

THE BUSINESS SITUATION

This article was prepared under the direction of Daniel Larkins.

ECONOMIC GROWTH slowed in the first quarter of 1995, according to the "advance" estimates of the national income and product accounts (NIPA's). Real gross domestic product (GDP) increased 2.8 percent in the first quarter after increasing 5.1 percent in the fourth quarter of 1994 and about 4 percent in the second and third quarters of 1994 (chart 1).¹ The slowdown was evident in the output of goods, services, and structures; within goods, motor vehicle output turned down, and the output of other goods increased less than in the fourth quarter (table 1).

Real gross domestic purchases increased 3.7 percent after increasing 4.2 percent (table 2). The slowdown in purchases was much smaller than the slowdown in GDP because net exports, which turned down sharply, are included in GDP but not in gross domestic purchases. Personal consumption expenditures slowed sharply, mainly reflecting a downturn in purchases of durable goods. Residential investment decreased after increasing. In contrast, nonresidential fixed investment, which had increased substantially in the fourth quarter, increased even more in the first, and inventory investment swung up sharply, as the rate of accumulation increased to \$63.0 bil-

lion. Government purchases decreased less than in the fourth quarter.

The fixed-weighted price index for gross domestic purchases increased 2.8 percent after increasing 2.6 percent. The fixed-weighted price index for GDP increased 3.1 percent after increasing 2.6 percent.

Motor vehicles.—Both output and sales of motor vehicles decreased in the first quarter; inventories increased for the fourth consecutive quarter. Output decreased 3.9 percent after increasing 13.0 percent (table 3). Final sales to domestic purchasers decreased 11.6 percent after increasing

1. Quarterly estimates in the national income and product accounts are expressed at seasonally adjusted annual rates, and quarterly changes are differences between these rates. Quarter-to-quarter percent changes are annualized. Real, or constant-dollar, estimates are expressed in 1987 dollars.

Table 1.—Real Gross Domestic Product, by Major Type of Product
(Seasonally adjusted at annual rates)

	Billions of 1987 dollars					Percent change from preceding quarter			
	Level	Change from preceding quarter							
		1994							
	1995:I	II	III	IV	I	II	III	IV	I
Gross domestic product ...	5,471.7	53.0	52.9	66.8	37.9	4.1	4.0	5.1	2.8
Goods	2,320.1	32.5	34.2	51.4	33.2	6.1	6.4	9.5	5.9
Motor vehicles	233.0	-12.2	4.8	7.1	-2.3	-19.2	8.9	13.0	-3.9
Other	2,087.1	44.7	29.4	44.3	35.5	9.6	6.1	9.1	7.1
Services	2,667.0	10.0	18.1	8.5	4.6	1.5	2.8	1.3	.7
Structures	484.5	10.4	.7	6.9	0	9.2	.6	5.9	0

NOTE.—Most series are found in NIPA table 1.4. Output of motor vehicles is the sum of auto output and truck output (from tables 8.4 and 8.6, respectively).

CHART 1

**Selected Measures:
Change From Preceding Quarter**

Percent



Note.—Percent change at annual rate from preceding quarter; based on seasonally adjusted estimates.

12.6 percent. Autos accounted for most of the decrease in output and all of the decrease in sales.

Final sales to consumers decreased 18.8 percent after increasing 21.6 percent; both autos and trucks contributed to the decrease. Factors frequently considered in analyses of consumer spending were mixed in the first quarter: The growth of real disposable personal income slowed, but the unemployment rate decreased, and the Index of Consumer Sentiment (prepared by the University of Michigan's Survey Research

Center) reached its highest level in 6 years. Factors specific to motor vehicles purchases also were mixed: Interest rates on new-vehicle loans increased for the fourth consecutive quarter, but manufacturers offered more sales-incentive programs during the first quarter.

Final sales to businesses increased 2.2 percent after increasing 14.5 percent. Trucks more than accounted for the first-quarter increase.

Nearly all of the first-quarter increase in inventories was accounted for by autos. The

Table 2.—Real Gross Domestic Product, Real Gross Domestic Purchases, and Real Final Sales to Domestic Purchasers

[Seasonally adjusted at annual rates]

	Billions of 1987 dollars					Percent change from preceding quarter			
	Level	Change from preceding quarter				1994			1995
		1994			1995	II	III	IV	I
	1995:I	II	III	IV	I				
Gross domestic product	5,471.7	53.0	52.9	66.8	37.9	4.1	4.0	5.1	2.8
Less: Exports of goods and services	696.9	24.3	22.6	31.4	-1.0	16.6	14.8	20.2	-6
Plus: Imports of goods and services	816.6	32.0	27.9	21.5	11.6	18.9	15.6	11.4	5.9
Equals: Gross domestic purchases	5,591.4	60.7	58.2	56.9	50.5	4.6	4.4	4.2	3.7
Less: Change in business inventories	63.0	33.8	-2.1	-7.7	13.6				
Equals: Final sales to domestic purchasers	5,528.4	26.9	60.3	64.6	36.9	2.0	4.6	4.8	2.7
Personal consumption expenditures	3,642.0	11.5	26.9	44.9	12.4	1.3	3.1	5.1	1.4
Nonresidential fixed investment	740.1	14.3	22.1	28.2	31.9	9.2	14.1	17.6	19.3
Residential investment	227.6	3.9	-3.6	1.3	-3.9	7.0	-6.0	2.3	-6.6
Government purchases	918.6	-2.8	14.9	-9.8	-3.6	-1.2	6.7	-4.1	-1.6

NOTE.—Dollar levels are found in NIPA tables 1.2 and 1.6. Percent changes are found in table 8.1.

