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4th Quarter GDP (Preliminary)

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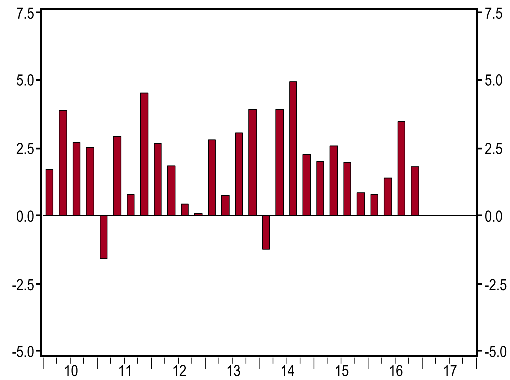
- Real GDP was unrevised at a 1.9% annual growth rate in Q4, lagging the consensus expected 2.1%.
- The largest upward revision was for consumption. Business investment, government purchases, residential investment and inventories were all revised down.
- The largest positive contribution to the real GDP growth rate in Q4 was personal consumption. The weakest component, by far, was net exports.
- The GDP price index was revised down slightly to a 2.0% annual growth rate from a prior estimate of 2.1%. Nominal GDP growth – real GDP plus inflation – was revised down to a 3.9% annual rate from a prior estimate of 4.0%.

Implications: Good news and bad news in today's GDP report, which is exactly what we should expect given the Plow Horse Economy. The second reading for real GDP growth was unrevised at a 1.9% annual rate for the fourth quarter, coming in below consensus expectations. However, the good news was that consumer spending, which tends to be more persistent, was revised higher, completely offsetting the declines in some more volatile categories, like government purchases and inventories. In other words, the "mix" of growth was slightly better than originally estimated. The bad news was that business investment and home building were revised lower as well. The bottom line is that today's report should not change anyone's impression about the economy. Nominal GDP growth (real growth plus inflation), was revised slightly lower to a 3.9% growth rate in Q4 versus a prior estimate of 4.0%. Still, nominal GDP grew 3.5% in 2016 and is up at a 3.2% annual rate in the past two years. All of these growth rates signal a federal funds target rate of 0.5 – 0.75% is far too low. This supports the case for the rise in the implied probability of a March rate hike based on the futures market, now at 48%. The Fed needs to move sooner than later as most measures of inflation are starting to creep up to the Fed's 2% target and will push though it as the year moves on. In other news this morning, the Chicago PMI, which measures manufacturing sentiment in that region, rose to 57.4 in February from 50.3, the highest reading for the index in more than two years. Meanwhile, the Richmond Fed index, a measure of mid-Atlantic factory sentiment, increased to +17 in February from +12 in January. These figures suggest tomorrow's national ISM report will beat consensus expectations of a reading of 56.2. In other news, the national Case-Shiller index, which measures home prices, increased 0.7% in December and is up 5.8% from a year ago, an acceleration from the 5.2% gain seen in 2015. Price gains in the past 12 months have been led by Seattle and Portland, with the slowest gains in Washington, DC and New York City.

Real GDP Growth

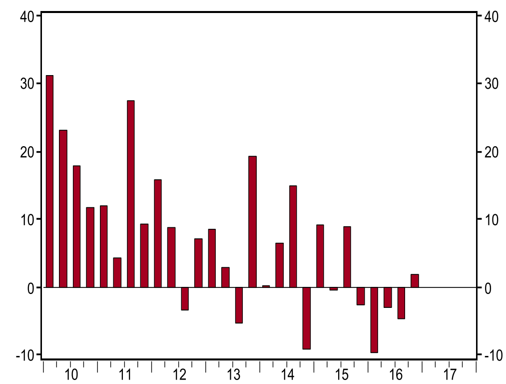
% Change - Annual Rate



Source: Bureau of Economic Analysis /Haver Analytics

Real Equipment Investment

% Change - Annual Rate



Source: Bureau of Economic Analysis /Haver Analytics

4th Quarter GDP Seasonally Adjusted Annual Rates	Q4-16	Q3-16	Q2-16	Q1-16	4-Quarter Change
Real GDP	**1.9%**	3.5%	1.4%	0.8%	1.9%
GDP Price Index	**2.0%**	1.4%	2.3%	0.5%	1.6%
Nominal GDP	**3.9%**	5.0%	3.7%	1.3%	3.5%
PCE	**3.0%**	3.0%	4.3%	1.6%	3.0%
Business Investment	**1.3%**	1.4%	1.0%	-3.4%	0.0%
Structures	**-4.4%**	12.0%	-2.1%	0.1%	1.2%
Equipment	**1.9%**	-4.5%	-3.0%	-9.5%	-3.9%
Intellectual Property	**4.5%**	3.2%	9.0%	3.8%	5.1%
Contributions to GDP Growth (p.pts.)	**Q4-16**	**Q3-16**	**Q2-16**	**Q1-16**	**4Q Avg.**
PCE	**2.1**	2.0	2.9	1.1	2.0
Business Investment	**0.2**	0.2	0.1	-0.4	0.0
Residential Investment	**0.4**	-0.2	-0.3	0.3	0.0
Inventories	**0.9**	0.5	-1.2	-0.4	0.0
Government	**0.1**	0.1	-0.3	0.3	0.0
Net Exports	**-1.7**	0.9	0.2	0.0	-0.2