:** Federal outlays (3), state and local construction put in place (2), and state and local employment (3);

**GDP prices:** Consumer price indexes (3), producer price indexes (3), U.S. import and export price indexes (3), and values and quantities of petroleum imports (2).

BEA made assumption for source data that were not available. Table A shows the assumptions for key series; a more comprehensive list is available on BEA's Web site at [www.bea.gov/bea/dn/home/gdp.htm](http://www.bea.gov/bea/dn/home/gdp.htm).

Table A. Summary of Major Source Data and Assumptions for Advance Estimates, 2005:IV

[Billions of dollars, seasonally adjusted at annual rates]

	2005					
	July	August	September	October	November	December <sup>1</sup>
Private fixed investment:						
Nonresidential structures:						
Value of new nonresidential construction put in place.....	242.9	248.9	250.5	249.0	250.5	249.7
Equipment and software:						
Manufacturers' shipments of complete aircraft.....	29.6	40.2	14.3	27.8	26.6	27.2
Residential structures:						
Value of new residential construction put in place:						
Single family.....	421.7	425.6	435.0	440.1	446.5	448.8
Multifamily.....	46.3	47.2	48.1	48.8	48.5	48.4
Change in private inventories:						
Change in inventories for nondurable manufacturing.....	5.0	-3.6	2.2	17.0	-8.0	10.7
Change in inventories for merchant wholesale and retail industries other than motor vehicles and equipment.....	3.0	47.1	25.5	-1.9	27.3	45.7
Net exports: <sup>2</sup>						
Exports of goods:						
U.S. exports of goods, international-transactions-accounts basis.....	900.8	920.5	881.5	902.4	928.3	920.9
Excluding gold.....	895.8	915.2	875.6	896.4	922.5	915.0
Imports of goods:						
U.S. imports of goods, international-transactions-accounts basis.....	1,651.3	1,689.2	1,737.3	1,780.3	1,754.9	1,767.2
Excluding gold.....	1,647.6	1,685.1	1,731.9	1,775.2	1,749.5	1,761.9
Net exports of goods.....	-750.5	-768.7	-855.9	-877.9	-826.5	-846.2
Excluding gold.....	-751.7	-769.9	-856.3	-878.8	-827.0	-846.9
State and local government structures:						
Value of new construction put in place.....	229.7	231.0	231.8	234.5	236.2	235.3

1. Assumption.

2. Nonmonetary gold is included in balance-of-payments exports and imports but is not used directly in the estimation of national income and product account exports and imports.

GDP growth in the fourth quarter, consumer spending increased 1.1 percent and added 0.79 percentage point after increasing 4.1 percent and adding 2.85 percentage points. The sharp deceleration reflected a downturn in spending on durable goods that was partly offset by an acceleration in spending on nondurable goods. Spending on durable goods decreased 17.5 percent and subtracted 1.56 percentage points from real GDP growth after two consecutive quarters of accelerating growth. The downturn was driven primarily by a sharp downturn in motor vehicles and parts. Spending on nondurable goods increased 5.1 percent and contributed 1.04 percentage points to real GDP after increasing 3.5 percent and contributing 0.73 percentage point. The acceleration reflected an acceleration in clothing and shoes and an upturn in gasoline, fuel oil, and other energy goods. Spending on services increased 3.2 percent and contributed 1.32 percentage points to real GDP growth after increasing 3.3 percent and contributing 1.36 percentage points.

Real imports of goods and services accelerated, increasing 9.1 percent and subtracting 1.42 percentage points from real GDP growth after increasing 2.4 percent and subtracting 0.38 percentage point. Goods imports increased 10.0 percent and subtracted 1.32 percentage points from real GDP growth after increasing 3.5 percent and subtracting 0.46 percentage point. Contributing to the acceleration in goods imports were upturns in imports of petroleum and products, of nonpetroleum industrial supplies and materials, and of nonautomotive consumer goods that were partly offset by a downturn in “other” goods imports. Services imports turned up, increasing 4.2 percent and subtracting 0.11 percentage point from real GDP growth after decreasing 3.2 percent and adding 0.09 percentage point.

Federal Government spending decreased 7.0 percent, subtracting 0.50 percentage point from real GDP growth after increasing 7.4 percent and adding 0.52 percentage point. The downturn was primarily due to a downturn in defense spending that was partly offset by an acceleration in nondefense spending. BEA recorded a downturn in defense spending even though the *Monthly Treasury Statement*, which BEA mainly uses to estimate defense spending, showed relatively strong spending in the quarter.<sup>4</sup> (See the box “The

*Monthly Treasury Statement* and BEA’s Estimates of Federal Government Spending.”) In general, BEA adjusts the *MTS* data to conform to NIPA concepts.

Business investment in equipment and software increased 3.5 percent and contributed 0.28 percentage point to real GDP growth after increasing 10.6 percent and contributing 0.82 percentage point. The deceleration was primarily due to downturns in transportation equipment and in “other” information processing equipment and software that were partly offset by accelerations in computers and peripheral equipment and in “other” equipment.