Table 3.—Motor Vehicle Output, Sales, and Inventories

[Seasonally adjusted at annual rates]

	Billions of 1987 dollars					Percent change from preceding quarter			
	Level	Change from preceding quarter				1994			1995
		1994			1995	II	III	IV	I
	1995:I	II	III	IV	I				
Output	233.0	-12.2	4.8	7.1	-2.3	-19.2	8.9	13.0	-3.9
Autos	128.8	-9.2	2.4	2.5	-2.0	-24.6	7.8	8.0	-6.0
Trucks	104.2	-3.0	2.4	4.6	-3	-11.4	10.2	19.7	-1.1
Less: Exports	22.8	-7	1.5	-1.8	3.8	-13.3	34.9	-30.4	107.4
Autos	16.4	-6	1.8	-2.6	3.2	-15.5	62.2	-51.3	138.3
Trucks	6.4	-1	-3	.8	.6	-7.2	-20.8	81.1	48.3
Plus: Imports	68.3	7.7	3.2	2.2	.9	70.0	22.3	14.2	5.4
Autos	57.6	7.5	2.7	1.2	.6	83.9	21.9	8.9	4.3
Trucks	10.7	.2	.5	1.0	.3	9.5	24.4	49.8	12.0
Equals: Gross domestic purchases	278.5	-3.8	6.5	11.1	-5.2	-5.5	10.1	17.3	-7.1
Autos	170.0	-1.1	3.3	6.3	-4.6	-2.6	8.2	15.8	-10.1
Trucks	108.5	-2.7	3.2	4.8	-6	-10.0	13.3	19.7	-2.2
Less: Change in business inventories	14.1	5.4	4.4	3.1	3.1				
Autos	13.8	4.6	1.9	6.8	3.7				
Trucks .....	.3	.8	2.5	-3.7	-6				
Equals: Final sales to domestic purchasers	264.4	-9.2	2.1	8.0	-8.3	-12.9	3.2	12.6	-11.6
Autos	156.2	-5.7	1.4	-0.5	-8.3	-12.8	3.5	-1.2	-18.7
Trucks	108.2	-3.5	.7	8.5	0	-13.0	2.9	38.7	0

NOTE.—Dollar levels for autos and trucks are found in NIPA tables 8.4 and 8.6, respectively.

inventory-sales ratio for new domestic autos, which is calculated from units data, increased from 2.4 to 2.9, the highest it has been since the fourth quarter of 1989; the traditional industry target is about 2.4.

Prices

The fixed-weighted price index for gross domestic purchases increased 2.8 percent in the first quarter after increasing 2.6 percent in the fourth (table 4 and chart 2). Prices of personal consumption expenditures (PCE) and of nonresidential fixed investment increased at about the same rates as in the fourth quarter; prices of government purchases stepped up, and prices of residential investment slowed.

Prices of PCE increased 2.6 percent after increasing 2.5 percent. Food prices increased 1.6 percent after increasing 2.8 percent; the deceleration was accounted for by fresh vegetables and nonalcoholic beverages (mainly coffee), both of which changed little after large increases in the fourth quarter. Energy prices increased slightly after almost no change. Prices for PCE other than food and energy increased 3.0 percent after increasing 2.6 percent; most major categories contributed to the step-up.

Prices of nonresidential fixed investment increased 1.3 percent after increasing 1.4 percent. Structures increased 2.7 percent, about half as much as in the fourth quarter. Producers' durable equipment increased 0.4 percent after decreasing 0.7 percent; prices of information

First-Quarter 1995 Advance GDP Estimate: Source Data and Assumptions

The advance GDP estimate for the first quarter is based on the following major source data, some of which are subject to revision. (The number of months for which data were available is shown in parentheses.)

Personal consumption expenditures: Sales of retail stores (3) and unit auto and truck sales (3);

Nonresidential fixed investment: Unit auto and truck sales (3), construction put in place (2), manufacturers' shipments of machinery and equipment (3), and exports and imports of machinery and equipment (2);

Residential investment: Construction put in place (2) and single-family housing starts (3);

Change in business inventories: Manufacturing and trade inventories (2) and unit auto and truck inventories (3);

Net exports of goods and services: Exports and imports of goods and services (2);

Government purchases: Military outlays (3), other Federal outlays (3), State and local construction put in place (2), and State and local employment (3);

GDP prices: Consumer Price Index (3), Producer Price Index (3), price indexes for nonpetroleum merchandise exports and imports (3), and values and quantities of petroleum imports (2).

The Bureau of Economic Analysis (BEA) made assumptions for the source data that were not available. Table A shows the assumptions for key series; a more comprehensive listing of assumptions is available on the Department of Commerce's Economic Bulletin Board or from BEA.

Table A.—Summary of Major Data Assumptions for Advance Estimates, 1995:1

[Billions of dollars, seasonally adjusted at annual rates]

	1994			1995		
	October	November	December	January	February	March ¹
Fixed investment:						
Nonresidential structures:						
Buildings, utilities, and farm:						
Value of new nonresidential construction put in place	141.0	146.6	146.6	146.7	147.0	149.8
Producers' durable equipment:						
Manufacturers' shipments of complete civilian aircraft	13.2	21.2	21.4	18.3	22.0	13.3
Residential structures:						
Value of new residential construction put in place:						
1-unit structures	153.2	153.1	154.0	152.8	151.8	147.0
2-or-more-unit structures	15.0	16.3	17.0	17.1	17.0	15.5
Change in business inventories nonfarm:						
Change in inventories for manufacturing and trade (except nonmerchant wholesalers) for industries other than motor vehicles and equipment in trade	80.5	59.0	29.3	96.9	83.4	54.1
Net exports:						
Exports of merchandise:						
U.S. exports of merchandise, balance-of-payments basis	519.5	537.8	557.9	531.6	546.0	563.8
Imports of merchandise:						
U.S. imports of merchandise, balance-of-payments basis	700.9	719.8	712.6	733.8	716.3	736.6
Net merchandise trade (exports less imports)	-181.4	-182.0	-154.7	-202.2	-170.3	-172.8
Government purchases:						
State and local:						
Structures:						
Value of new construction put in place	120.8	116.5	119.8	117.9	116.3	117.0

1. Assumed.

processing equipment were unchanged after decreasing, as computer prices decreased less than in the fourth quarter. Prices of residential investment increased 1.8 percent after increasing 4.5 percent.

