

Ah the French

Dear Mr. Montebourg:

I have just returned to the United States from Australia where I have been for the past few weeks on business; therefore, my apologies for answering your letter dated 31 January 2013.

I appreciate your thinking that your Ministry is protecting industrial activities and jobs in France. I and Titan have a 40-year history of buying closed factories and companies, losing millions of dollars and turning them around to create a good business, paying good wages. [Goodyear](#) tried for over four years to save part of the Amiens jobs that are some of the highest paid, but the French unions and French government did nothing but talk.

I have visited the factory a couple of times. The French workforce gets paid high wages but works only three hours. They get one hour for breaks and lunch, talk for three, and work for three. I told this to the French union workers to their faces. They told me that's the French way!

The Chinese are shipping tires into France – really all over Europe – and yet you do nothing. In five years, Michelin won't be able to produce tire in France. France will lose its industrial business because government is more government.

Sir, your letter states you want Titan to start a discussion. How stupid do you think we are? Titan is the one with money and talent to produce tires. What does the crazy union have? It has the French government. The French farmer wants cheap tire. He does not care if the tires are from China or India and governments are subsidizing them. Your government doesn't care either. "We're French!"

The U.S. government is not much better than the French. Titan

had to pay millions to Washington lawyers to sue the Chinese tire companies because of their subsidizing. Titan won. The government collects the duties. We don't get the duties, the government does.

Titan is going to buy a Chinese tire company or an Indian one, pay less than one Euro per hour and ship all the tires France needs. You can keep the so-called workers. Titan has no interest in the Amien North factory.

*Best regards,
Maurice M. Taylor, Jr.
Chairman and CEO*



French Labor Strike

Today's [New York Times](#) brings a story that will warm the hearts of believers in free markets everywhere. At least one U.S. capitalist understands capitalism. That gentleman is Maurice Taylor Jr., the head of Titan International, a U.S.-based tire manufacturer. He has been in "negotiations" over the last four years aimed at keeping the Goodyear plant in Amiens, France, open. As of today that deal appears off the table. Ah, the French. They would rather cut off an arm than seek treatment for the infection.

France: Home of the 35 Hour Work Week

France is the home of the original 35 hour work week. This law, 13 years old this month, limits workers to 35 hours per week *at no change in weekly pay*. Economists recognize this as a negative supply shock that leads to higher unemployment and short-term inflation. The law is based on the long-discredited “bundle of work” economic hypothesis. If there is only a certain amount of work that can be done in an economy, then limiting workers’ hours will spread the work among more employees. On its face, that is an attractive model. But it assumes the amount of work is limited. In fact, the quantity of labor in any economy is directly related to the country’s gross domestic product – which, as almost everyone knows, fluctuates. The quantity of labor demanded is not fixed, but varies in response to a number of variables.

Titan, the Amiens Plant, and the French Government

Some facts are in order. **The Amiens plant employs 1,173 French workers. Four years ago the French government asked Titan to try to save the plant.** Rather than describe the course of the negotiations, I’ll simply quote Mr. Taylor’s letter to the French industry minister, Arnaud Montebourg (text from [BusinessInsider](#), typographical and grammatical errors in the BusinessInsider version). See pullquote →

Comparing the U.S. and France

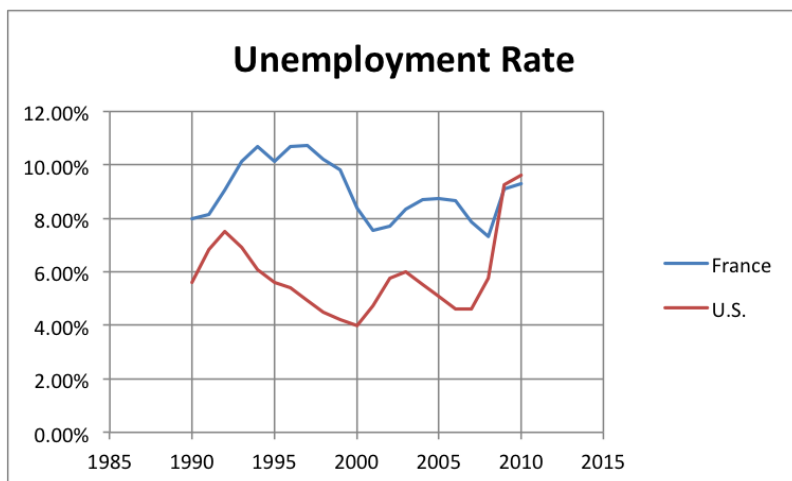
Using OECD data, I assembled two economic indicators: the growth rate of real GDP per capita and the unemployment rate.