Residential fixed investment increased 3.5 percent and contributed 0.21 percentage point to real GDP growth after increasing 7.3 percent and contributing 0.43 percentage point. The deceleration was mainly due to a downturn in brokers’ commissions that was partly offset by an acceleration in single-family housing.

Inventory investment added 1.45 percentage points to real GDP growth after subtracting 0.43 percentage point. Businesses increased real inventories \$25.7 billion in the fourth quarter after two consecutive quarters of inventory reduction. The inventory accumulation primarily reflected increased inventory investment by retail motor vehicle and parts dealers. Manufacturing industries liquidated inventories for the third consecutive quarter.

The advance estimates for the third quarter also show the following:

- Real spending for private investment in nonresidential structures decelerated, increasing 0.7 percent and contributing 0.02 percentage point to real GDP growth after increasing 2.2 percent and contributing 0.06 percentage point. The deceleration was primarily due to a downturn in investment in commercial and health care structures that was partly offset by an upturn in investment in manufacturing structures.
- Real exports of goods and services increased 2.4 percent and contributed 0.25 percentage point to real GDP, about the same as in the third quarter. Real exports of goods increased 3.8 percent and contributed 0.27 percentage point in real GDP growth after increasing 3.2 percent. The step-up was mainly due to an upturn in civilian aircraft, engines, and parts and an acceleration in “other” nonautomotive capital goods that were partly offset by a larger decrease in industrial supplies and materials and by a down-

4. See the “Technical Note,” at <[www.bea.gov/bea/newsrelarchive/2006/tech405a.htm](http://www.bea.gov/bea/newsrelarchive/2006/tech405a.htm)>.

turn in “other” exports. Services exports turned down. The deceleration in exports of goods and services in the third and fourth quarters of 2005 followed accelerations in real exports in both the first and second quarters of 2005.

- Real state and local government spending increased 0.4 percent and contributed 0.05 percentage point to real GDP growth after increasing 0.2 percent and contributing 0.03 percentage point.
- Real final sales of domestic product (real GDP less the change in private inventories) decreased 0.3 percent—the first decrease since the third quarter of 2001—after increasing 4.6 percent in the third quarter.
- Real gross domestic purchases (GDP less net exports) increased 2.2 percent after increasing 4.0 percent in the third quarter.
- The production of goods, of services, and of structures decelerated (table 2).
- Motor vehicle output turned down, decreasing 15.9 percent and subtracting 0.58 percentage point from

real GDP growth after increasing 17.6 percent and adding 0.56 percentage point.

- Final sales of computers increased 46.4 percent and added 0.33 percentage point to real GDP growth after increasing 20.3 percent and adding 0.16 percentage point.
- Real disposable personal income (DPI) increased 7.0 percent in contrast to a decrease of 2.0 percent in the third quarter. Current-dollar DPI increased 9.8 percent after increasing 1.6 percent. The current-dollar acceleration reflected a strong acceleration in personal income that was somewhat offset by an acceleration in personal current taxes.
- The personal saving rate was a negative 0.4 percent in the fourth quarter; the saving rate was a negative 1.8 percent in the third quarter.<sup>5</sup>

5. The personal saving rate is measured as personal saving as a percentage of current-dollar disposable personal income. An estimate of the national saving rate (measured as gross saving as a percentage of gross national income), along with the “final” NIPA estimates for the fourth quarter, will be available at the end of March.

**Table 2. Real Gross Domestic Product by Type of Product**

[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)	
	2004	2005	2005				2004	2005	2005					2005
			I	II	III	IV			I	II	III	IV		
<b>Gross domestic product (GDP)</b> .....	<b>4.2</b>	<b>3.5</b>	<b>3.8</b>	<b>3.3</b>	<b>4.1</b>	<b>1.1</b>	<b>4.2</b>	<b>3.5</b>	<b>3.8</b>	<b>3.3</b>	<b>4.1</b>	<b>1.1</b>	<b>100.0</b>	
Final sales of domestic product.....	3.9	3.8	3.5	5.6	4.6	-0.3	3.87	3.81	3.51	5.45	4.58	-0.33	99.8	
Change in private inventories.....							0.35	-0.32	0.29	-2.14	-0.43	1.45	0.2	
Goods.....	6.5	4.6	4.4	5.0	5.3	0.6	2.06	1.46	1.41	1.58	1.70	0.19	31.3	
Services.....	2.7	2.7	3.2	1.5	3.6	1.1	1.59	1.54	1.86	0.88	2.09	0.66	57.7	
Structures.....	5.7	4.8	5.2	8.4	3.3	2.5	0.57	0.49	0.53	0.85	0.35	0.26	11.0	
<b>Addenda:</b>														
Motor vehicle output.....	4.6	3.5	4.3	-0.3	17.6	-15.9	0.16	0.12	0.15	-0.01	0.56	-0.58	3.3	
GDP excluding motor vehicle output.....	4.2	3.5	3.8	3.4	3.7	1.8	4.05	3.37	3.66	3.32	3.58	1.70	96.7	
Final sales of computers.....	20.4	39.6	54.9	45.4	20.3	46.4	0.15	0.28	0.37	0.32	0.16	0.33	0.9	
GDP excluding final sales of computers.....	4.1	3.2	3.5	3.0	4.0	0.8	4.07	3.21	3.44	2.98	3.98	0.79	99.1	

NOTE. Percent changes are from NIPA table 1.2.1, and contributions to percent change are from NIPA table 1.2.2. Shares are calculated from NIPA table 1.2.5.

