Advance estimates released by the Commerce Department in late April show real GDP rising 5.6% in the first quarter—the largest gain in nearly 10 years and one that substantially exceeded expectations. Economists participating in April's Blue Chip survey were anticipating a 3.1% growth rate. Although the Commerce Department's advance estimates are constructed with preliminary and incomplete data, an analysis of past GDP revisions suggests that the reestimate of the first-quarter growth rate (to be released in May and June) will not fall below 5.0%.

Consumer spending, inventory accumulation, and business fixed investment led the first-quarter advance. Although exports rose sharply, imports increased at an even faster rate, and the trade deficit widened. Government spending continued to contract.

Looking ahead, most analysts now expect the economy's growth rate to slow to 2.0% by the end of the year. Forecasts tend to revert to that rate because many economists believe it is consistent with patterns of U.S. labor force participation, capital accumulation, and productivity gains over the past decade or so. Some observers, however, are beginning to question whether these estimates of the economy's growth potential are too low.

(continued on next page)
Consumer outlays accounted for most of the first-quarter surge. Real personal disposable income increased at a healthy year-over-year clip during the winter months, fueling strong expenditure growth as well as some improvement in household balance sheets. New home sales declined slightly in March, but remain at high levels and continue to show strong year-over-year gains (9.4%). Housing starts and building permits also remain at healthy levels.

Another major component of the first quarter's favorable growth performance was inventory accumulation. February's inventory-to-sales ratios (the latest available data) appeared low at the manufacturing, wholesale, and retail levels. Any subsequent buildup is likely to have been intended and should not hamper near-term growth.

Business fixed investment bounded ahead in the first quarter at twice the rate of total GDP, continuing the investment boom that started in 1991. Computers and related products accounted for most of this gain. Residential investment reversed a two-quarter decline.

Industrial production jumped approximately 0.9% in April, with gains in every component. The industrial sector, which has demonstrated particularly strong growth since early 1996, is operating at 84.1% of capacity, a two-year high. The latest purchasing managers' survey also confirms the strength of the nation's industries. More than 54% of the respondents reported higher output and orders growth in April, marking the eleventh consecutive monthly reading above 50%.