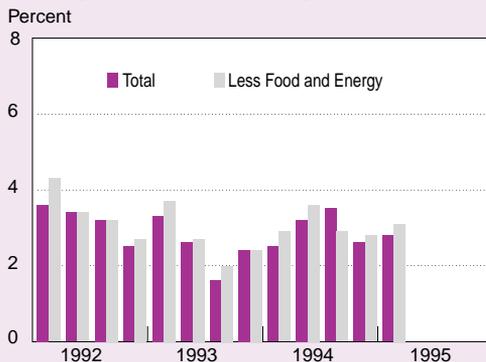
Prices of government purchases increased 4.5 percent after increasing 3.3 percent. Prices paid by the Federal Government increased 4.5 percent after increasing 3.9 percent; prices of national defense purchases stepped up, and prices of nondefense purchases slowed. These increases reflected a first-quarter pay raise for all Federal

employees; excluding the pay raise, prices paid by the Federal Government would have decelerated instead of accelerating. Prices of State and local government purchases increased 4.4 percent after increasing 2.8 percent.

The price index for GDP, which measures prices paid for goods and services produced in the United States, increased 3.1 percent after increasing 2.6 percent. This index, unlike the index for gross domestic purchases, includes the prices of exports and excludes the prices of imports. Export prices increased 6.8 percent after increasing 5.4 percent. Import prices increased 2.6 percent after increasing 4.3 percent. The price of imported petroleum and petroleum products turned up sharply, but prices of "other" merchandise imports—especially of foods, feeds, and beverages and of automotive components—slowed.

CHART 2

Gross Domestic Purchases Prices (Fixed Weights): Change From Preceding Quarter



Note.—Percent change at annual rate from preceding quarter; based on seasonally adjusted index numbers (1987=100).

U.S. Department of Commerce, Bureau of Economic Analysis

Table 4.—Fixed-Weighted Price Indexes

[Percent change at annual rates; based on seasonally adjusted index numbers (1987=100)]

	1994			1995
	II	III	IV	I
Gross domestic product	2.9	3.0	2.6	3.1
Less: Exports of goods and services	2.7	3.1	5.4	6.8
Plus: Imports of goods and services	5.8	8.2	4.3	2.6
Equals: Gross domestic purchases	3.2	3.5	2.6	2.8
Less: Change in business inventories .....	.....	.....	.....	.....
Equals: Final sales to domestic purchasers	3.2	3.5	2.6	2.8
Personal consumption expenditures	2.8	3.6	2.5	2.6
Food	1.3	5.5	2.8	1.6
Energy	-8	10.4	-1	.8
Other personal consumption expenditures	3.4	2.8	2.6	3.0
Nonresidential fixed investment	2.7	2.7	1.4	1.3
Structures	2.0	4.6	5.2	2.7
Producers' durable equipment	3.1	1.7	-7	.4
Residential investment	2.7	6.3	4.5	1.8
Government purchases	4.9	3.0	3.3	4.5
Addenda:				
Merchandise imports	7.7	8.9	3.3	4.2
Petroleum and products	79.6	50.0	-18.3	17.3
Other merchandise	3.4	5.9	5.5	3.1

NOTE.—Percent changes in major aggregates are found in NIPA table 8.1. Most index number levels are found in tables 7.1 and 7.2.

Alternative measures

For the first quarter of 1995, BEA's chain-type annual-weighted measure of real GDP increased 2.1 percent, 0.7 percentage point less than the featured fixed-1987-weighted measure; the benchmark-years-weighted alternative measure increased 2.2 percent (table 5). Most of the difference between the fixed-weighted and alternative measures was accounted for by a strong increase in purchases of computers, a product whose prices have decreased steadily since 1987. In the fourth quarter of 1994, the chain-type measure increased 4.0 percent, 1.1 percentage point less than the fixed-weighted measure; the benchmark-years measure increased 4.1 percent. Almost all of the difference between the fixed-

Table 5.—Fixed-Weighted and Alternative Quantity and Price Indexes

[Percent change at annual rates; based on seasonally adjusted index numbers (1987=100)]

	1994			1995
	II	III	IV	I
Gross domestic product:				
Quantity indexes:				
Fixed 1987 weights	4.1	4.0	5.1	2.8
Chain-type annual weights	4.2	3.6	4.0	2.1
Benchmark-years weights	4.1	3.6	4.1	2.2
Price indexes:				
Fixed 1987 weights	2.9	3.0	2.6	3.1
Chain-type annual weights	2.7	2.8	2.5	3.1
Benchmark-years weights	2.7	2.7	2.6	3.1
Gross domestic purchases:				
Price indexes:				
Fixed 1987 weights	3.2	3.5	2.6	2.8
Chain-type annual weights	3.1	3.2	2.4	2.7
Benchmark-years weights	3.1	3.2	2.5	2.8

NOTE.—Percent changes are found in NIPA table 8.1. Index number levels are found in tables 7.1 and 7.2.

weighted and alternative measures was also due to a strong increase in purchases of computers.

The chain-type measure of gross domestic purchases prices increased 2.7 percent in the first quarter, 0.1 percentage point less than the fixed-weighted measure; the benchmark-years measure increased 2.8 percent, the same as the fixed-weighted measure. In the fourth quarter of 1994, both of the alternative measures had increased less than the fixed-weighted measure: The chain-type measure had increased 2.4 percent—0.2 percentage point less than the fixed-weighted measure—and the benchmark-years measure had increased 2.5 percent.