## Effects of the hurricane

Hurricanes, like other natural disasters, have a twofold effect on economic activity: They destroy property and thus reduce the stock of fixed assets, and they change the volume and pattern of current economic activity.

**Destruction of property.** The BEA measure of capital depreciation, the consumption of fixed capital (CFC), captures the reduction in the stock of fixed assets. A rise in CFC results in an equal decline in national income and net domestic product. In the fourth quarter, the hurricane added \$27.5 billion (at an annual rate) to CFC, much less than the hurricanes added in the third quarter (\$383.8 billion).

The destruction of property also affected personal and business income and triggered payments of insurance benefits. BEA estimates of the affected net income flows are included in its estimates of proprietors' income, rental income, corporate profits, and business current transfer payments (net) (table 3).<sup>6</sup> The estimates reflect both the uninsured losses resulting from the hurricane and the treatment of insurance services that BEA introduced as part of its 2003 comprehensive revision of the NIPAs.<sup>7</sup>

**Changed economic activity.** Natural disasters have myriad economic consequences, as normal production and activities are curtailed or terminated. In the case of hurricanes, for example, the reduction in incomes and tourism could adversely affect consumer and business spending. Also, damages to commercial assets could adversely affect industrial production in the area.

6. See the box "The Impact of the Third-Quarter Hurricanes on the NIPAs," SURVEY OF CURRENT BUSINESS 85 (December 2005): 4. For a broader explanation of the effects of disasters on the NIPAs, see <[www.bea.gov/bea/faq/national/FAQ.htm](http://www.bea.gov/bea/faq/national/FAQ.htm)>.

7. See Brent R. Moulton and Eugene P. Seskin, "Preview of the 2003 Comprehensive Revision of the National Income and Product Accounts: Changes in Definitions and Classifications," SURVEY 83 (June 2003): 17–34; and Baoline Chen and Dennis J. Fixler, "Measuring the Services of Property-Casualty Insurance in the NIPAs: Changes in Concepts and Methods," SURVEY 83 (October 2003): 10–26.

However, as assets are restored, the effects of construction will be reflected in investment spending.

These kinds of changes in the current level and pattern of activity are not separately identifiable in the GDP estimates, because they cannot be identified in the source data that are used to calculate the NIPA aggregates.

**Table 3. Hurricane Damages and Insurance Settlements for the Fourth Quarter of 2005<sup>1</sup>**

(Billions of dollars; quarterly estimates at annual rates)<sup>2</sup>

Line	Total	Damage to fixed assets	Insurance benefits <sup>3</sup>	
				Level
1	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	
2	Less: Consumption of fixed capital (CFC) .....	27.5	27.5	.....
3	<b>Equals: National income/net domestic product</b> .....	<b>-27.5</b>	<b>-27.5</b>	<b>0.0</b>
4	Proprietors' income with capital consumption adjustment (CCAdj) .....	-0.5	-4.1	3.6
5	Rental income of persons with CCAdj .....	-2.6	-15.0	12.3
6	Corporate profits with inventory valuation adjustment (IVA) and CCAdj .....	-22.9	-8.5	-14.4
7	Total payouts .....	.....	.....	-27.9
8	Insurance benefits received by corporations .....	.....	.....	8.4
9	National Flood Insurance Program .....	.....	.....	0.8
10	Florida Citizens Property Insurance Corporation .....	.....	.....	4.4
11	Business current transfer payments (net) .....	-1.6	.....	-1.6
12	Net insurance settlements to persons <sup>4</sup> .....	.....	.....	3.6
13	Net insurance settlements to government .....	.....	.....	-5.2
14	Federal .....	.....	.....	-0.8
15	State and local .....	.....	.....	-4.4
16	Less: Corporate profits with CCAdj .....	-22.9	-8.5	-14.4
17	Business current transfer payments to government .....	-5.2	.....	-5.2
18	<b>Equals: Personal income</b> .....	<b>0.5</b>	<b>-19.0</b>	<b>19.6</b>
Addenda:				
19	Personal income .....	0.5	-19.0	19.6
20	Proprietors' income with CCAdj .....	-0.5	-4.1	3.6
21	Rental income of persons with CCAdj .....	-2.6	-15.0	12.3
22	Net insurance settlements to persons .....	3.6	.....	3.6

1. Includes only explicit adjustments to source data for write-offs of nonrepairable damage and for insurance. Excludes impacts that are assumed to be reflected in source data.

