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Revised Data Reveal Bigger Boost from New Growth Drivers in Moderate US Recovery

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The US economic rebound has been relatively modest, in contrast with previous recoveries from deep recessions. Although the initial stage of recovery was sparked by a new mix of growth drivers, led by exports, we believe that a sustainable cycle will require broader contributions from domestic sectors as well.

The current US economic recovery doesn't fit the historical mold. GDP has not rebounded strongly, as it usually does following a very deep recession, and the composition of economic growth is radically different than the first year of any other recovery downturn in modern times. These two key differences have made it harder for analysts and policymakers to forecast the economy's path, since many features of the current cycle are unique.

However, we believe the distinguishing features of the US recovery that began in mid-2009 do not necessarily undermine the economy's ability to secure long-term growth. In fact, our analysis of the recent preliminary second-quarter GDP figures and revised data for the past three years suggests that a new mix of growth drivers is helping the US economy get even closer to a sustainable and balanced recovery than widely perceived.

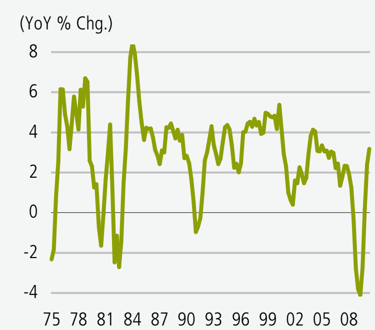
The below-average pace of the current recovery is particularly noteworthy because it has diverged from the historical pattern in which the severity of a recession is often a harbinger of the pace of recovery that follows. Indeed, deep downturns in the past have generally been followed by sharp upturns, while shallow recessions have been followed by weaker recoveries.

Current Recovery Looks Different

According to revised data, GDP recorded a record peak-to-trough decline of 4.1% during the Great Recession of 2008–2009, or 0.5 percentage points worse than initial estimates. Although this was a record economic slump in the postwar period, the rebound during the first year of the recovery proved to be modest by historical standards, as real GDP advanced by just 3.2% in its first year—well below the historical average of 4.7% **(Display 1)**.

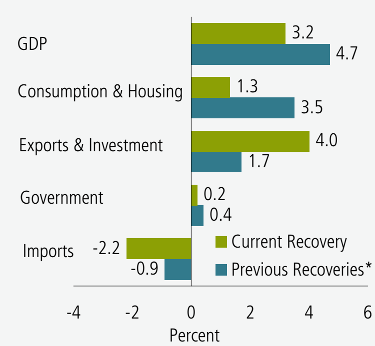
The rebound still ranks higher than the weak GDP recoveries of 1991–1992 and 2002, when the economy advanced by 1.9% and 2.6% respectively. But following deep downturns, recoveries of economic growth tend to exceed the recessionary decline by a factor of two or more. That's

Display 1
Modest Recovery Follows Record Slump



Source: Bureau of Economic Analysis and Haver Analytics

Display 2
New Mix of GDP Growth: First Year of Recovery



*Economic recoveries after recession since World War II
Source: Bureau of Economic Analysis and Haver Analytics

what happened following the deep downturns of 1973–1975 and 1981–1982, when first year gains of 6.2% and 7.7% respectively more than doubled the output decline of the recession.

New Mix Drives GDP Gains

In the past, no matter how fast or slow the economy rebounded after a recession, the first year of recovery was always driven by the early cyclical sectors of consumer spending and housing. Not this time. For the first time in the postwar period, exports and investment drove an economic recovery, with a combined contribution to real GDP from both sectors that exceeded the overall gain in real GDP. According to the revised data, growth in exports and business investment added four percentage points to real GDP growth over the past year. That's almost one percentage point more than the total gain and nearly 2.5 times more than the average contributions from these two important sectors in previous economic recoveries **(Display 2)**.

These new drivers of economic growth came at an opportune time because the traditional engines of growth—consumption and housing—were providing little support for the recovery. These two sectors added 1.3 percentage points to GDP growth in the first year of recovery, roughly a third of the typical contribution during the postwar period. The weak contribution was expected because consumer spending power and psychology was hit hard during the recession, through a combination of record job losses and wealth destruction. As a result, many people chose to delay big ticket purchases, reduce debt positions to more manageable levels and increase savings in the process.

Personal Finances Are Improving

The good news is that consumers have accomplished this much faster than anyone had expected. According to the GDP revisions, personal income was revised up by $170 billion at the end of 2009 **(Display 3)**, reflecting higher employee compensation, as well as upward revisions to dividends, interest payments and proprietors (or small business income). The income revision is noteworthy because the Bureau of Economic Analysis now has complete information on wage and salary income through the fourth quarter of 2009, which was found to have been understated by nearly $50 billion. In our view, personal income is probably still being understated, because the upturn in federal withheld income tax receipts started in April 2010, four months after the point up to which the government has hard income data.