Personal income

Real disposable personal income (DPI) increased 4.4 percent in the first quarter after increasing 7.5 percent in the fourth (chart 3). Current-dollar DPI slowed to a 7.0-percent increase after

a 9.2-percent increase; the slowdown mainly reflected smaller increases in wages and salaries and in farm proprietors' income. The personal saving rate (saving as a percentage of current-dollar DPI) jumped from 4.6 percent to 5.2 percent—the highest rate in more than 2 years.

Personal income increased \$106.5 billion after increasing \$122.1 billion (table 6). Wage and salary disbursements increased \$46.8 billion after increasing \$62.5 billion. The service and distributive industries accounted for most of the slowdown; manufacturing and other commodity-producing industries also slowed, while government and government enterprises accelerated. In most private industries, the first-quarter slow-

Table 6.—Personal Income and Its Disposition

[Billions of dollars; seasonally adjusted at annual rates]

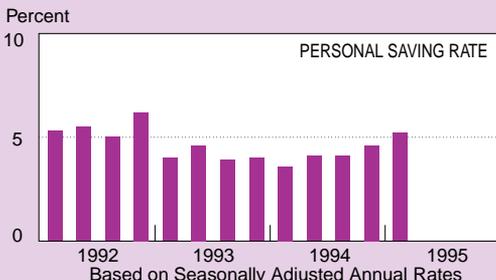
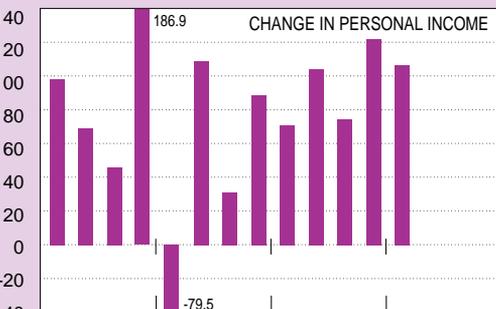
	Level	Change from preceding quarter			
		1995: I	1994		
			II	III	IV
					1995: I
Wage and salary disbursements	3,403.2	48.9	36.7	62.5	46.8
Commodity-producing industries	848.8	9.7	10.2	15.5	11.5
Manufacturing	638.8	3.4	5.5	11.2	9.3
Other	210.0	6.3	4.7	4.3	2.2
Distributive industries	778.8	13.9	11.0	16.1	9.2
Service industries	1,160.0	19.2	13.1	26.2	19.5
Government and government enterprises	615.6	6.2	2.5	4.6	6.6
Other labor income	399.6	5.2	5.3	5.0	10.9
Proprietors' income	493.8	.3	-4.3	18.7	8.1
Farm	45.1	-7.9	-9.5	11.9	3.4
Nonfarm	448.7	8.1	5.2	6.9	4.7
Rental income of persons	25.6	18.8	-1.5	-3.6	-3.4
Personal dividend income	205.5	6.0	5.2	5.8	2.8
Personal interest income	724.5	18.3	24.8	26.9	23.4
Transfer payments to persons	1,004.6	10.2	11.4	10.7	24.9
Less: Personal contributions for social insurance	293.7	3.6	3.0	3.7	7.1
Personal income	5,963.1	104.1	74.6	122.1	106.5
Less: Personal tax and nontax payments	774.3	23.4	-2.3	10.6	19.6
Equals: Disposable personal income	5,188.8	80.7	76.8	111.6	86.9
Less: Personal outlays	4,918.8	55.1	74.6	82.3	49.5
Equals: Personal saving	270.0	25.6	2.2	29.3	37.4
Addenda: Special factors in personal income:					
In wages and salaries:					
Federal Government and Postal Service pay adjustments, including "buyouts"		1.5	-1.5	.8	2.9
Profit sharing and bonus pay		-2.1	0	3.0	2.7
In other labor income:					
Employer pension contributions		0	0	0	6.3
In farm proprietors' income:					
Agricultural subsidy payments		-2.9	-7.3	7.2	2.2
In transfer payments to persons:					
Social security retroactive payments .....		.1	-1	1.2	-1.2
Cost-of-living increases in Federal transfer payments		0	0	0	10.2
Earned Income Tax Credit payments		0	0	0	5.1
In personal contributions for social insurance:					
Social security rate and base changes and increase in premium for supplementary medical insurance and in medicare taxable wage base		0	0	0	3.9

NOTE.—Most dollar levels are found in NIPA table 2.1.
IVA Inventory valuation adjustment
CCAdj Capital consumption adjustment

CHART 3

Selected Personal Income and Saving Measures

Billions \$



Note—Changes are from preceding quarter.

U.S. Department of Commerce, Bureau of Economic Analysis

BEA Estimates of Wages and Salaries for 1994

The annual change from 1993 to 1994 in the national income and product accounts (NIPA's) estimate of wage and salary disbursements is about \$14 billion more than the change in the U.S. total of the State estimates that appear in this issue of the SURVEY OF CURRENT BUSINESS. As explained below, the difference mainly reflects the incorporation in the State estimates of newly available source data that are more accurate and more comprehensive; these data will be incorporated into the NIPA's in the upcoming comprehensive revision.

The NIPA estimate for 1994, which appears in table 2.1 of the "Selected NIPA Tables," is based primarily on national data on (1) total employment and (2) average weekly hours and average hourly earnings of production and nonsupervisory workers; the data are from the Bureau of Labor Statistics (BLS) monthly establishment survey. The State estimates for 1994 are based primarily

on BLS tabulations of wages and salaries of employees covered by unemployment insurance tabulations for the first three quarters and on BEA estimates for the fourth quarter. (The U.S. total of the State estimates for the first three quarters of 1994 published in the January 1995 SURVEY was based primarily on the monthly national establishment survey data.)

In July, as part of the regular quarterly revision of State personal income, the 1994 State estimates will be revised to incorporate the fourth-quarter 1994 unemployment-insurance tabulations. In December, as part of the comprehensive revision of the NIPA's, the 1994 national estimate will be revised to incorporate the four quarters of unemployment-insurance tabulations.¹

1. These tabulations would usually be incorporated into the NIPA estimates in July as part of the annual NIPA revision; however, this year's annual revision will be combined with the comprehensive NIPA revision.

down was the result of a modest downturn in average weekly hours and a slowing in average hourly earnings. In government, a pay raise for Federal civilian and military employees more than accounted for the acceleration.