2. The estimates of the actual damages and insurance settlements (not at an annual rate) can be derived by dividing the numbers shown in the table by 4; actual damages to fixed assets in personal income, for example, are estimated to be \$4.8 billion (\$19.0 billion at an annual rate).

3. Includes business interruption insurance.

4. Includes benefits paid to persons for the loss of personal property, such as motor vehicles and household furnishings and equipment.

NOTE: The estimates reflect the "advance" GDP release on January 27, 2006.

### The Monthly Treasury Statement and BEA's Estimates of Federal Government Spending

The Treasury Department's *Monthly Treasury Statement* (*MTS*) is an important source of data that the Bureau of Economic Analysis (BEA) relies on to calculate its estimates of Federal Government spending in the national income and product accounts (NIPAs). Many users of BEA's data use the *MTS* to get an early indication of BEA's quarterly estimates. While the *MTS* can be a useful tool for tracking Federal Government spending, there are critical differences between the two. The *MTS* is a financial accounting statement for the Federal Government; BEA's estimates of Federal spending in GDP are a measure of economic output derived from production.

Only about a third of the Federal budget constitutes spending on production activities. For example, \$1,475 billion in Federal current transfer payments for 2005, an important component of the Federal budget, are not counted as production and are therefore excluded from GDP. GDP also excludes Federal payments from the National Flood Insurance Program and transfers to states, individuals, and businesses for hurricane-related disaster relief. BEA's calculation of GDP also includes methods to ensure consistent accounting so that changes in government accounting procedures over time do not affect the measures of economic output from production.

The differences between the two measures can be large in absolute size and timing. For example, in calendar year 2005, Federal spending as measured in the *MTS* increased 8.1 percent, while Federal Government spending included in GDP increased 5.7 percent.

In the fourth quarter of 2005, key differences between the two measures were apparent: The NIPA data showed a significant drop in Federal Government defense spending, but the *MTS* data showed an increase in Federal military outlays, boosted by a significant rise in military personnel outlays in October. The difference stemmed mainly from the differing treatment of contributions to the Medicare-eligible retiree health care fund. The *MTS* for October captured a large annual payment of \$10.8 billion (\$43.1 billion at an annual rate) to this fund, recording it as a military personnel outlay. As a result, the October outlays for military personnel were the highest monthly outlay ever recorded by the *MTS*. In the NIPAs, payment to the Medicare-eligible retiree health care fund is treated as compensation, and the payment is spread over the course of the fiscal year on an accrual basis.

Military personnel spending in the *MTS* rose to historical highs even though the normal military pay usually disbursed at the beginning of the month was not included. Military pay typically is paid on the first day of the month. When the first day of the month falls on a weekend or a Federal holiday, the Department of Defense

disburses military pay on the last working day of the previous month. Because October 1, 2005, was a Sunday, the monthly pay measure was included in the September *MTS*. In December, the *MTS* recorded an extra pay day because January 1, 2006, was a holiday. In the NIPAs, military compensation is shown on an accrual basis and reflects the same number of pay days in each quarter. BEA makes the necessary pay day adjustments monthly and sums them for the quarter.

In general, *MTS* data can be useful for tracking BEA's defense consumption expenditures and gross investment, provided that users are aware of BEA's adjustments to the *MTS* data and key methodological differences.

However, the *MTS* is less effective for tracking NIPA measures of nondefense consumption expenditures and gross investment. The *MTS* reports on all types of Federal spending—unemployment insurance payments, Medicaid grants to state and local governments, subsidy payments to farmers, and spending for a multitude of other Federal programs. NIPA estimates of nondefense consumption expenditures and gross investment represent a small fraction of this other spending. The result is that growth in the two measures often differs significantly. In 2005, for example, the *MTS* data show that nondefense spending rose 7.8 percent, but the NIPA measure of nondefense Federal Government spending grew 5.3 percent.

BEA research reveals that trends in total *MTS* outlays or even department-level outlays will not accurately predict the estimates for nondefense consumption expenditures, because the volatility in these outlays typically is unrelated to spending for nondefense consumption expenditures and gross investment, which primarily reflect routine administrative costs and the pattern of investment in structures and equipment.

Every year, BEA publishes a table that reconciles the Federal NIPA estimates on a not seasonally adjusted basis to the *MTS* data in "Table 3.18B. Relation of Federal Government Current Receipts and Expenditures in the National Income and Product Accounts to the Budget, Fiscal Years and Quarters," which is published in the October SURVEY and is available at <[www.bea.gov](http://www.bea.gov)>.

This table itemizes the types of transactions included in the *MTS* that are not included in the Federal NIPA estimates and vice versa. It shows transactions that are recorded as negative outlays in the *MTS* but that are recorded as receipts in the NIPAs. It also delineates the types of timing adjustments needed to put the data on an accounting basis consistent with the NIPAs. In addition to these adjustments, other techniques are used to spread various once-a-year payments over the year and to account for the early payment of military compensation.

