As expected, the economy grew more slowly in the second quarter than in the first. According to the Commerce Department’s advance estimates, real GDP grew at an annualized rate of 1.4% in 1998:IIQ. This stands in stark contrast to the first quarter’s revised growth rate of 5.5%, but the slowdown may not warrant much concern. At several other times in the current expansion, GDP growth has slipped for a quarter or two before rebounding. Forecasters currently expect real GDP to grow at a rate of 2.2% in the third quarter and 3.3% for the entire year.

The major factors leading to the slowdown in GDP growth were weakened net exports and a smaller inventory accumulation. Inventories rose $44.7 billion in the second quarter after growing a revised $91.4 billion in the first. This came as no surprise to forecasters, who had been expecting inventory accumulation to slow after its spectacular growth in the last few quarters. The dip in net exports, caused by plunging exports to Asia as well as continued rapid growth of imports, was equally significant. However, consumer spending, business fixed investment, and residential investment remained strong. Indeed, final sales to domestic purchasers (GDP excluding net exports and inventories) grew 6.3%, nearly equaling the strong first quarter growth of 6.6%.

After a small gain in May, industrial production dropped in June. (continued on next page)
Much of this decline is related to the now-resolved General Motors strike although industrial production excluding motor vehicles and parts also dipped slightly. Some of the overall decline was likely related to the recent trimming of inventories and declining exports to Asia.

The slump in the manufacturing sector is shown clearly in the National Association of Purchasing Management index. An index of less than 50 indicates contraction in the manufacturing sector; an index of more than 50 indicates growth. For both June and July, this index has been showing contraction in the manufacturing sector, following an extended growth streak. The resolution of the General Motors strike should reverse some of this slump, but adverse economic conditions in Asia may put a damper on manufacturing for the rest of 1998.

In contrast to the pause in the manufacturing sector, consumers continue to display confidence. Real personal consumption expenditures have grown 5.4% since last June, while real disposable income has grown 3.0%. The robust housing sector provides key evidence of consumers’ continued optimism. This June, new home sales soared to a record annual rate of 935,000 units. Existing home sales slipped somewhat for the month, but still remain near record levels.