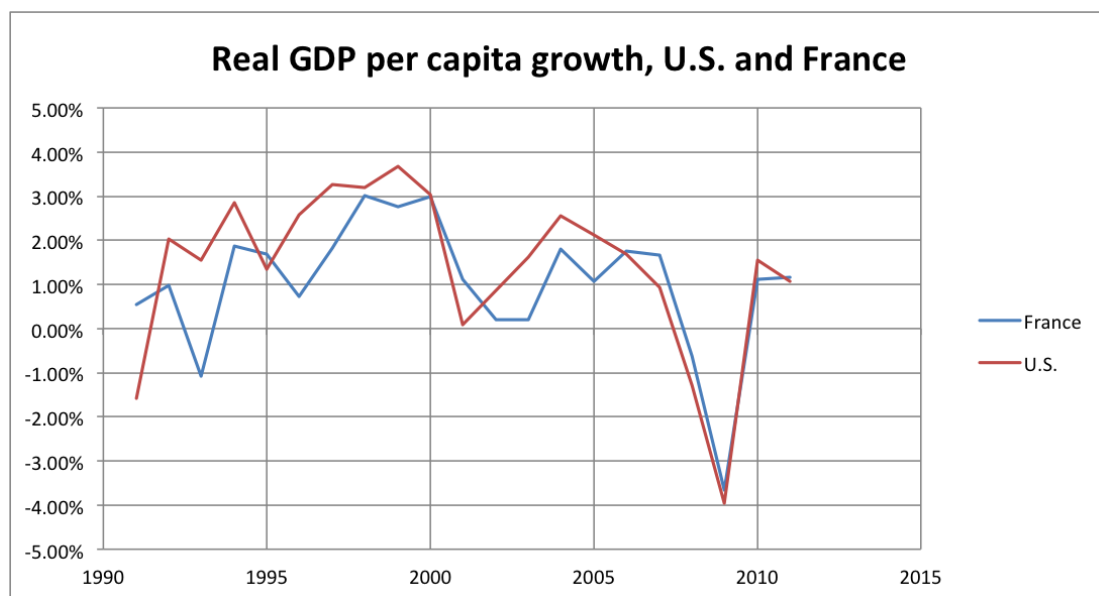
Both variables covered the period 1990-2011 (the latest annual data available in the OECD online database). Here are the averages:

| Country | Average Unemployment Rate (1990 – 2011) | Average growth, real GDP per capita (1995 – 2011) |
|---------|---|---|
| France | 9.01% | 1.00% |
| U.S. | 5.84% | 1.39% |

Pay close attention to that last column. The difference in the growth rate is 0.39% per year. Doesn't sound like much, does it? First, you should know that real GDP is the same as the purchasing power of income (per capita). Let's consider these growth rates over 30 years (usually the definition of one generation). If the annual income in year 1 was 20,000 (dollars or euros), after 30 years French income will be \$26,992.89 versus \$30,258.12 in the U.S. The U.S. economic standard of living will grow faster than that of France.

Let's look at some graphs of the same variables. There's something disturbing about one of them. I'll point it out below.





Did you spot it? **Since 2008 (the beginning of the Obama administration) the U.S. unemployment rate has risen to French levels. You may draw your own conclusions. I've written about this issue many times before. You can read my thoughts by clicking [here](#) and [here](#) and [here](#).**

As always, my data sources and methods are transparent. [Click here](#) to download an Excel 2007 file containing all data and calculations.

Conclusion

Mr. Taylor has stated his case very well. **France is traveling the same road that Greece, Spain, and some other European countries followed years before. When the French economy**

begins to collapse I doubt very much that the German government will bail *them* out.

The Current State of the Government Debt

On Jan. 20, 2009, the national debt stood at \$10.627 trillion—or \$34,782 for every man, woman and child. As of Tuesday, it had reached \$16.435 trillion, or \$52,139 for every American. The public debt was equal to 40.8% of gross domestic product on Jan. 20, 2009. By the end of last year, it had reached 72.8% of GDP and is forecast by the nonpartisan Congressional Budget Office to hit 76.1% this year.