Pamela A. Kelly

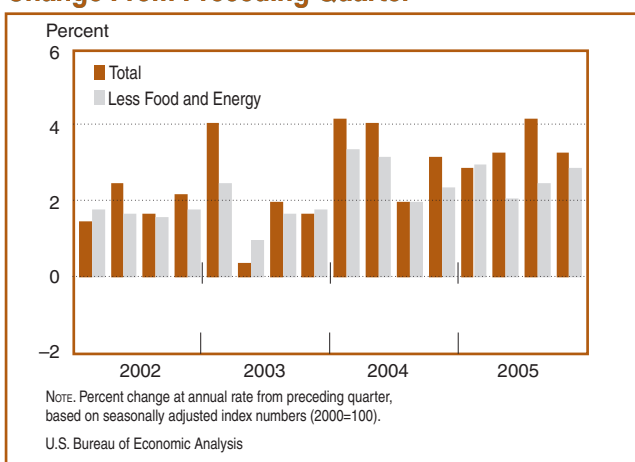
## Prices

Inflation as measured by the price index for gross domestic purchases decelerated to 3.3 percent in the fourth quarter from 4.2 percent in the third quarter (table 4). Energy prices decelerated in the fourth quarter, and food prices accelerated. Excluding prices for food and energy, gross domestic purchases prices increased 2.9 percent after increasing 2.5 percent (chart 2).

Prices of goods and services purchased by consumers increased 2.6 percent after increasing 3.7 percent. The prices paid for durable goods decreased for the third consecutive quarter, decreasing 1.0 percent in the fourth quarter after decreasing 3.0 percent in the third quarter. The smaller decrease primarily reflected an upturn in prices paid for motor vehicles and parts. Prices paid for nondurable goods decelerated sharply, increasing 0.7 percent after increasing 7.9 percent, mainly because of a downturn in prices of gasoline, fuel oil, and other energy goods. Prices paid for services accelerated, increasing 4.4 percent after increasing 3.1 percent, primarily reflecting an acceleration in prices paid for household energy services.

The prices paid by consumers for energy goods and services decelerated in the fourth quarter. The price index for consumer purchases excluding food and energy, which is sometimes viewed as an indicator of the

**Chart 2. Gross Domestic Purchases Prices: Change From Preceding Quarter**



**Table 4. Prices for Gross Domestic Purchases**

[Percent change at annual rates; based on seasonally adjusted index numbers (2000=100)]

	Change from preceding period (percent)						Contribution to percent change in gross domestic purchases prices (percentage points)					
	2004	2005	2005				2004	2005	2005			
			I	II	III	IV			I	II	III	IV
<b>Gross domestic purchases</b> .....	<b>2.9</b>	<b>3.2</b>	<b>2.9</b>	<b>3.3</b>	<b>4.2</b>	<b>3.3</b>	<b>2.9</b>	<b>3.2</b>	<b>2.9</b>	<b>3.3</b>	<b>4.2</b>	<b>3.3</b>
<b>Personal consumption expenditures (PCE)</b> .....	<b>2.6</b>	<b>2.8</b>	<b>2.3</b>	<b>3.3</b>	<b>3.7</b>	<b>2.6</b>	<b>1.7</b>	<b>1.9</b>	<b>1.5</b>	<b>2.2</b>	<b>2.5</b>	<b>1.8</b>
Durable goods .....	-1.9	-0.5	0.9	-0.5	-3.0	-1.0	-0.2	0.0	0.1	0.0	-0.2	-0.1
Nondurable goods .....	3.3	3.7	1.3	5.7	7.9	0.7	0.6	0.7	0.3	1.1	1.5	0.1
Services .....	3.2	3.1	3.0	2.9	3.1	4.4	1.3	1.2	1.2	1.1	1.2	1.7
<b>Gross private domestic investment</b> .....	<b>3.1</b>	<b>3.0</b>	<b>2.6</b>	<b>2.7</b>	<b>3.7</b>	<b>4.6</b>	<b>0.5</b>	<b>0.5</b>	<b>0.4</b>	<b>0.4</b>	<b>0.6</b>	<b>0.7</b>
Fixed investment .....	3.2	3.0	2.6	2.7	4.0	4.9	0.5	0.5	0.4	0.4	0.6	0.8
Nonresidential .....	1.3	2.1	3.1	1.9	2.5	3.7	0.1	0.2	0.3	0.2	0.3	0.4
Structures .....	5.5	10.0	10.3	9.9	16.5	19.5	0.1	0.2	0.2	0.2	0.4	0.5
Equipment and software .....	-0.1	-0.4	0.9	-0.7	-1.8	-1.2	0.0	0.0	0.1	-0.1	-0.1	-0.1
Residential .....	6.7	4.7	1.6	4.3	6.5	7.1	0.3	0.3	0.1	0.2	0.4	0.4
Change in private inventories .....							0.0	0.0	0.0	0.0	0.0	0.0
<b>Government consumption expenditures and gross investment</b> .....	<b>3.7</b>	<b>4.7</b>	<b>5.7</b>	<b>3.7</b>	<b>6.7</b>	<b>4.9</b>	<b>0.7</b>	<b>0.8</b>	<b>1.0</b>	<b>0.7</b>	<b>1.2</b>	<b>0.9</b>
Federal .....	4.2	3.6	7.0	2.1	3.0	0.3	0.3	0.2	0.5	0.1	0.2	0.0
National defense .....	4.0	3.5	6.6	1.4	3.5	0.5	0.2	0.2	0.3	0.1	0.2	0.0
Nondefense .....	4.6	3.7	7.9	3.6	2.1	-0.1	0.1	0.1	0.2	0.1	0.1	0.0
State and local .....	3.4	5.4	4.9	4.7	9.0	7.6	0.4	0.6	0.5	0.5	1.0	0.8
<b>Addenda:</b>												
Gross domestic purchases:												
Food .....	3.1	2.3	1.0	3.5	1.2	2.9	0.3	0.2	0.1	0.3	0.1	0.3
Energy goods and services .....	11.6	19.1	5.1	28.1	50.6	12.7	0.5	0.8	0.2	1.2	2.0	0.6
Excluding food and energy .....	2.4	2.5	3.0	2.1	2.5	2.9	2.1	2.2	2.6	1.8	2.1	2.5
Personal consumption expenditures:												
Food .....	3.1	2.2	1.0	3.5	1.3	2.6						
Energy goods and services .....	11.5	17.3	3.6	28.6	50.0	9.0						
Excluding food and energy .....	2.0	2.0	2.4	1.7	1.4	2.2						
"Market-based" PCE .....	2.3	2.7	2.1	3.4	3.9	2.4						
Excluding food and energy .....	1.5	1.7	2.2	1.5	1.1	1.8						
Gross domestic product .....	2.6	2.8	3.1	2.6	3.3	3.0						

