

BUSINESS SITUATION

Ralph W. Morris prepared the first section of this article, and Daniel Larkins prepared the section on corporate profits.

REAL gross domestic product (GDP) increased 2.2 percent in the third quarter of 2000, according to the "final" estimates of the national income and product accounts (NIPAs), after increasing 5.6 percent in the second quarter (table 1 and chart 1).¹ The 2.2-percent increase in the third quarter was the smallest increase in 4 years and was well below the 3.7-percent average annual growth rate over the current expansion, which began in the second quarter of 1991.

The growth in real GDP reflected growth in both domestic and foreign demand. Domestic demand (gross domestic purchases) increased 3.0 percent, and foreign demand (exports of goods

and services) increased 13.9 percent (table 2).² The increase in domestic demand reflected increases in consumer spending and business fixed investment

2. Gross domestic purchases—a measure of purchases by U.S. residents regardless of where the purchased goods and services were produced—is calculated as the sum of personal consumption expenditures, gross private domestic investment, and government consumption expenditures and gross investment.

1. Quarterly estimates in the NIPAs are expressed at seasonally adjusted annual rates. Quarter-to-quarter dollar changes are the differences between the published estimates. Quarter-to-quarter percent changes are annualized and are calculated from unrounded data unless otherwise specified.

Real estimates are calculated using a chain-type Fisher formula with annual weights for all years and quarterly weights for all quarters; real estimates are expressed both as index numbers (1996=100) and as chained (1996) dollars. Price indexes (1996=100) are also calculated using a chain-type Fisher formula.

Table 1.—Real Gross Domestic Product, Real Gross Domestic Purchases, and Real Final Sales to Domestic Purchasers

[Seasonally adjusted at annual rates]

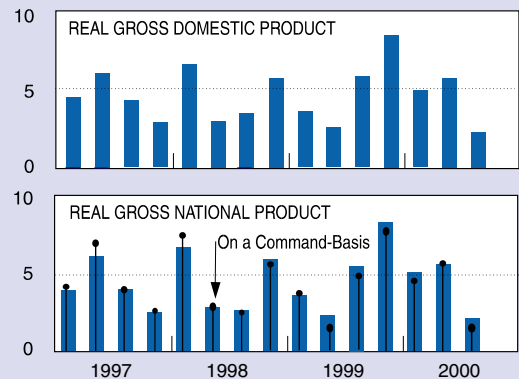
	Billions of chained (1996) dollars					Percent change from preceding quarter			
	Level	Change from preceding quarter				1999		2000	
		2000	1999	2000			IV	I	II
		III	IV	I	II	III			
Gross domestic product	9,369.5	178.3	107.7	127.1	50.6	8.3	4.8	5.6	2.2
Less: Exports of goods and services	1,158.8	25.8	16.4	37.0	37.0	10.3	6.3	14.3	13.9
Plus: Imports of goods and services	1,586.4	35.7	40.8	63.5	61.2	10.7	12.0	18.6	17.0
Equals: Gross domestic purchases	9,766.0	187.4	129.5	150.7	71.7	8.4	5.6	6.5	3.0
Less: Change in private inventories	72.5	41.8	-44.3	42.0	-6.1				
Nonfarm	67.4	29.5	-40.0	39.3	-4.9				
Farm	5.0	12.9	-4.3	2.6	-1.2				
Equals: Final sales to domestic purchasers	9,687.3	147.6	169.5	110.6	76.8	6.6	7.5	4.7	3.2
Personal consumption expenditures	6,329.8	87.2	112.5	47.1	69.2	5.9	7.6	3.1	4.5
Durable goods	903.2	25.6	46.4	-11.5	16.5	13.0	23.6	-5.0	7.6
Nondurable goods	1,882.6	32.0	26.7	16.3	21.5	7.4	6.0	3.6	4.7
Services	3,559.3	31.9	44.2	39.5	32.6	3.8	5.2	4.6	3.7
Private fixed investment	1,791.3	28.8	64.3	46.7	13.7	7.2	16.4	11.2	3.1
Nonresidential	1,438.8	29.3	63.5	47.2	26.3	9.5	21.0	14.6	7.7
Structures	286.6	6.0	13.4	3.0	9.6	9.7	22.3	4.4	14.6
Equipment and software	1,162.4	23.5	50.3	46.2	15.8	9.5	20.6	17.9	5.6
Residential	362.3	.5	2.9	1.2	-10.3	.5	3.2	1.3	-10.6
Government consumption expenditures and gross investment	1,578.2	31.7	-4.4	18.6	-5.5	8.5	-1.1	4.8	-1.4
Federal	545.8	17.1	-21.0	21.7	-13.0	13.2	-14.2	17.2	-9.0
National defense	346.2	10.5	-19.4	13.6	-8.9	12.6	-19.8	16.9	-9.7
Nondefense	199.4	6.6	-1.7	8.2	-4.2	14.4	-3.3	17.8	-7.9
State and local	1,031.9	14.8	16.2	-2.8	7.3	6.1	6.6	-1.1	2.9
Addendum: Final sales of domestic product	9,290.9	138.7	147.5	87.3	55.6	6.4	6.7	3.9	2.4

