

MACROCOSM

Still Waiting for that "New Era"

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Revised GDP data deepens doubt about seemingly inevitable consumer retrenchment.

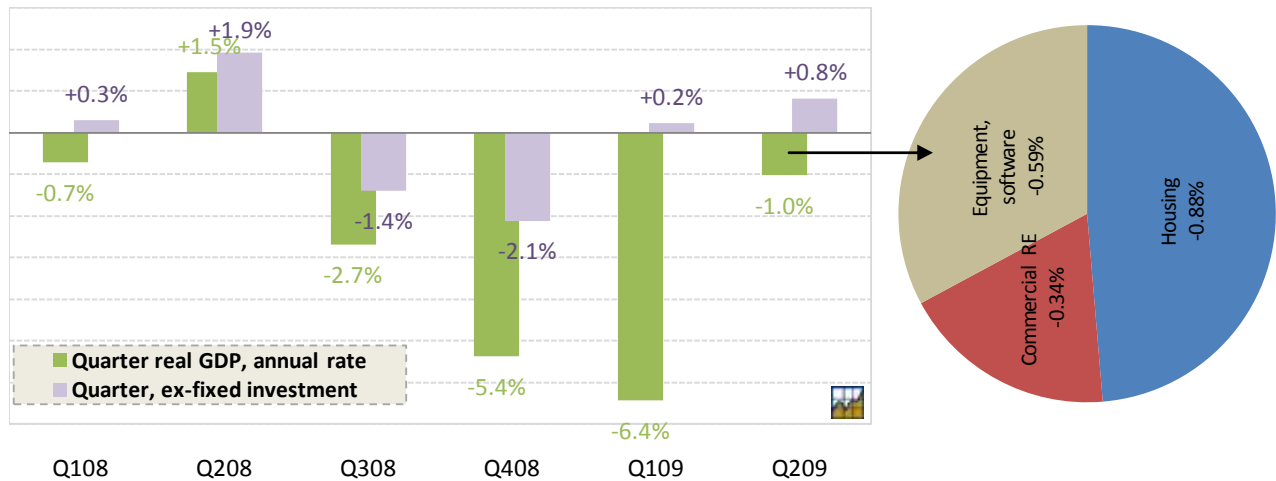
The [release this morning](#) of second quarter 2009 Gross Domestic Product data, including [substantial revisions](#) to past data, strengthens our views about the timing and cause of the recession, and about the prospects for a secular change in consumption patterns. We expect to write more later today about the likelihood, with today's new information, that the recession has troughed. With this report, we reiterate and amplify the broader views we expressed in May (see "[It's an Old New Era](#)" May 1, 2009) -- that this has been entirely an investment-led recession brought on by an exogenous credit shock, and that we still find no evidence to implicate popular alternative theories concerning "global imbalances" or the "retrenchment" of the "over-indebted US consumer."

Update to strategic view

US MACRO: Q2 GDP data, and revisions to past data, show an ongoing investment-led recession. There remains absolutely no evidence for the popular theory expecting a secular shift toward retrenchment in US consumption.

[\[see Investment Strategy Dashboard\]](#)

The chart below shows that the dominant cause of the recession was an extreme drop in fixed investment, which worsened as the credit crisis climaxed. Excluding fixed investment -- that is, residential and non-residential structures, and software and equipment -- the two most recent quarters *would have been positive*, even including large negative changes in private inventories,



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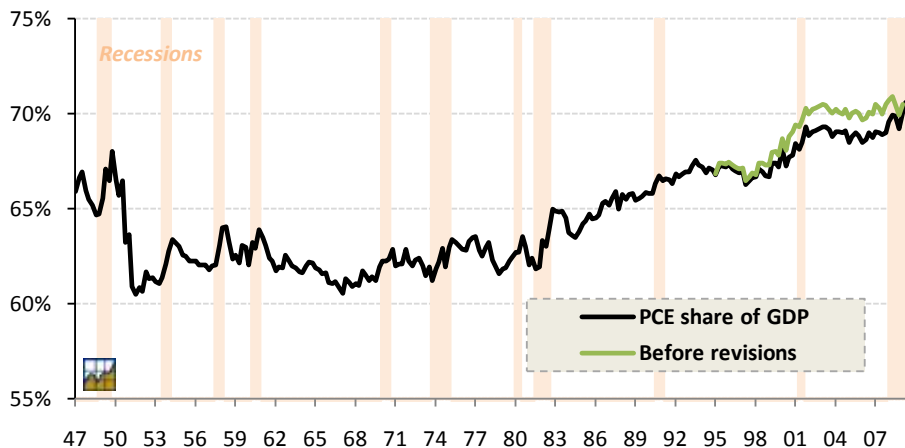
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which we do not count as investment for this analysis. The pace of decline in real fixed investment slowed somewhat in Q2 09 to 13.5%, an improvement from Q1 09's decline of 39.0%. But at that, it still more than explains the entire net decline in real GDP. In nominal terms, it leaves the fixed investment share of GDP at a new all-time low of only 12.3%.

Much has been written this morning about the large downward revision to Q1 2009 GDP -- by 0.9%. We would note that Q4 2008 was revised *upward* by slightly more -- 1.0% -- but considering that those two quarters together represented the worst of the credit market tempest, it doesn't seem important how results are allocated between them. What is more interesting to us is the 2.2% negative revision to Q3 2008, taking real GDP from what had been an only modestly negative 0.5% to a strongly negative 2.7%. This means that the recession became truly worthy of the name in *that* quarter, not Q4 2008 as the data had previously indicated. This revision is consistent with our narrative that the recession was triggered by the exogenous shock of the sudden intensification of the world credit crisis -- which actually began in earnest mid-quarter, in July 2008, with the onset of Fannie Mae and Freddie Mac's collapse -- followed in September by the fall of Lehman, Merrill, AIG, Wachovia and Washington Mutual.

Most noteworthy to us in the new data and the revisions is personal consumption expenditures. In *real* terms, PCE fell at an annual rate of 1.2% in the quarter, outpacing on the downside the overall fall in real GDP of 1.0%. But in *nominal* terms, which permits an apples-to-apples comparison of all the components of GDP, consumption *grew* 0.1% while overall GDP *fell* 0.8%. This means that the consumption share of GDP rose quarter-on-quarter. In fact, PCE rose to 70.6% of GDP, *which is a new all-time record*. What's more, with this morning's revisions, we can now see that throughout this recession, the consumption share of GDP *has consistently been higher than it was before the recession began*.



This starkly contradicts the popular notion that this recession was triggered by the fragility of the supposedly over-indebted US consumer, and his supposed post-millennial consumption binge that turned America into what [Warren Buffet calls](#) "Squanderville." Among the

most persistent voices for this theory among professional economists has been David Rosenberg, who with the intensification of recession late last year, declared victory by proclaiming a "new theme," a "frugal future" of consumer retrenchment (see ["Is This a 'New Era' Recession?"](#) December 29, 2008). These notions are not without their compelling logic, and many of our clients are strongly convinced of them. However, this morning's revisions move downward the consumption share of GDP since 2000 from above 70% to the mid-high 60%'s (see the chart above). And the data now shows a spike in the consumption share concomitant with the present recession, exactly when the "frugal future" idea would have predicted it would decline (again, see the chart above). It may yet play out. But so far it has always been invisible in the data -- and has just gotten more so.

BOTTOM LINE: Q2 GDP data, and revisions to past data, show an ongoing investment-led recession. There remains absolutely no evidence for the popular theory expecting a secular shift toward retrenchment in US consumption. ▶