Farm proprietors' income increased \$3.4 billion after increasing \$11.9 billion. Farm subsidies increased \$2.2 billion after increasing \$7.2 billion; the slowdown reflected smaller payments made under the Conservation Reserve Program. Other farm income increased \$1.2 billion after increasing \$4.7 billion; the slowdown reflected downturns in crop output and crop prices.

Personal interest income and nonfarm proprietors' income increased somewhat less than in the fourth quarter. Rental income decreased about as much as in the fourth quarter.

Other labor income increased \$10.9 billion after increasing \$5.0 billion; the first-quarter increase reflected the inclusion of a \$6.3 billion pension plan contribution by a motor vehicle manufacturing firm.

Transfer payments to persons increased \$24.9 billion after increasing \$10.7 billion. The step-up reflected cost-of-living adjustments to benefits under social security and other Federal retirement and income support programs, increases in veterans compensation and benefits, and increases in Earned Income Tax Credit program payments.

Personal tax and nontax payments increased \$19.6 billion after increasing \$10.6 billion. The first-quarter step-up primarily reflected 1995 payments for 1994 income tax liabilities, which had been increased by provisions of the Omnibus Budget Reconciliation Act of 1993.

Corporate Profits and Property Income in 1994

Profits from current production increased \$56.9 billion in 1994, to \$542.7 billion, after increasing \$80.7 billion in 1993 (table 7).²

2. Profits from current production is estimated as the sum of profits before tax, the inventory valuation adjustment (IVA), and the capital consumption adjustment (CCAdj); it is shown in NIPA tables 1.14, 1.16, and 6.16C as "Corporate profits with IVA and CCAdj."

Table 7.—Corporate Profits

	Level		Change from preceding year
	1995	1994	1995
	Billions of dollars		
Profits from current production	542.7	80.7	56.9
Domestic industries	482.3	76.0	61.8
Financial	88.3	21.6	-1.2
Nonfinancial	394.0	54.3	63.1
Rest of the world	60.5	4.7	-4.8
IVA	-19.5	.2	-13.3
CCAdj	37.7	13.8	8.2
Profits before tax	524.5	66.5	62.1
Profits tax liability	202.5	33.5	29.3
Profits after tax	322.0	33.0	32.8
Cash flow from current production	567.3	37.6	38.6
Profits by industry:			
Corporate profits with IVA	505.0	66.8	48.8
Domestic industries	444.6	62.2	53.6
Financial	104.0	21.8	.3
Nonfinancial	340.6	40.4	53.3
Manufacturing	145.6	19.7	31.4
Trade	67.6	6.4	6.4
Transportation and public utilities	72.3	9.4	7.3
Other	55.1	4.9	8.2
Rest of the world	60.5	4.7	-4.8
Receipts (inflows)	84.2	8.8	10.0
Payments (outflows)	23.7	4.1	14.8
	Dollars		
Unit price, costs, and profits of domestic nonfinancial corporations:			
Unit price	1.171	.009	.012
Unit labor cost .....	.766	.001	-.002
Unit nonlabor cost .....	.278	-.005	-.001
Unit profits from current production .....	.126	.013	.014

NOTE.—Levels of these and other profits series are found in NIPA tables 1.14, 1.16, 6.16C, and 7.15.

IVA Inventory valuation adjustment

CCAdj Capital consumption adjustment

Profits from the domestic operations of nonfinancial corporations increased \$63.1 billion after increasing \$54.3 billion. Real gross product of these corporations increased 6.1 percent after increasing 5.0 percent, and profits per unit of real product increased substantially in both years.

Profits from the domestic operations of financial corporations decreased \$1.2 billion after increasing \$21.6 billion. Profits from the rest of the world decreased \$4.8 billion after increasing \$4.7 billion in 1993.

Cash flow from current production, a profits-related measure of internally generated funds available to corporations for investment, increased \$38.6 billion, up slightly from 1993. However, cash flow as a percentage of nonresidential fixed investment—an indication of the adequacy of internally generated funds—was 81.3 percent in 1994, down from 85.8 percent in 1993 but still

much higher than its 72.1-percent average in the 1980's.

Industry profits show a picture similar to that shown by current-production measures.³ Profits from domestic operations of nonfinancial corporations increased more than in 1993; profits from domestic operations of financial corporations changed little after a large increase; and profits from the rest of the world turned down. Most of the step-up in nonfinancial profits was accounted for by manufacturing industries, especially by manufacturers of electronic equipment, of food, and of "other nondurable goods." Petroleum refiners posted the biggest slowdown among manufacturing industries. In contrast to the step-up in manufacturing profits, profits in trade increased the same amount as in 1993, and profits

3. Industry profits are estimated as the sum of profits before tax and the inventory valuation adjustment; they are shown in NIPA table 6.16C. Estimates of the capital consumption adjustment by industry do not exist.

Rates of Return

The rate of return discussed in the text (beginning on page 9) is measured as the ratio of property income to the value of net reproducible assets. Property income is the sum of profits from current production—corporate profits with inventory valuation adjustment and capital consumption adjustment—and net interest payments. Net reproducible tangible assets consist of fixed capital stock and inventories; both are measured at current replacement cost.

A rate of return calculated in this way has several attractive features. First, by using property income in the numerator, it captures the total return to investment—regardless of whether the investment is financed out of equity or debt. Second, because this numerator reflects the current replacement costs of inventory withdrawals and of capital used up in production, it is not distorted by inventory "profits" and spurious "profits" resulting from over- or under-depreciation of capital. Third, because the denominator is measured at current replacement cost—that is, because assets are valued at the prices that would have been paid for them if they had been purchased new in the period to which the stock estimates refer—the rate of return is an estimate of the current average profitability of investment.