NOTE.—Chained (1996) dollar series are calculated as the product of the chain-type quantity index and the 1996 current-dollar value of the corresponding series, divided by 100. Because the formula for the chain-type quantity indexes uses weights of more than one period, the corresponding chained-dollar estimates usually are not additive. Chained (1996) dollar levels and residuals, which measure the extent of nonadditivity in each table, are shown in NIPA tables 1.2, 1.4, and 1.6. Percent changes are calculated from unrounded data. Percent changes in major aggregates are shown in NIPA table S.1. (See "Selected NIPA Tables," which begins on page D-2 in this issue.)

CHART 1

Selected Product Measures: Change from Preceding Quarter

Percent



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

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

Table 2.—Contributions to Percent Change in Real Gross Domestic Product

[Seasonally adjusted at annual rates]

	1999		2000	
	IV	I	II	III
Percent change at annual rate:				
Gross domestic product	8.3	4.8	5.6	2.2
Percentage points at annual rates:				
Personal consumption expenditures	4.08	5.03	2.14	2.99
Durable goods	1.04	1.79	-.42	.61
Nondurable goods	1.47	1.19	.74	.93
Services	1.58	2.04	1.83	1.46
Gross private domestic investment	3.04	.92	3.66	.33
Fixed investment	1.26	2.68	1.93	.55
Nonresidential	1.22	2.54	1.87	1.02
Structures .....	.29	.63	.14	.44
Equipment and software .....	.94	1.91	1.73	.58
Residential .....	.03	.14	.06	-.47
Change in private inventories	1.78	-1.76	1.73	-.22
Net exports of goods and services	-.37	-.94	-1.00	-.90
Exports	1.09	.67	1.48	1.45
Goods .....	.94	.46	1.37	1.54
Services .....	.15	.21	.11	-.09
Imports	-1.45	-1.61	-2.48	-2.35
Goods	-1.28	-1.28	-2.26	-1.90
Services	-.17	-.33	-.22	-.44
Government consumption expenditures and gross investment	1.50	-.18	.85	-.24
Federal .....	.79	-.93	.97	-.57
National defense .....	.48	-.86	.60	-.38
Nondefense .....	.30	-.07	.37	-.18
State and local .....	.71	.75	-.12	.33

NOTE.—More detailed contributions to percent change in real gross domestic product are shown in NIPA table 8.2. Contributions to percent change in major components of real gross domestic product are shown in tables 8.3 through 8.6.

that were partly offset by decreases in private residential investment, Federal Government spending, and private inventory investment.³ The increase in domestic demand also reflected a 17.0-percent increase in imports of goods and services.

The deceleration in real GDP growth in the third quarter reflected downturns in private inventory investment, in Federal Government spending, and in private residential investment and a sharp deceleration in business investment in equipment

3. In the NIPAs, consumer spending is shown as personal consumption expenditures and government spending is shown as government consumption expenditures and gross investment.

