Real GDP increased at an annualized rate of 2.5% in 2006:IIQ, according to the Commerce Department’s advance estimate. This was a sharp decrease from the previous quarter’s annualized growth rate of 5.6% and somewhat less than was generally expected. (The Blue Chip forecast for 2006:IIQ growth was 2.8% as of July 10.) The slowdown between 2006:IQ and 2006:IIQ was evident in all major components of GDP except imports. The advance estimate is consistent with other evidence that the economy slowed in 2006:IIQ.

Contributions from almost all components of the change in real GDP decreased significantly over the quarter. Residential investment caused a decrease of 0.40 percentage point (pp) in GDP compared to a drop of 0.02 pp in 2006:IQ. Personal consumption, which was $49.2 billion (chained 2000 dollars), contributed 1.74% pp to the quarterly change in real GDP. By comparison, personal consumption contributed 3.38 pp in 2006:IQ and 2.10 pp over the past four quarters. Change in inventories contributed 0.40 pp to growth in 2006:IIQ, after adding almost nothing in 2006:IQ. One bright spot is imports, which exerted virtually no drag on the U.S. economy in 2006:IIQ, compared with –1.46 pp the previous quarter.

Total industrial production rose 4.52% from June 2005 to June 2006 and was up 0.80% from May 2006. Capacity utilization has increased steadily since June 2003, reaching 82.4% of capacity in 2006:IIQ, the first time in six years that it has exceeded 82%.

Per capita personal income differs across states. Furthermore, the states’

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relative rankings are persistent: A scatter plot shows that states with low per capita incomes in 1960 also had (relatively) low per capita incomes in 2005. In other words, states do not show much mobility with respect to per capita income: If they did, the scatter plot would look more like a shotgun blast pattern.

Average personal tax rates, computed from the difference between personal income and personal disposable income, likewise display great persistence. States with high tax rates in 1960 tended to have high tax rates in 2005 as well (the scatter plot lines up roughly along an upward-sloping line).

Along with persistence in states’ per capita income rankings, there is also evidence of income convergence. States with low per capita income in 1960 exhibited, on average, faster real growth in 1960–2005 than those with high income in 1960, implying that the low-income states are catching up. In fact, economic theory predicts such convergence.

One might think that high taxes inhibit growth by discouraging capital accumulation. Do the data support this view? To control for the effect of initial income on growth, we can define “unexplained growth” as the difference between actual 1960–2005 growth and the best-fit line of growth against initial income. A scatter plot of unexplained growth against 1960 tax rates reveals no obvious pattern. One explanation is that average personal tax rates are not relevant; the tax rates on business income might be better measures but are difficult to construct using available data. Alternatively, states may use tax revenues partly to enhance growth, perhaps through improved infrastructure or workforce quality.