NOTE: Most percent changes are from NIPA table 1.6.7; percent changes for personal consumption expenditures on food and on energy goods and services and for personal consumption expenditures excluding food and energy are calculated from index numbers in NIPA table 2.3.4. Contributions to percent change are from NIPA table 1.6.8.

underlying core rate of inflation, increased 2.2 percent after increasing 1.4 percent.

Prices of private nonresidential fixed investment increased 3.7 percent after increasing 2.5 percent. Prices of structures accelerated, increasing 19.5 percent after increasing 16.5 percent, but prices of equipment and software decreased 1.2 percent after decreasing 1.8 percent. Prices of residential fixed investment increased 7.1 percent after increasing 6.5 percent and have accelerated for three successive quarters.

Prices paid by government increased 4.9 percent after increasing 6.7 percent. Prices paid by the Federal Government for defense goods and services decelerated; prices paid for nondefense goods and services turned down. Prices paid by state and local governments also decelerated.

The GDP price index increased 3.0 percent in the fourth quarter, 0.3 percentage point less than the price index for gross domestic purchases.<sup>8</sup> The smaller increase in the GDP price index reflected a smaller increase in export prices (which are included in the GDP price index) than in import prices (which are included in the price index for gross domestic purchases).

### Personal Income

Real disposable personal income (DPI) rebounded in the fourth quarter, increasing 7.0 percent after decreasing 2.0 percent in the third quarter (chart 3). The upturn reflected a sharp acceleration in current-dollar DPI and a deceleration in the implicit price deflator for personal consumption expenditures (PCE). Current-dollar DPI increased 9.8 percent after increasing 1.6 percent, primarily because of a strong acceleration in personal income that was somewhat offset by an acceleration in personal current taxes (table 5).<sup>9</sup> The PCE implicit price deflator (which is used to deflate DPI) increased 2.6 percent after increasing 3.7 percent.

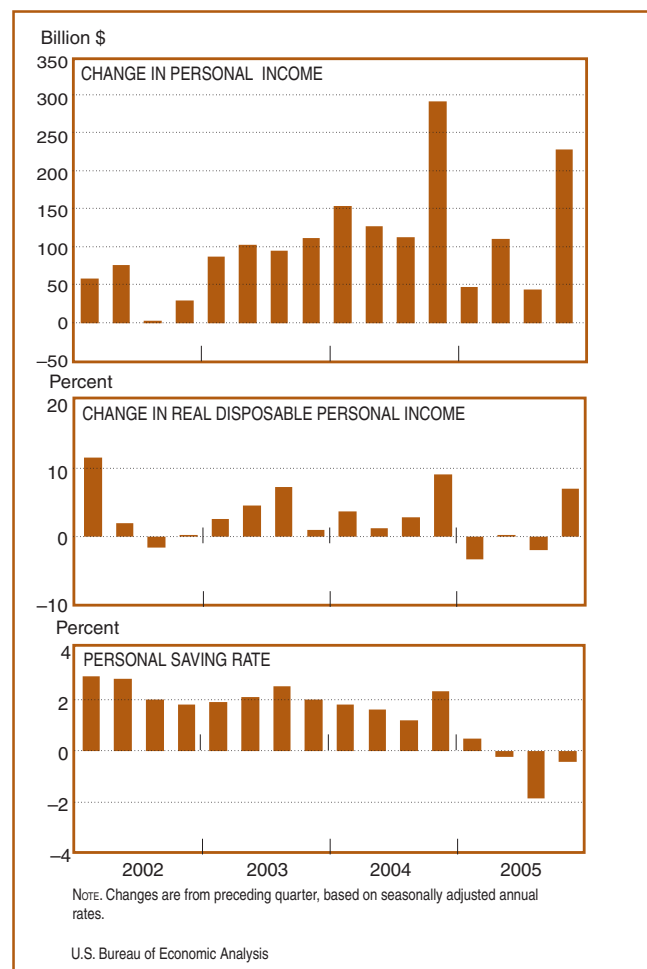
8. The GDP price index measures the prices paid for goods and services produced in the United States. The price index for gross domestic purchases measures the prices paid for goods and services purchased by U.S. residents, regardless of where those goods and services were produced.