Table 3.—Revisions to Change in Real Gross Domestic Product and Prices, Third Quarter 2000

[Seasonally adjusted at annual rates]

	Percent change from preceding quarter		Final estimate minus preliminary estimate	
	Preliminary estimate	Final estimate	Percentage points	Billions of chained (1996) dollars
Gross domestic product	2.4	2.2	-0.2	-4.0
Less: Exports of goods and services	15.4	13.9	-1.5	-3.9
Goods	19.8	21.0	1.2	2.1
Services	4.8	-2.8	-7.6	-5.5
Plus: Imports of goods and services	17.4	17.0	-.4	-1.3
Goods	16.6	16.2	-.4	-1.4
Services	22.1	22.3	.2	.1
Equals: Gross domestic purchases	3.1	3.0	-.1	-1.7
Less: Change in private inventories				-1.0
Farm				0
Nonfarm				-1.0
Equals: Final sales to domestic purchasers	3.3	3.2	-.1	-8
Personal consumption expenditures	4.5	4.5	0	-.7
Durable goods	8.1	7.6	-.5	-.9
Nondurable goods	4.8	4.7	-.1	-.5
Services	3.7	3.7	0	.6
Fixed investment	3.3	3.1	-.2	-.6
Nonresidential	7.8	7.7	-.1	-.6
Structures	14.9	14.6	-.3	-.2
Equipment and software	5.8	5.6	-.2	-.3
Residential	-10.5	-10.6	-.1	0
Government consumption expenditures and gross investment	-1.5	-1.4	.1	.5
Federal	-9.0	-9.0	0	0
National defense	-9.6	-9.7	-.1	0
Nondefense	-8.0	-7.9	.1	0
State and local	2.7	2.9	.2	.5
Addenda:				
Final sales of domestic product	2.6	2.4	-.2	-3.2
Gross domestic purchases price index	2.3	2.0	-.3	
GDP price index	1.9	1.6	-.3	

NOTE.—The final estimates for the third quarter of 2000 incorporate the following revised or additional major source data that were not available when the preliminary estimates were prepared.

Personal consumption expenditures: Revised retail sales for September and newly available brokerage services data for the third quarter.

Nonresidential fixed investment: Revised construction put-in-place for August and September, revised manufacturers' shipments of machinery and equipment for September, and newly available unemployment insurance data for the second quarter.

Residential fixed investment: Revised construction put-in-place for August and September and revised sales of new houses for July through September.

Change in private inventories: Revised manufacturing and trade inventories for September.

Exports and imports of goods and services: Revised data on exports and imports of goods for September and revised international transactions data on exports and imports of services for the second and third quarters.

Government consumption expenditures and gross investment: Revised State and local construction put-in-place for August and September.

Wages and salaries: Revised employment, average hourly earnings, and average weekly hours for August and September.

GDP prices: Revised export and import prices for June through September, revised unit-value index for petroleum imports for September, and revised prices of single-family houses under construction for the quarter.

and software. These changes were partly offset by an acceleration in consumer spending and an upturn in State and local government spending.

The final estimate of the change in real GDP is 0.2 percentage point less than the 2.4-percent increase indicated by the "preliminary" estimate reported in the December "Business Situation" (table 3). For 1978–99, the average revision (without regard to sign) from the preliminary estimate to the final estimate was 0.3 percentage point. The downward revision to third-quarter real GDP primarily reflected a downward revision to exports of goods and services, as a downward revision to services more than offset an upward revision to goods. The downward revision to exports of services reflected the incorporation of newly available quarterly data from BEA's international transactions accounts; the upward revision to exports of goods reflected the incorporation of revised Census Bureau data for September.

Real gross domestic purchases increased 3.0 percent, 0.1 percentage point less than the preliminary estimate; in the second quarter, this measure increased 6.5 percent. Real final sales of domestic product increased 2.4 percent, 0.2 percentage point less than the preliminary estimate; in the second quarter, this measure increased 3.9 percent.⁴

The prices of gross domestic purchases increased 2.0 percent, 0.3 percentage point less than the preliminary estimate; in the second quarter, these prices increased 2.1 percent. The downward revision primarily reflected downward revisions to the prices of "other" personal consumption expenditures (PCE) for services, specifically, revisions to the implicit prices of imputed financial charges that resulted from the incorporation of newly available data from the Federal Deposit Insurance Corporation. GDP prices increased 1.6 percent in the third quarter, also 0.3 percentage point less than the preliminary estimate; in the second quarter, GDP prices increased 2.4 percent.

