Fourth Quarter GDP Report

Economic growth during the fourth quarter slowed to an annual rate of 0.7 percent, down from 2.0 percent from the previous quarter. Excluding inventories, final sales grew at an annual rate of 1.2 percent. The slowdown was broadly based**.** Consumers, equipment, exports and inventory accounted for the bulk of the softness. New home construction was a bright spot in the report.

Just about every cylinder in the engine stalled during the final quarter of 2015.Furthermore, the economy has been losing altitude since mid-2014 contradicting healthy job gains. The recent rout in the stock market has damaged consumer and business confidence pointing to further weakness in the underlying strength of the economy.

One of the largest drag on the economy was consumer spending which accounts for about 70 percent of the GDP. They had every reason to spend including healthy employment gains, cheaper gasoline and lower import prices. Instead, consumers remained cautious about spending boosting the savings rate instead. The unseasonably warm weather contributed to the softness, especially for apparel and utilities.

Consumers were more interested in bargains forcing retailers to shave margins and diminishing total sales. Consumers are not in a position to splurge either. High prices for homes, rents and healthcare in addition to near-record level of auto purchases constrained their ability to spend.

Clearly consumers are not about to open their wallets. Consumers' spending habits are slow to change. The limited increase in household income, as evidenced by the sluggish wage increases, will continue to weigh on spending. Consumers are not going to be a major source of strength in economic growth during 2016.

Capital spending was another disappointment. Economic uncertainties are encouraging businesses to postpone spending. The plunge in oil price hurting the related industries was another impediment to growth.

Inventories continue to shave economic growth. There was overbuilding of inventories during the first half of the year. With soft sales, businesses are drawing down unwanted inventories. During the final quarter of 2015, inventories subtracted 0.5 percentage from economic growth on the heels of 0.7 percentage during the third quarter.

The strong dollar and the weak economies overseas have been another headwind for the economy. Exports fell while imports rose slowing overall economic growth.

Inflation was absent. PCE, monitored by the Federal Reserve remained flat, after 1.3 percent gain in the third quarter. This is below central bank’s target of 2 percent.

The Federal Reserve should be worried by the report. The monetary authorities would want to make sure that economic growth is on a healthy upward trend before raising the interest rate again in 2016.