Rates of return are sometimes calculated in other ways; the following paragraphs describe several.

The income measure in the numerator of the ratio can be defined exclusive of net interest or in terms of some measure other than the current-production variant for profits. For example, the numerator could be profits after tax or retained earnings, and these incomes can be measured with or without inventory valuation and capital consumption adjustments.

The denominator can include the net capital stock valued at *historical* cost, that is, at the prices at which the assets were purchased when new.

However, historical-cost estimates are problematic because they treat a dollar of capital stock purchased in 1970 as equivalent to a dollar of capital stock purchased in 1990; the estimates do not incorporate any adjustment for changes in the price level. Moreover, for companies that use the last-in-first-out (LIFO) method of inventory accounting, historical-cost valuation of inventories is not feasible; this part of inventories can only be valued at replacement cost.¹ If one assumes that the historical cost and replacement cost of LIFO inventories are equal, then historical-cost rates of return can be calculated. Until recently, historical cost rates have generally been substantially higher than replacement cost rates; in 1988, for example, the historical-cost rate was 5.5 percentage points higher than the replacement-cost rate of return. By 1994, however, the two rates were virtually identical at 10.2 percent. The convergence of these rates, of course, reflects a convergence of the historical-cost and replacement-cost estimates of the capital stock: In recent years, increases in the prices of many assets, which would make replacement costs higher than historical costs, have been largely offset by decreases in computer prices.

The denominator need not be limited to reproducible assets. For example, land (including subsoil resources), goodwill, and intellectual property might also be included. Alternatively, rates of return on stockholders' equity and on sales can be calculated, as is done for mining, manufacturing, retail trade, and wholesale trade corporations by the Census Bureau in the *Quarterly Financial Report (QFR)*. (QFR measures of book profits, not profits from current production, are used in the numerators.)

1. The Census Bureau's *Quarterly Financial Report* contains estimates of fixed assets based on historical costs and total inventories based on a mixture of accounting methods.

in the transportation and public utilities group slowed.

About two-thirds of the sharp slowdown in financial profits reflected insurance company profits. Insurance profits decreased in 1994, as a result of the earthquake that struck Northridge, California, in January of that year; that decrease came on the heels of a sharp 1993 increase that represented a rebound from the impact of Hurricanes Andrew and Iniki.

Profits from the rest of the world decreased \$4.8 billion after increasing \$4.7 billion. This component of profits measures receipts of profits from foreign affiliates of U.S. corporations less payments of profits by U.S. affiliates of foreign corporations. Receipts increased slightly more than in 1993, but payments increased much more than in 1993, reflecting a step-up in the growth of the U.S. economy. Manufacturing affiliates dominated the receipts picture, while most of the step-up in payments was concentrated in manufacturing, wholesale trade, and banking.

Related measures.—Profits before tax increased \$62.1 billion. The difference between this increase and the \$56.9 billion increase in profits from current production reflects a decrease in the IVA that was only partly offset by an increase in the CCADj.

The IVA is an estimate of the inventory profits (with the sign reversed) that are included in PBT. Inventory profits increased \$13.3 billion in 1994.

The CCADj is the difference between the predominantly tax-based depreciation measure that underlies PBT and BEA's estimate of the consump-

tion of fixed capital. The CCADj increased \$8.2 billion in 1994.

Property income

Corporate property income includes net interest payments as well as profits from current production. For domestic nonfinancial corporations, net interest payments increased \$9.2 billion in 1994, to \$123.2 billion, after increasing only \$0.5 billion in 1993.

Chart 4 and table 8 provide a perspective on the recent changes in profits and net interest. From 1970 to 1990, both types of property income trended up. Net interest grew at an average annual rate of 11.4 percent; this rapid growth reflected both increased use of debt by corporations and, until the early 1980's, generally rising inter-

Table 8.—Property Income of Domestic Nonfinancial Corporations and Related Series, 1959–94

[Billions of dollars]