Real disposable personal income (DPI) increased 2.6 percent in the third quarter, 0.2 percentage point more than the preliminary estimate; in the second quarter, real DPI increased 3.7 percent. Current-dollar DPI increased 4.4 percent in the third quarter, 0.2 percentage point less than the preliminary estimate; the downward revision was

4. Final sales of domestic product is calculated as GDP less change in private inventories.

more than accounted for by a downward revision to personal interest income, reflecting the incorporation of newly available data from the Federal Deposit Insurance Corporation. The upward revision to real DPI reflected the downward revision to the implicit price deflator for PCE, which is used to deflate current-dollar DPI.

The personal saving rate—personal saving as a percentage of current-dollar DPI—was -0.2 percent, the same as the preliminary estimate; in the second quarter, the rate was 0.3 percent.

Gross national product (GNP).—In the third quarter, real GNP—goods and services produced by labor and property supplied by U.S. residents—increased 2.1 percent, 0.1 percentage point less than real GDP (table 4).⁵ Income receipts from the rest of the world decreased more than income payments to the rest of the world; both decreases reflected corporate profits.

Real GNP on a command basis, which measures the purchasing power of goods and services produced by the U.S. economy, increased less than real GNP—1.8 percent, compared with 2.1 percent—reflecting a deterioration in the terms of trade.⁶ In the second quarter, real GNP on a command basis increased more than real GNP—5.9 percent, compared with 5.6 percent—reflecting an improvement in the terms of trade. The terms of trade had deteriorated in each of the preceding four quarters.

5. GNP equals GDP plus income receipts from the rest of the world less income payments to the rest of the world.

The national saving rate—gross saving as a percentage of GNP—was 18.5 percent in the third quarter, down slightly from 18.6 percent in the second quarter. The national saving rate has ranged from 18.2 to 18.6 percent in the last six quarters after ranging from 18.7 to 19.0 percent in the preceding five quarters.

Corporate Profits

According to revised estimates, profits from current production increased \$6.7 billion (or 0.7 percent at a quarterly rate) in the third quarter after increasing \$27.3 billion (2.9 percent) in the second quarter (table 5).⁷

Profits from the rest of the world increased \$7.8 billion (5.8 percent) in the third quarter, as pay-

6. In the estimates of command-basis GNP, the current-dollar value of the sum of exports of goods and services and income receipts is deflated by the implicit price deflator (IPD) for the sum of imports of goods and services and income payments.

The terms of trade is a measure of the relationship between the prices that are received by U.S. producers for exports of goods and services and the prices that are paid by U.S. purchasers for imports of goods and services. It is measured by the following ratio, with the decimal point shifted two places to the right: In the numerator, the IPD for the sum of exports of goods and services and of income receipts; in the denominator, the IPD for the sum of imports of goods and services and of income payments.

Changes in the terms of trade reflect the interaction of several factors, including movements in exchange rates, changes in the composition of the traded goods and services, and changes in producers' profit margins. For example, if the U.S. dollar depreciates against a foreign currency, a foreign manufacturer may choose to absorb this cost by reducing the profit margin on the product it sells to the United States, or it may choose to raise the price of the product and risk a loss in market share.

7. Profits from current production is estimated as the sum of profits before tax, the inventory valuation adjustment, and the capital consumption adjustment; it is shown in NIPA tables 1.9, 1.14, 1.16, and 6.16C (see "Selected NIPA Tables," which begins on page D-2 of this issue) as corporate profits with inventory valuation and capital consumption adjustments.

Percent changes in profits are shown at quarterly, not annual, rates.