Importantly, the revision to personal saving was even larger than the income revision, as the government also lowered spending and tax numbers a bit. Personal saving in the fourth quarter of 2009 reached $623.4 billion, roughly $220 billion more than the earlier estimates, according to the revised GDP data. The personal saving rate was revised by nearly two percentage points to 5.9% in 2009 and is estimated to have risen to 6.2% in the second quarter. For the past year and half, the personal saving rate has averaged close to 6% **(Display 4)**. The last time it was near 6% for that length of time was in the early 1990s.

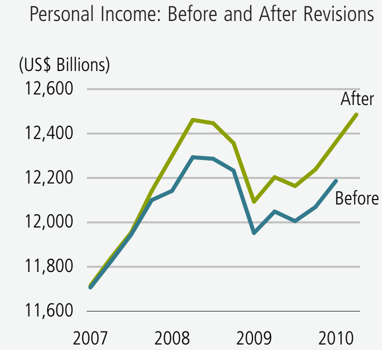
Better Prospects for Consumers

Upward revisions to personal income and saving data indicate that the US economy is getting much closer to the point in the cycle at which the consumer will support the recovery with additional spending and investment. Of course, confidence in the sustainability of the cycle is still lacking and labor markets remain weak, so it may take time before consumers are eager to take additional risk. Yet we think concern about the pace and sustainability of the recovery is unwarranted, as the underlying data are showing signs of better balance.

Some analysts argue that heavy reliance on overseas demand is unhealthy and unsustainable, and risks triggering a quick and sharp setback in the GDP cycle. We believe the transition of US economic growth toward a new mix of growth drivers, with exports and investment leading the way, injected a much-needed spark into the recovery.

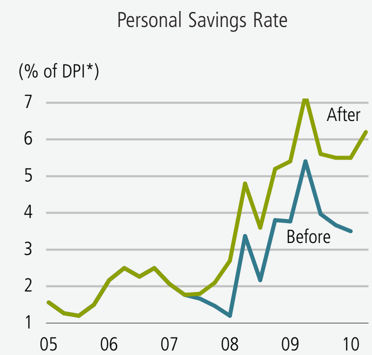
Yet we have also consistently argued that the new drivers of US economic growth must eventually filter back into domestic consumption and housing, via wealth creation and household income and saving flows, in order to foster long-term sustainable economic growth. We are starting to see many of the fundamental adjustments needed for the cycle to become more sustainable. But more improvements must unfold before consumers gain enough confidence to spend more, and that is only likely to come when news from labor markets improves. ■

Display 3
Good News: Income Revised Up Sharply



Source: Bureau of Economic Analysis and Haver Analytics

Display 4
Better News: Personal Savings Revised Even More



*Disposable Personal Income
Source: Bureau of Economic Analysis and Haver Analytics

AllianceBernstein US Economic Forecast

August 2010

Levels (2000 Dollars)	Quarterly					Annual			
	1Q:10	2Q:10	3Q:10	4Q:10	1Q:11	2008	2009	2010	2011
Real GDP	13,138.8	13,216.5	13,317.5	13,444.5	13,563.5	13,228.9	12,880.6	13,279.3	13,739.5
Consumption	9,225.4	9,262.7	9,312.4	9,360.4	9,420.4	9,265.0	9,153.9	9,290.2	9,504.2
Durables	1,138.9	1,159.6	1,175.0	1,185.0	1,195.0	1,136.4	1,094.6	1,164.6	1,217.5
Nondurables	2,053.5	2,061.7	2,075.0	2,090.0	2,115.0	2,041.2	2,017.4	2,070.1	2,142.5
Services	6,029.6	6,041.0	6,062.0	6,085.0	6,110.0	6,082.3	6,032.7	6,054.4	6,143.8
Investment									
Nonresidential Structures	319.3	323.3	327.0	330.0	334.0	464.2	369.6	324.9	344.0
Nonresidential Equip & Software	989.7	1,039.9	1,065.0	1,100.0	1,125.0	1,082.0	916.3	1,048.7	1,161.3
Res Structures	330.7	351.6	355.0	359.0	365.0	444.2	342.7	349.1	377.0
Change in Inventories	44.1	75.7	48.0	45.0	40.0	-37.6	-113.1	53.2	39.0
Net Exports	-338.4	-425.9	-388.0	-360.0	-340.0	-504.1	-363.0	-378.1	-307.5
Exports	1,616.4	1,656.7	1,700.0	1,745.0	1,780.0	1,647.7	1,490.7	1,679.5	1,842.5
Imports	1,954.8	2,082.6	2,088.0	2,105.0	2,120.0	2,151.8	1,853.8	2,057.6	2,150.0
Government	2,540.2	2,567.5	2,576.4	2,588.4	2,597.4	2,502.7	2,542.6	2,568.1	2,599.9