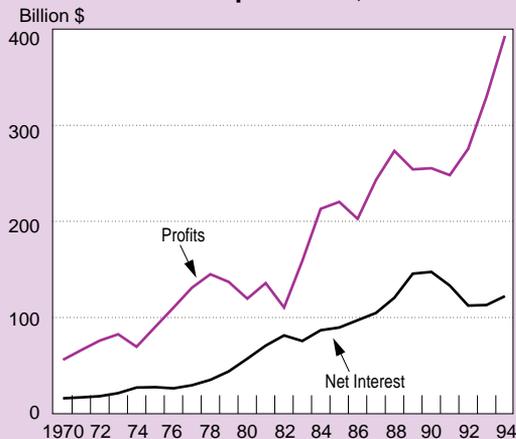
Year	Property income					Domestic income	Net reproducible assets ¹
	Total	Profits from current production			Net interest		
		Total	Profits tax liability	Profits after tax			
(1)	(2)	(3)	(4)	(5)	(6)	(7)	
1959	45.8	42.6	20.7	21.9	3.1	217.2	392.0
1960	43.4	40.0	19.2	20.8	3.5	224.6	406.9
1961	44.7	40.8	19.5	21.3	4.0	230.1	417.7
1962	52.7	48.2	20.6	27.5	4.5	252.8	431.0
1963	58.6	53.8	22.8	31.0	4.8	269.7	448.6
1964	65.4	60.0	24.0	36.1	5.3	292.0	471.0
1965	76.4	70.3	27.2	43.1	6.1	322.8	503.4
1966	82.3	74.9	29.5	45.4	7.4	356.2	551.0
1967	80.5	71.8	27.8	43.9	8.8	372.8	603.9
1968	86.1	76.0	33.6	42.4	10.1	409.3	660.4
1969	84.4	71.3	33.3	37.9	13.2	443.3	729.3
1970	74.2	57.1	27.2	29.9	17.1	452.8	800.2
1971	85.3	67.2	29.9	37.2	18.1	487.3	871.0
1972	96.1	77.0	33.8	43.2	19.2	543.2	955.2
1973	106.0	83.6	40.2	43.4	22.5	612.0	1,076.2
1974	98.9	70.6	42.2	28.4	28.3	655.7	1,273.1
1975	120.2	91.5	41.5	50.0	28.7	700.6	1,468.0
1976	139.0	111.5	53.0	58.5	27.5	795.7	1,612.9
1977	162.6	132.0	59.9	72.1	30.6	904.4	1,779.3
1978	182.4	146.1	67.1	79.0	36.3	1,032.6	2,000.4
1979	183.2	138.1	69.6	68.5	45.1	1,147.4	2,283.1
1980	178.9	120.7	67.0	53.7	58.2	1,232.4	2,606.0
1981	208.9	136.9	63.9	73.0	71.9	1,373.6	2,938.1
1982	194.0	111.5	46.3	65.2	82.5	1,404.0	3,180.3
1983	236.6	159.9	59.4	100.4	76.7	1,508.2	3,300.2
1984	302.2	214.3	73.7	140.7	87.9	1,711.4	3,435.8
1985	312.1	221.4	69.9	151.5	90.7	1,815.3	3,606.7
1986	302.0	203.8	75.6	128.2	98.3	1,883.6	3,744.1
1987	350.0	244.2	93.5	150.8	105.8	2,024.9	3,889.6
1988	396.0	274.4	101.7	172.6	121.6	2,210.2	4,101.4
1989	401.8	255.2	99.5	155.7	146.6	2,322.0	4,327.7
1990	404.9	256.4	93.9	162.6	148.5	2,425.8	4,516.6
1991	383.4	249.2	83.1	166.1	134.2	2,436.5	4,629.2
1992	390.1	276.6	87.8	188.8	113.5	2,541.1	4,699.8
1993	445.0	330.9	116.8	214.1	114.0	2,704.2	4,834.5
1994	517.1	394.0	144.7	249.2	123.2	2,909.1	5,056.4

1. Structures, equipment, and inventories, valued at current replacement cost. Data are averages of end-of-year values for adjacent years.

NOTE.—Property income is profits from current production plus net interest. Profits from current production is corporate profits with inventory valuation adjustment and capital consumption adjustment. Profits after tax is also shown with inventory valuation adjustment and capital consumption adjustment. Current data on most series are shown in table 1.16 of the "Selected NIPA Tables." The value of structures and equipment through 1993 are from *Fixed Reproducible Tangible Wealth in the United States, 1925–89*, (Washington DC: U.S. Government Printing Office, 1993) and from SURVEY OF CURRENT BUSINESS 74(August 1994): 57–58. Data on structures and equipment for 1994 and all data on inventories are unpublished BEA estimates.

CHART 4

Profits From Current Production and Net Interest, Domestic Nonfinancial Corporations, 1970–94



U.S. Department of Commerce, Bureau of Economic Analysis

est rates. Profits grew substantially slower—7.8 percent, on average. As a result, the share of net interest in property income rose from 23.0 percent in 1970 to 36.7 percent in 1990.

In the 1990's, these trends ended: Net interest decreased substantially in 1991 and 1992 and changed little in 1993 before increasing in 1994. The weakness in net interest reflected the ebbing of the wave of leveraged buyouts that were so prominent in the 1980's, the efforts by corporations to reduce indebtedness, and, through 1993, falling interest rates. Profits, in contrast, dipped only modestly in 1991 before increasing strongly in the 1992, 1993, and 1994. As a consequence of these different paths, the share of net interest in property income slid to 23.8 percent in 1994, only a shade higher than it was in 1970.

Further perspective on recent changes in property income can be gained by examining the relationship of property income to the stock of net reproducible assets and to domestic income. Net reproducible assets consist of fixed capital stock and inventories. Measured at current replacement cost, these assets increased 4.6 percent in 1994 after increasing 2.9 percent in 1993. From

1970 to 1990, in contrast, these assets had grown much faster—at an average rate of 9.0 percent. Domestic income of corporations—which consists of property income plus compensation of employees—increased 7.6 percent in 1994 after increasing 6.4 percent in 1993.

The ratio of property income to the stock of net reproducible assets is the average rate of return on these assets (see box on page 7). The use of property income, rather than profits alone, as the numerator of this ratio captures the total return to investment (profits plus interest) regardless of whether the investment was financed by equity or by debt.

The ratio of property income to domestic income is property income's share of domestic income—that is, the fraction of domestic income

Table 9.—Rate of Return, Income Share, and Average Product of Capital, Domestic Nonfinancial Corporations, 1959–94

[Percent]