Table 4.—Relation of Real Gross Domestic Product, Real Gross National Product, and Real Command-Basis Gross National Product

[Seasonally adjusted at annual rates]

	Billions of chained (1996) dollars					Percent change from preceding quarter			
	Level		Change from preceding quarter			1999	2000		
	2000	1999	2000				IV	I	II
	III	IV	I	II	III				
Gross domestic product	9,369.5	178.3	107.7	127.1	50.6	8.3	4.8	5.6	2.2
Plus: Income receipts from the rest of the world	348.7	14.3	15.8	21.2	-4.5	20.3	21.6	28.1	-5.0
Less: Income payments to the rest of the world	354.8	13.0	10.8	22.1	-3.1	17.7	14.0	29.1	-3.4
Equals: Gross national product	9,362.8	179.6	112.7	126.0	49.1	8.3	5.1	5.6	2.1
Less: Exports of goods and services and income receipts from the rest of the world	1,508.9	40.6	33.0	58.9	31.4	12.6	9.9	17.7	8.8
Plus: Command-basis exports of goods and services and income receipts from the rest of the world ¹	1,532.8	33.6	24.5	65.5	23.9	10.1	7.1	19.4	6.5
Equals: Command-basis gross national product	9,386.7	172.6	104.2	132.6	41.6	8.0	4.7	5.9	1.8
Addendum: Terms of trade ²	101.6	-6	-7	.4	-5	-2.3	-2.7	1.6	-1.9

1. Exports of goods and services and income receipts deflated by the implicit price deflator for imports of goods and services and income payments.
 2. Ratio of the implicit price deflator for exports of goods and services and income receipts

to the corresponding implicit price deflator for imports divided by 100.
 NOTE. See note to table 1 for an explanation of chained (1996) dollar series. Levels of these series are shown in NIPA tables 1.10 and 1.11.

ments by U.S. affiliates of foreign corporations decreased more than receipts of earnings from foreign affiliates of U.S. corporations.⁸ Profits of domestic financial corporations increased \$6.1 billion (3.6 percent). Profits of domestic nonfinancial corporations decreased \$7.1 billion (1.1 percent). Unit profits of domestic nonfinancial corporations decreased, as unit costs increased more than unit prices; the real product of these corporations increased 1.1 percent (or 4.4 percent at an annual rate).

The revised estimate of profits from current production is \$0.9 billion lower than the preliminary estimate. Profits of domestic nonfinancial corporations were revised down \$5.3 billion; this revision was largely offset by upward revisions to

profits of domestic financial corporations (\$1.7 billion) and to profits from the rest of the world (\$2.7 billion).

Cash flow from current production, a profits-related measure of internally generated funds available for investment, increased \$20.1 billion after increasing \$35.3 billion.⁹ The ratio of cash flow to nonresidential fixed investment—an indicator of the share of the current level of investment that could be financed by internally generated funds—decreased from 74.3 percent to 74.0 percent, its lowest level since 1986.

Domestic industry profits and related measures.—Domestic industry profits increased \$3.9 billion after increasing \$27.7 billion.¹⁰ Profits of domestic

8. Profits from the rest of the world is calculated as (1) receipts by U.S. residents of earnings from their foreign affiliates plus dividends received by U.S. residents from unaffiliated foreign corporations minus (2) payments by U.S. affiliates of earnings to their foreign parents plus dividends paid by U.S. corporations to unaffiliated foreign residents.

These estimates include capital consumption adjustments (but not inventory valuation adjustments) and are derived from BEA's international transactions accounts.

9. Cash flow from current production is undistributed profits with inventory valuation and capital consumption adjustments plus the consumption of fixed capital.

10. Domestic industry profits are estimated as the sum of corporate profits before tax with the inventory valuation adjustment; they are shown in NIPA table 6.16C (on page D-17 of this issue).

Estimates of the capital consumption adjustment do not exist at a detailed industry level; they are available only for the total financial and total nonfinancial industries.

Table 5.—Corporate Profits


[Seasonally adjusted]

