



## **Busy Economic Week: GDP Growth, the Fed, and the Budget**

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The past week was momentous for the U.S. economy.

First, preliminary estimates for fourth quarter growth in real gross domestic product were a decent 4 percent. This was well below consensus estimates and sharply lower than the 8.2 percent pace posted in the third quarter. While it is likely that this advance estimate will be revised upward, it was still a bit disappointing. Consumption spending slowed dramatically from a 7 percent gain in the third quarter to 2.6 percent in the fourth. This is a bit better than it sounds, since third quarter spending was boosted by massive auto incentives. Business investment spending also slowed from its torrid third quarter pace. The recovery in business inventories was in line with expectations, but surprisingly, government spending slowed again, and this is partly why I expect that the fourth quarter estimates will be revised upward. Putting the fourth quarter GDP report into perspective, it is useful to note that a 4 percent growth rate is quite good – strong enough to demonstrate momentum, but not so strong as to promote inflation.

Second, the federal reserve decided to keep the fund rate at a historically low one percent rate. Beginning last summer most analysts, including me, expected that the Fed would quickly raise rates as the economy recovered. Instead, the Fed has held rates down and pronounced that it would continue to do so “for a considerable period of time.” But last week the Fed dropped this proviso and noted that it would only “be patient.” This signals that the long awaited tightening is going to happen sooner rather than later.

Third, the President announced his budget recommendations for the fiscal year beginning in October. He proposed spending \$2.4 trillion – an increase of 3.5 percent. He projected a deficit of \$521 billion next year and claimed that his plan would cut this in half by 2009. Military spending would increase 7 percent and homeland security 10 percent, but all other discretionary spending would be

limited to 0.5 percent, with outright cuts in agriculture and the EPA. However, the budget does not count at least an additional \$50 billion that the President plans to request in supplemental defense spending for the wars in Iraq and Afghanistan. This alone increases spending by not 3.5 percent but by 6 percent! Furthermore, it is just not credible to call for congress to “bring discipline to the appropriations process” in an election year and in light of the extra \$50 billion that the President plans to ask for later this year.

The bottom line is that interest rates will go up this spring and summer, but not so high as to seriously impact housing markets. Thus, for Florida as long as the economy is growing at 4 percent or more and mortgage rates remain below 7 percent, we will be just fine.

This is Hank Fishkind for 90.7 FM, WMFE News.