4th Quarter GDP (Preliminary)

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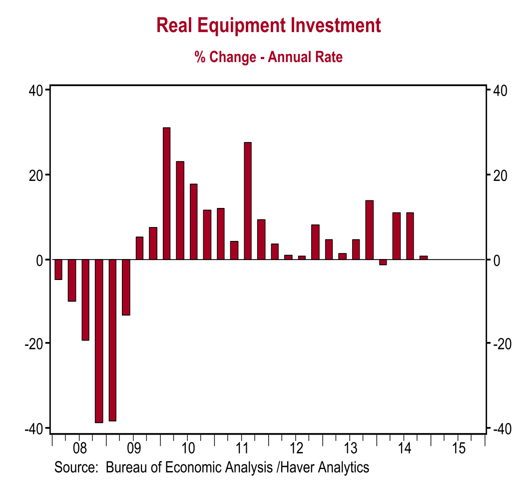
- Real GDP was revised to a 2.2% annual growth rate in Q4 from a prior estimate of 2.6%, beating the consensus expected revision to 2.0%.
- The largest downward revision, by far, was for inventories. Business investment was revised upward.
- The largest positive contribution to the real GDP growth rate in Q4 was personal consumption. The weakest component, by far, was net exports.
- The GDP price index was revised upward slightly to a 0.1% annual rate of change from a prior estimate of 0.0%. Nominal GDP growth – real GDP plus inflation – was revised down to a 2.3% annual rate from a prior estimate of 2.5%.

Implications: Real GDP growth was revised down for the fourth quarter, but still beat consensus expectations and presented a better "mix" for growth in 2015. The reason today's report is better for the economic outlook is that all of the downward revision came from inventories, which leaves more room to fill shelves and showrooms in future quarters. Meanwhile, business investment in equipment, intellectual property, and structures were all revised higher. Overall, what we have here is another plow horse report. Expect another report just like this for Q1, with unusually harsh East Coast weather and a West Coast port strike (now resolved) holding growth a little below what we think is a trend of 2.5% to 3%. Note that nominal GDP (real growth plus inflation) is up 3.6% from a year ago and up at a 4.1% annual rate in the past two years. These figures signal that a federal funds target rate of essentially zero is too loose. As a result, we think the Fed is still on track to start raising rates in June. In other news this morning, the Chicago PMI, a survey of manufacturing sentiment, fell to 45.8 in February from 59.4 in January. We think the drop reflects weather (a lot), the port strike (a little), and will rebound sharply next month. However, we're now forecasting that Monday's national ISM manufacturing report will decline to 52.0 from 53.5 in January. Also today, pending home sales, which are contracts on existing homes, increased 1.7% in January. Plugging this into our models suggests existing home sales (counted at closing) increase to 4.93 million in February.



4th Quarter GDP Seasonally Adjusted Annual Rates	Q4-14	Q3-14	Q2-14	Q1-14	4-Quarter Change
Real GDP	2.2%	5.0%	4.6%	-2.1%	2.4%
GDP Price Index	0.1%	1.4%	2.1%	1.3%	1.2%
Nominal GDP	2.3%	6.4%	6.8%	-0.8%	3.6%
PCE	4.2%	3.2%	2.5%	1.2%	2.8%
Business Investment	4.8%	8.9%	9.7%	1.6%	6.2%
Structures	5.0%	4.8%	12.6%	2.9%	6.2%
Equipment	0.9%	11.0%	11.2%	-1.0%	5.4%
Intellectual Property	10.9%	8.8%	5.5%	4.7%	7.4%
Contributions to GDP Growth (p.pts.)	**Q4-14**	**Q3-14**	**Q2-14**	**Q1-14**	**4Q Avg.**
PCE	2.8	2.2	1.8	0.8	1.9
Business Investment	0.6	1.1	1.2	0.2	0.8
Residential Investment	0.1	0.1	0.3	-0.2	0.1
Inventories	0.1	0.0	1.4	-1.2	0.1
Government	-0.3	0.8	0.3	-0.2	0.2
Net Exports	-1.2	0.8	-0.3	-1.7	-0.6