Percentage Changes	Quarterly % SAAR					% 4Q/4Q				Annual			
	1Q:10	2Q:10	3Q:10	4Q:10	1Q:11	2008	2009	2010	2011	2008	2009	2010	2011
Real GDP	3.7%	2.4%	3.1%	3.9%	3.6%	-2.8%	0.2%	3.3%	3.6%	0.0%	-2.6%	3.1%	3.5%
Consumption	1.9%	1.6%	2.2%	2.1%	2.6%	-1.9%	0.2%	1.9%	2.4%	-0.3%	-1.2%	1.5%	2.3%
Durables	8.8%	7.5%	5.4%	3.4%	3.4%	-12.3%	4.8%	6.3%	5.1%	-5.2%	-3.7%	6.4%	4.5%
Nondurables	4.2%	1.6%	2.6%	2.9%	4.9%	-2.9%	1.1%	2.8%	3.6%	-1.1%	-1.2%	2.6%	3.5%
Services	0.1%	0.8%	1.4%	1.5%	1.7%	0.3%	-0.8%	0.9%	1.5%	0.9%	-0.8%	0.4%	1.5%
Investment													
Nonresidential Structures	-17.8%	5.1%	4.7%	3.7%	4.9%	-1.5%	-26.5%	-1.6%	7.6%	5.9%	-20.4%	-12.1%	5.9%
Nonresidential Equip & Software	20.5%	21.9%	10.0%	13.8%	9.4%	-11.8%	-4.9%	16.4%	9.1%	-2.4%	-15.3%	14.5%	10.7%
Res Structures	-12.3%	27.8%	3.9%	4.6%	6.9%	-24.6%	-13.4%	5.1%	8.6%	-24.0%	-22.9%	1.9%	8.0%
Net Exports													
Exports	11.4%	10.4%	10.9%	11.0%	8.3%	-2.9%	-0.1%	10.9%	10.0%	6.0%	-9.5%	12.7%	9.7%
Imports	11.2%	28.8%	1.0%	3.3%	2.9%	-6.0%	-7.2%	10.6%	3.8%	-2.6%	-13.8%	11.0%	4.5%
Government	-1.6%	4.4%	1.4%	1.9%	1.4%	3.1%	0.8%	1.5%	0.6%	2.8%	1.6%	1.0%	1.2%
Domestic Demand	3.9%	5.1%	2.1%	2.9%	2.9%	-3.3%	-0.9%	3.5%	2.8%	-1.1%	-3.6%	3.1%	2.9%

Key Macro Indicators	Quarterly					Annual			
Nominal GDP (Levels)	14,446.4	14,597.7	14,756.6	14,953.4	15,153.5	14,369.1	14,119.1	14,688.5	15,492.2
% Q-o-Q SAAR	4.8%	4.3%	4.4%	5.4%	5.5%				
% Y-o-Y	2.8%	4.0%	4.5%	4.7%	4.9%	2.19%	-1.74%	4.03%	5.47%
Industrial Production (Index)	90.6	92.1	94.0	96.0	97.5	96.7	87.7	93.2	99.5
% Q-o-Q SAAR	7.1%	6.5%	8.7%	8.8%	6.4%				
% Y-o-Y	2.7%	7.2%	7.3%	7.7%	7.6%	-3.3%	-9.3%	6.2%	6.8%
Housing Starts (Millions)	0.62	0.60	0.65	0.70	0.75	0.90	0.55	0.64	0.86
Industry Auto Sales (Millions)	11.0	11.3	12.0	12.0	12.2	13.2	10.3	11.6	12.5
Personal Savings Rate	5.5%	6.2%	5.8%	5.5%	5.5%	4.1%	5.9%	5.8%	5.5%
Unemployment Rate	9.7%	9.7%	9.4%	9.0%	8.7%	5.8%	9.3%	9.5%	8.4%
Operating Profits (% Y-o-Y)	37.6%	37.9%	28.3%	18.1%	9.2%	-16.4%	-0.4%	29.8%	7.5%
After-Tax Profits (% Y-o-Y)	27.0%	27.2%	19.5%	13.3%	9.2%	-10.4%	5.1%	21.3%	7.1%

Inflation (% Y-o-Y)									
GDP Deflator	1.0%	1.8%	1.3%	1.5%	1.8%	2.2%	0.9%	0.9%	1.9%
Consumer Price Index	1.5%	-0.7%	1.8%	2.4%	1.8%	3.8%	-0.3%	1.7%	1.9%

Key Interest Rates (End of Period)									
Federal Funds Rate	0.13%	0.13%	0.13%	0.13%	0.50%	0.13%	0.13%	0.13%	1.50%
Three-Mo T-Bill (BEY)	0.16%	0.18%	0.20%	0.20%	0.50%	0.11%	0.06%	0.20%	1.50%
Two-Yr Note	1.02%	0.61%	0.75%	0.80%	1.10%	0.76%	1.14%	0.80%	2.25%
10-Yr Note	3.84%	2.97%	3.50%	3.65%	3.75%	2.25%	3.85%	3.65%	4.75%
30-Yr Bond	4.72%	3.91%	4.10%	4.25%	4.50%	2.69%	4.63%	4.25%	5.50%

*There is no guarantee that any forecasts or opinions in this material will be realized. Information should not be construed as investment advice.