	Billions of dollars (annual rate)					Percent change (quarterly rate)				
	Level	Change from preceding quarter				1999	2000			
	2000	1999	2000			IV	I	II	III	
	III	IV	I	II	III					
Profits from current production	970.3	51.2	43.1	27.3	6.7	6.1	4.8	2.9	0.7	
Domestic industries	828.1	42.6	34.7	21.9	-1.2	5.8	4.5	2.7	-1	
Financial	175.2	19.7	4.0	-5.5	6.1	13.1	2.3	-3.2	3.6	
Nonfinancial	653.0	22.9	30.8	27.3	-7.1	3.9	5.1	4.3	-1.1	
Rest of the world	142.1	8.6	8.4	5.4	7.8	7.6	7.0	4.2	5.8	
Receipts (inflows)	202.9	5.3	13.1	12.0	-3.9	3.0	7.2	6.2	-1.9	
Payments (outflows)	60.8	-3.3	4.8	6.5	-11.7	-5.2	7.8	10.0	-16.2	
IVA	-4.5	.5	-5.8	11.4	9.1	.....	.....	.....	.....
CCAdj	29.7	-1.1	-1.0	-5.9	-5.0	.....	.....	.....	.....
Profits before tax	945.1	51.7	50.0	21.8	2.6	6.3	5.7	2.4	.3	
Profits tax liability	290.6	16.6	15.5	5.7	-1.4	6.6	5.7	2.0	-5	
Profits after tax	654.4	35.1	34.5	16.0	4.0	6.2	5.7	2.5	.6	
Cash flow from current production	1,029.6	34.8	37.7	35.3	20.1	3.9	4.0	3.6	2.0	
Domestic industry profits:										
Corporate profits of domestic industries with IVA	798.4	43.6	35.8	27.7	3.9	6.3	4.9	3.6	.5	
Financial	195.5	20.1	4.6	-3.8	7.4	12.0	2.5	-2.0	4.0	
Nonfinancial	602.9	23.6	31.1	31.6	-3.6	4.5	5.7	5.5	-6	
Manufacturing	192.1	-6.8	20.7	8.1	-9.7	-3.8	12.0	4.2	-4.8	
Transportation and public utilities	103.1	12.8	.5	2.0	-8	14.4	.5	2.0	-8	
Wholesale trade	71.1	4.9	2.0	8.5	1.4	9.0	3.3	14.0	1.9	
Retail trade	91.8	6.5	8.3	2.2	-6	8.7	10.1	2.4	-6	
Other	144.9	6.2	-4	10.8	6.2	5.0	-3	8.4	4.5	
	Dollars									
Unit price, costs, and profits of nonfinancial corporations:										
Unit price	1.032	0	0.006	0.006	0.001	.....	.....	.....	.....
Unit labor cost .....	.661	-.003	0	.001	.002	.....	.....	.....	.....
Unit nonlabor cost .....	.247	.001	.002	.002	0	.....	.....	.....	.....
Unit profits from current production .....	.123	.002	.004	.004	-.003	.....	.....	.....	.....

NOTE.—Levels of these and other profits series are in NIPA tables 1.14, 1.16, 6.16C, and 7.15.
IVA Inventory valuation adjustment
CCAdj Capital consumption adjustment

nonfinancial corporations decreased \$3.6 billion after increasing \$31.6 billion. Profits of manufacturing, retail trade, and the transportation and utilities group turned down, and profits of wholesale trade and “other nonmanufacturing” increased less than in the second quarter.¹¹ The downturn in manufacturing was largely accounted for by chemicals, petroleum, and electronic equipment. Profits of domestic financial corporations increased \$7.4 billion after decreasing \$3.8 billion.

Profits before tax (PBT) increased \$2.6 billion after increasing \$21.8 billion. For the third quarter, the difference between the increase in PBT and the

increase in profits from current production reflected an increase in the inventory valuation adjustment that was partly offset by a decrease in the capital consumption adjustment.¹² 

12. As prices change, companies that value inventory withdrawals at original acquisition (historical) costs may realize inventory profits or losses. Inventory profits—a capital-gains-like element in profits—result from an increase in inventory prices, and inventory losses—a capital-loss-like element in profits—result from a decrease in inventory prices. In the NIPA's, inventory profits or losses are removed from business incomes by the inventory valuation adjustment (IVA); a negative IVA removes inventory profits, and a positive IVA removes inventory losses.

The capital consumption adjustment converts depreciation of fixed assets valued at historical cost and based on service lives and depreciation patterns specified in the tax code to depreciation valued at replacement cost and based on empirical evidence on the prices of used equipment and structures in resale markets. For more information on depreciation in the NIPAs, see Shelby W. Herman, “Fixed Assets and Consumer Durable Goods: Estimates for 1925–98,” *SURVEY OF CURRENT BUSINESS* 80 (April 2000): 17–30.

11. “Other nonmanufacturing” industries include agriculture, mining, construction, and services.