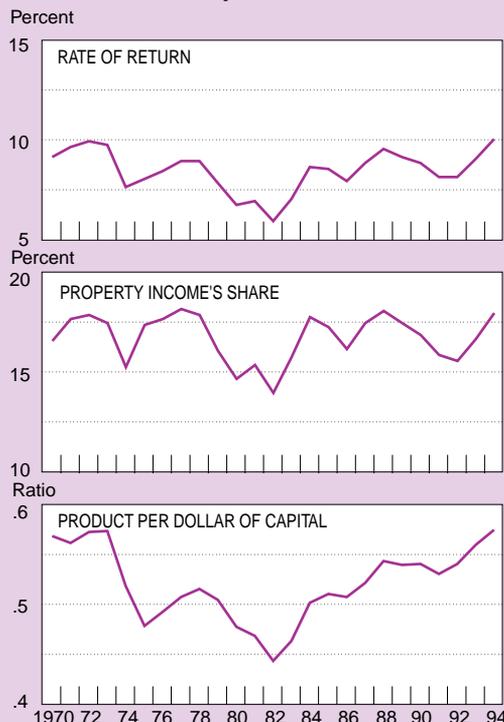
Year	Rate of return					Share of domestic income			Average product of capital
	Property income					Property income			
	Total	Profits from current production		Net interest	Total	Profits from current production	Net interest		
		Total	Profits tax liability					Profits after tax	
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	
1959	11.7	10.9	5.3	5.6	0.8	21.1	19.6	1.4	0.555
1960	10.7	9.8	4.7	5.1	.9	19.3	17.8	1.5	.554
1961	10.7	9.8	4.7	5.1	.9	19.4	17.7	1.7	.552
1962	12.2	11.2	4.8	6.4	1.1	20.8	19.1	1.8	.587
1963	13.1	12.0	5.1	6.9	1.1	21.7	19.9	1.8	.604
1964	13.9	12.7	5.1	7.7	1.1	22.4	20.6	1.8	.621
1965	15.2	14.0	5.4	8.6	1.2	23.7	21.8	1.9	.641
1966	14.9	13.6	5.4	8.2	1.3	23.1	21.0	2.1	.645
1967	13.3	11.9	4.6	7.3	1.5	21.6	19.2	2.4	.616
1968	13.0	11.5	5.1	6.4	1.5	21.0	18.6	2.5	.619
1969	11.6	9.8	4.6	5.2	1.8	19.0	16.1	3.0	.611
1970	9.3	7.1	3.4	3.7	2.1	16.4	12.6	3.8	.567
1971	9.8	7.7	3.4	4.3	2.1	17.5	13.8	3.7	.560
1972	10.1	8.1	3.5	4.5	2.0	17.7	14.2	3.5	.571
1973	9.9	7.8	3.7	4.0	2.1	17.3	13.7	3.7	.572
1974	7.8	5.5	3.3	2.2	2.2	15.1	10.8	4.3	.517
1975	8.2	6.2	2.8	3.4	2.0	17.2	13.1	4.1	.477
1976	8.6	6.9	3.3	3.6	1.7	17.5	14.0	3.5	.491
1977	9.1	7.4	3.4	4.1	1.7	18.0	14.6	3.4	.506
1978	9.1	7.3	3.4	3.9	1.8	17.7	14.1	3.5	.514
1979	8.0	6.0	3.0	3.0	2.0	15.9	12.0	3.9	.503
1980	6.9	4.6	2.6	2.1	2.2	14.5	9.8	4.7	.476
1981	7.1	4.7	2.2	2.5	2.4	15.2	9.9	5.2	.467
1982	6.1	3.5	1.5	2.1	2.6	13.8	7.9	5.9	.442
1983	7.2	4.8	1.8	3.0	2.3	15.6	10.6	5.1	.462
1984	8.8	6.2	2.1	4.1	2.6	17.6	12.5	5.1	.500
1985	8.7	6.1	1.9	4.2	2.5	17.1	12.2	5.0	.509
1986	8.1	5.4	2.0	3.4	2.6	16.0	10.8	5.2	.506
1987	9.0	6.3	2.4	3.9	2.7	17.3	12.1	5.2	.520
1988	9.7	6.7	2.5	4.2	3.0	17.9	12.4	5.5	.542
1989	9.3	5.9	2.3	3.6	3.4	17.3	11.0	6.3	.538
1990	9.0	5.7	2.1	3.6	3.3	16.7	10.6	6.1	.539
1991	8.3	5.4	1.8	3.6	2.9	15.7	10.2	5.5	.529
1992	8.3	5.9	1.9	4.0	2.4	15.4	10.9	4.5	.539
1993	9.2	6.8	2.4	4.4	2.4	16.5	12.2	4.2	.558
1994	10.2	7.8	2.9	4.9	2.4	17.8	13.5	4.2	.573

Source: Table 8.

NOTE.—Columns 1–5 are percentages of the stock of net reproducible assets (structures, equipment, and inventories) valued at current replacement cost. Columns 6–8 are percentages of domestic income. Column 9 is calculated as the ratio of column 1 to column 6.

CHART 5

Selected Ratios, Domestic Nonfinancial Corporations, 1970–94



that is not used to compensate labor. Property income's share is related to the rate of return by a third ratio—the ratio of domestic income to the value of net reproducible assets, which measures the average annual product per dollar of capital.⁴

The three ratios are plotted for 1970–94 in [chart 5](#) and are reported, along with related ratios, for 1959–94 in [table 9](#). Property income's rate of return (column 1) and its share of do-

mestic income (column 6) appear to have shifted to lower levels around 1970. The rate of return fell from an average of 12.8 percent in 1959–69 to an average of 8.6 percent in 1970–94; the share of domestic income fell from an average of 21.2 percent to an average of 16.6 percent.

In 1994, property income's rate of return and its share of domestic income continued to rebound from cyclical decreases in 1991. Higher profits were responsible for the rebounds in both ratios. 

4. It should be noted that this ratio is not appropriate for use in productivity analysis; for productivity analysis, the denominator should measure capital services, not capital stock.

Comprehensive Revision of the NIPA's

Revised and updated estimates of the national income and product accounts (NIPA's) resulting from a comprehensive, or benchmark, revision are scheduled for release in late 1995. These estimates will incorporate statistical revisions resulting from (1) newly available source data, such as the 1987 benchmark input-output tables, the 1992 Economic Censuses, and several annual surveys for 1993 and 1994 and (2) changes in methodology. The estimates will also reflect changes in definitions and classifications. (For additional information, see "Mid-Decade Strategic Review of BEA's Economic Accounts: An Update" in this

issue.) In addition, table formats will be revised, and new series will be presented. The changes to be introduced in the comprehensive revision will be described in upcoming articles in the SURVEY OF CURRENT BUSINESS.

In general, the statistical revisions will affect the estimates back to 1983, but the changes in definitions and classifications will affect the estimates as far back as necessary. The estimates released in late 1995 will be limited to 1959 forward and will consist only of those usually shown in July SURVEY tables; estimates for earlier periods will be released during 1996.