ECONOMIC UPDATE
REGIONS
January 26, 2023

Q4 2022 GDP: Headline Growth Print Hides Loss Of Momentum As 2022 Came To A Close

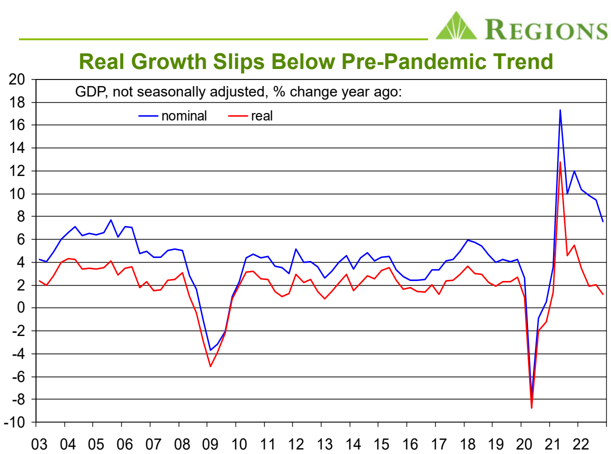
- The BEA's first estimate shows real GDP grew at an annualized rate of 2.9 percent in Q4 after 3.2 percent growth in Q3
- Full-year 2022 real GDP growth was 2.1 percent, following growth of 5.9 percent in 2021

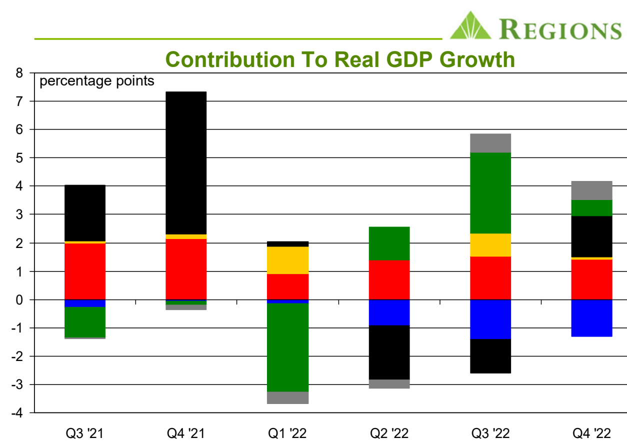
Real GDP grew at an annualized rate of 2.9 percent in Q4 2022 according to the initial estimate from the BEA, a touch better than our forecast of 2.8 percent growth and further ahead of the consensus forecast of 2.6 percent growth. For full-year 2022, real GDP grew by 2.1 percent after advancing by 5.9 percent in 2021. In any given quarter, the initial GDP print is based on highly incomplete source data, with BEA estimates filling in the gaps. As more source data are released, and revised, the initial estimate of GDP is prone to sizable revision, and there is no reason to think the initial estimate of Q4 GDP will be an exception to that general rule. Indeed, as we noted in this week's *Economic Preview*, a host of data releases coinciding with the release of the GDP report left considerable uncertainty around our forecast, and while our forecast of real GDP growth was close to the mark, the composition of that growth was not what we expected. For instance, relative to our expectations, inventories and trade made larger contributions to growth while consumer spending and business investment made smaller contributions. Again, the initial estimate will be revised twice, and both the headline growth number and the details could ultimately, differ from what BEA reported today. The much more relevant question, however, is not how the economy performed in last year's final quarter but instead how the economy is positioned for 2023. The economy clearly lost momentum over the final weeks of 2022, and the December data on consumer spending and business investment are in keeping with our premise that this year will see only meager growth in private domestic demand. Indeed, real private domestic demand growing at an annual rate of just 0.2 percent in Q4 sets the stage for a weak start to 2023 growth.

Real consumer spending grew at an annual rate of 2.9 percent in Q4 and while services spending was the main driver of that growth, the 2.6 percent annualized increase in real services spending was smaller than our forecast anticipated. Growth in our proxy for discretionary services spending (consumer spending on services less housing, utilities, health care, and financial services) slowed meaningfully in Q4, and while we've for some time anticipated growth slowing, the extent of the slowdown reported in the Q4 GDP data is surprising. Either way, we expect discretionary services spending to soften further over this year's first half and at the same time expect some retrenchment in consumer spending on goods which, at year-end 2022, remained above the pre-pandemic trend. A softer trajectory of growth in consumer spending is a key factor in our expectation for only middling growth in private domestic demand.

Real business fixed investment grew at an annualized rate of just 0.7 percent in Q4, falling short of our forecast. While we have noted the monthly data on core capital goods was pointing to slower growth in business investment in equipment and machinery as reported in the GDP data, we nonetheless expected more out of Q4 than the annualized 3.7 percent decline. There were substantial declines in business spending on computer and communications equipment in Q4, and while those declines have to be put in the context of the rapid growth seen since the onset of the pandemic, they nonetheless were a drag on Q4 growth. Real outlays on intellectual property products grew at an annualized rate of 5.3 percent in Q4, well below the trend rate of growth in this key component of business investment, key in that spending on intellectual property products tends to drive subsequent changes in labor productivity.

As we anticipated, the contraction in real residential fixed investment in Q4 was smaller, albeit only modestly, than that seen in last year's third quarter. The sharp pullback in starts of single family homes remains the biggest drag on residential fixed investment. While we expect this drag to abate over the course of 2023, slower growth in consumer spending and business fixed investment will become bigger drags on growth in private domestic demand. The initial estimate shows a smaller trade deficit added just over half a percentage point to top-line real GDP growth in Q4, which came as a bit of a surprise given the widening in the trade in goods deficit in December. At the same time, BEA estimates that nonfarm business inventory accumulation added 1.46 percentage points to top-line real GDP growth, a larger add than we expected. It is worth noting that trade and inventories tend to be quite volatile from one quarter to the next, to the point that they can and often do skew top-line growth, hence our emphasis on private domestic demand as a better indicator of the underlying health of the U.S. economy.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com