9. Current-dollar DPI is defined as personal income less personal current taxes.

Personal income, which is only measured in current dollars, increased \$231.6 billion (or 9.4 percent) after increasing \$45.3 billion (or 1.8 percent) in the second quarter.<sup>10</sup> The acceleration primarily reflected a sharp upturn in rental income of persons, an upturn in non-

10. Quarterly NIPA estimates are presented at annual rates, which show the value that would be registered if the rate of activity that is measured for a quarter were maintained for a full year. The annual rates are determined simply by multiplying the estimated rate of activity by 4.

**Chart 3. Selected Personal Income and Saving Measures**





farm proprietors' income, and accelerations in government social benefits and in personal interest income. Changes in these components were partly offset by a sharp downturn in "other" current transfer receipts from business and by decelerations in wages and salaries and in employer contributions for employee pension and insurance funds.

The upturns in rental income and in nonfarm proprietors' income primarily reflected rebounds from the uninsured losses from the third-quarter hurricanes. The acceleration in government social benefits primarily reflected an upturn in state and local Medicaid payments that are part of current personal transfer receipts. The acceleration in personal interest income was mainly due to an increase in interest rates.

The downturn in "other" current transfer receipts

from business reflected the third-quarter net settlements that had been paid to persons for hurricane losses. The deceleration in wages and salaries primarily reflected data on employment, hours, and earnings from the Bureau of Labor Statistics. The deceleration in employer contributions for employee pension and insurance funds primarily reflected a deceleration in health insurance contributions. Employer contributions government social insurance also decelerated.<sup>11</sup>

Personal dividend income accelerated for the third consecutive quarter, increasing \$15.3 billion after increasing \$13.8 billion in the third quarter.

11. Employer contributions for government social insurance do not affect personal income. In the calculation of personal income, they are added in "supplements to wages and salaries" and subtracted in "contributions for government social insurance."

**Table 5. Personal Income and Its Disposition**

[Billions of dollars; quarterly estimates are seasonally adjusted at annual rates]

