United States

Déjà vu?

■ **GDP growth was disappointing in Q1 2016, but this was no surprise. Unlike previous years, however, this sluggish performance cannot be blamed on exogenous shocks, weather conditions or strikes.**

■ **Mirroring a dynamic job market, household spending is holding up well, and public spending continues to turn around.**

■ **In contrast, productive investment contracted. Although this reflects the deterioration in corporate margins, what is alarming is its effect on productivity and potential growth.**

Like most years recently, 2016 began with virtually zero growth in the first quarter. The similarities are so striking that it is tempting to reprint word for word our commentary from the previous year or two. Yet there are some key differences. First, weather conditions are not to blame in 2016. Second, growth was not particularly strong in late 2015, at an annualised quarterly rate of only 1.4%. And last but not least, it is the breakdown of growth, or the lack thereof, that differentiates Q1 2016 from previous years.

GDP rose 0.5%, with all main components making smaller contributions to growth: changes in inventory, foreign trade and final domestic demand. The decline in domestic demand was due less to household consumption and public sector spending, than to corporate spending. Government spending increased at roughly the same pace as in previous quarters. Household spending slowed slightly but was still solid, notably residential investment.

Non-residential investment, in contrast, contracted for the second consecutive quarter, and the year-on-year rate of change slipped into negative territory for the first time since the end of the recession in 2009. At first sight, spending on structures would seem to be the main source of weakness. Yet this component of corporate investment integrates spending commodity extraction structures, which pulled down its overall contribution. Without this element, non-residential construction held up almost as well as its residential counterpart.

In the end, productive investment, i.e. spending on equipment and software, was the main source of weakness. Spending declined in late 2015, and this trend accelerated in early 2016. Short-term prospects are not very encouraging either: new orders of durable goods (excluding defence equipment and aircrafts) remained flat in March after a sharp decline in February.

This shortfall of investment is alarming in terms of future labour productivity gains. Since the revival of the job market in 2011, labour productivity has barely increased (up 0.5% a year on average). This sluggish pace has driven up unit labour costs despite wage moderation, which explains part of the slowdown in corporate margins. Higher unit labour costs coupled with the dollar's appreciation eroded America's external competitiveness at a time of sluggish world growth.

Torn between the desire to move away from the zero lower bound as far and as quickly as possible, and the need to counter growing job market tensions and deteriorating medium-term prospects, the Fed faces a big dilemma. It was not surprising that the monetary status quo was maintained at the last FOMC meeting, despite dissent from Esther L. George (President of the Kansas City Federal Reserve Bank). Although many welcomed the decision to no longer mention the risks related to global growth, a more pessimistic interpretation is also possible: this decision could also be explained by the increase in domestic risks more than by the easing of external risks.

Growth and its components

Quarterly growth, annualised rate, %	2016Q1	2015Q4	2015Q3
GDP	0.5	1.4	2.0
Final Domestic Demand	1.3	1.7	2.9
Private consumption	1.9	2.4	3.0
Government spending	1.2	0.1	1.8
Fixed Investment	-1.6	0.4	3.7
Residential	14.9	10.1	8.2
Non residential	-5.8	-2.1	2.6
Equipment & Software	-8.6	-2.1	9.9
Structures	-10.6	-5.1	-7.2
Intellectual Property Products	1.7	-0.1	-0.8
Change in inventories (contrib.)	-0.4	-0.2	-0.7
Net exports (contrib.)	-0.4	-0.1	-0.3
Exports	-2.6	-2.0	0.7
Imports	0.2	-0.7	2.3

Table 1 Source: US Bureau of Economic Analysis

Non-farm productive sector

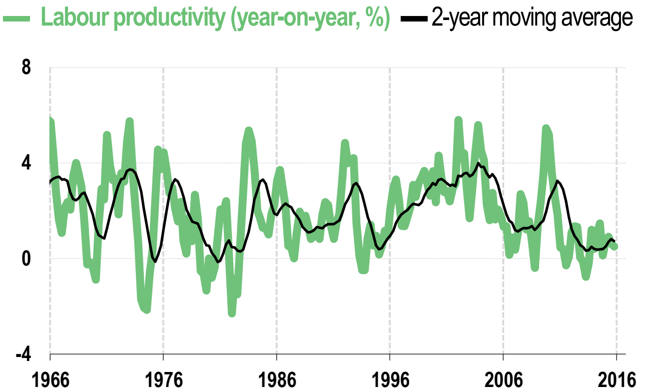

Chart 1 Source: US Bureau of Labor Statistics