	Level		Change from preceding period					
	2005	2005	2004	2005	2005			
		IV			I	II	III	IV
Compensation of employees, received .....	7,113.6	7,237.3	366.5	426.0	105.9	58.5	95.2	81.9
Wage and salary disbursements .....	5,711.9	5,803.6	278.3	322.5	67.0	42.4	69.3	62.0
Private industries .....	4,740.4	4,822.0	242.2	290.4	55.2	36.9	61.6	55.4
Goods-producing industries .....	1,114.4	1,132.4	42.7	64.5	16.2	8.0	11.8	13.4
Manufacturing .....	720.1	728.7	19.0	32.4	7.5	0.2	5.3	7.9
Services-producing industries .....	3,626.0	3,689.7	199.5	225.9	38.9	29.1	49.7	42.1
Trade, transportation, and utilities .....	954.6	967.6	41.1	54.9	6.7	13.3	10.8	5.7
Other services-producing industries .....	2,671.4	2,722.1	158.4	171.0	32.2	15.8	38.8	36.5
Government .....	971.4	981.6	36.2	31.9	11.8	5.5	7.7	6.6
Supplements to wages and salaries .....	1,401.8	1,433.7	88.1	103.7	38.9	16.1	25.9	19.9
Proprietors' income with IVA and CCAAdj .....	937.8	964.2	79.4	48.2	17.0	18.7	-4.2	31.8
Farm .....	20.1	17.9	8.1	-15.7	0.1	-5.1	-1.6	-0.1
Nonfarm .....	917.7	946.3	71.4	63.9	16.9	23.9	-2.8	32.0
Rental income of persons with CCAAdj .....	73.9	84.5	2.5	-60.3	-10.7	-13.6	-115.5	95.6
Personal income receipts on assets .....	1,456.7	1,510.3	57.8	60.2	-85.7	31.9	29.1	41.4
Personal interest income .....	945.0	977.5	-11.7	39.1	8.0	20.6	15.2	26.3
Personal dividend income .....	511.7	532.9	69.5	21.1	-93.7	11.3	13.8	15.3
Personal current transfer receipts .....	1,525.5	1,545.5	83.5	98.0	39.6	20.8	48.5	-12.6
Less: Contributions for government social insurance .....	869.4	879.2	45.6	47.2	17.5	3.9	7.7	6.6
<b>Equals: Personal income .....</b>	<b>10,238.2</b>	<b>10,462.6</b>	<b>544.2</b>	<b>524.9</b>	<b>48.6</b>	<b>112.3</b>	<b>45.3</b>	<b>231.6</b>
Less: Personal current taxes .....	1,206.9	1,234.3	49.2	157.8	77.1	34.6	9.9	18.4
<b>Equals: Disposable personal income .....</b>	<b>9,031.3</b>	<b>9,228.3</b>	<b>495.0</b>	<b>367.1</b>	<b>-28.4</b>	<b>77.7</b>	<b>35.4</b>	<b>213.2</b>
Less: Personal outlays .....	9,072.8	9,261.6	516.2	560.3	129.6	146.6	172.7	87.7
<b>Equals: Personal saving .....</b>	<b>-41.6</b>	<b>-33.3</b>	<b>-21.0</b>	<b>-193.4</b>	<b>-158.0</b>	<b>-68.9</b>	<b>-137.4</b>	<b>125.6</b>
<b>Addenda: Special factors in personal income</b>								
In government wages and salaries:								
Federal pay raise .....		7.0			6.6	0.4	0.0	0.0
Federal civilian retroactive pay .....		0.0			0.0	0.0	0.0	0.0
Reservists' pay .....		8.1			0.3	-0.9	-0.7	0.1
In supplements to wages and salaries:								
Employer contributions for social insurance .....		4.1			4.1	0.0	0.0	0.0
In nonfarm proprietors' income:								
Hurricane-related net insurance settlements (excluding owner-occupied housing) .....		-0.5			0.0	0.0	-21.6	21.1
In rental income of persons:								
Hurricane-related net insurance settlements (excluding owner-occupied housing) .....		-2.6			0.0	0.0	-103.7	101.1
In personal dividend income:								
Microsoft "special" dividend payments .....		0.0			-99.4	0.0	0.0	0.0
In personal current transfer receipts:								
Social security retroactive payments .....		2.2			-2.5	0.0	0.0	2.2
Cost-of-living adjustments under Federal transfer programs .....		15.7			15.3	0.0	0.0	0.4
Hurricane-related net insurance settlements (excluding owner-occupied housing) .....		3.6			0.0	0.0	48.8	-41.9
In contributions for government social insurance:								
Changes in premium for supplementary medical insurance .....		5.4			5.4	0.0	0.0	0.0
In personal current taxes:								
Federal tax law changes .....		-2.7			-2.7	0.0	0.0	0.0
Refunds, settlements, and other .....		49.6			49.6	0.0	0.0	0.0

NOTE: Dollar levels are from NIPA tables 2.1 and 2.2B.  
IVA Inventory valuation adjustment  
CCAAdj Capital consumption adjustment

### Real GDP for 2005

Real GDP increased 3.5 percent in 2005 after increasing 4.2 percent in 2004 (table 1). Real gross domestic purchases increased 3.6 percent after increasing 4.7 percent.

The deceleration in real GDP primarily reflected a downturn in private inventory investment and decelerations in consumer spending and in Federal Government spending that were partly offset by a deceleration in imports.

Businesses reduced inventory investment in 2005 by \$34.8 billion. The reduction subtracted 0.32 percentage point from real GDP growth in contrast to the inventory accumulation in 2004 that added 0.35 percentage point to real growth.

Consumer spending increased 3.6 percent and contributed 2.49 percentage points to real GDP growth after increasing 3.9 percent in 2004 and adding 2.71 percentage points. The deceleration was primarily due to a downturn in spending for motor vehicles and parts and to a deceleration in spending for furniture and household equipment.

Federal Government spending increased 2.0 percent and contributed 0.14 percentage point to real GDP growth in 2005 after increasing 5.2 percent and con-

tributing 0.36 percentage point. Partly offsetting this deceleration, state and local spending increased 1.5 percent and contributed 0.18 percentage point to real GDP growth after increasing 0.4 percent and contributing 0.05 percentage point.

Imports decelerated in 2005, increasing 6.2 percent after increasing 10.7 percent. Imports subtracted 0.96 percentage point from real GDP growth in 2005 after subtracting 1.53 percentage points. The deceleration was widespread across imports of goods and of services.

The price index for gross domestic purchases increased 3.2 percent, compared with an increase of 2.9 percent in 2004, mainly reflecting an acceleration in energy prices; food prices decelerated (table 4). The price index for gross domestic purchases excluding food and energy remained roughly constant over 2004, increasing 2.5 percent in 2005 after increasing 2.4 percent.

Real DPI increased 1.4 percent after increasing 3.4 percent. The deceleration reflected a deceleration in current-dollar personal income that was reinforced by an acceleration in personal current taxes.