Today's entry was prompted by [Karl Rove's column in the Wall Street Journal](#) (Jan. 17, 2013, p. A15). Mr. Rove cites numerous statistics showing how the U.S. economy has declined in the first four years of the Obama administration. I noticed one interesting number and decided to investigate the current state of the government debt.

Mr. Rove includes a paragraph on the debt situation:

Hmmm. The key phrase is “public debt.” We economists call it the government debt. And, like most issues related to government finance, it's messy.

Boring Stuff: Details of the Debt

The government debt is made up of two big parts: the federal government debt and total state and local debt. As of January 1, 2012 (effectively the end of calendar year 2011), the federal government debt was \$10,810.6 billion. State and local debt totaled \$2,985.0 billion. The sum of those two

figures is \$13,795.6 billion. Both of these figures are from the Federal Reserve database as maintained by the [Federal Reserve Bank of St. Louis](#) in their [FRED database](#). Total government debt as stated by the Treasury department is \$15,582.1 billion (also downloaded from FRED). My guess is that the Treasury number includes debt owned by banks and other financial institutions, while the Federal Reserve figures are government debt in the hands of the nonfinancial public (including nonfinancial businesses).

GDP numbers are from the [Bureau of Economic Analysis](#). There is a direct link from that page that downloads GDP totals (real and nominal, annual and quarterly) directly as an Excel workbook. If only Treasury would learn from BEA and BLS.

So here's the result:

| | |
|--|---------|
| Federal Government Debt as percentage of GDP (Federal Reserve) | 71.71% |
| State & Local Government Debt as percentage of GDP (Federal Reserve) | 91.51% |
| Federal Government Debt as percentage of GDP (U.S. Treasury Dept.) | 103.36% |

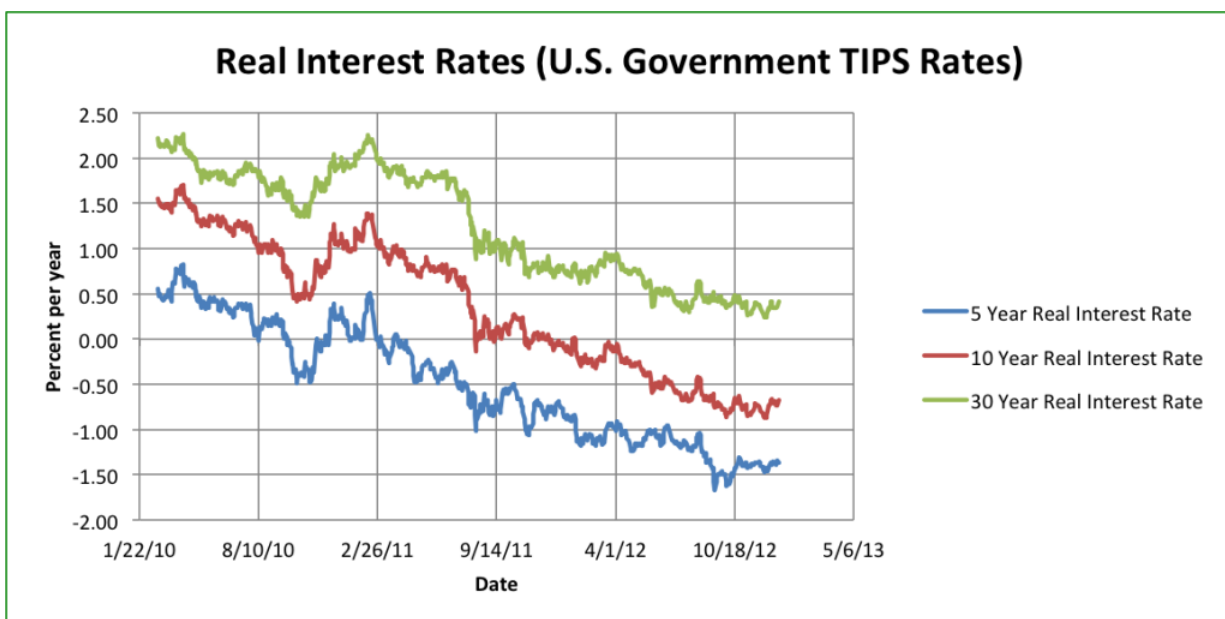
Mr. Rove apparently used the first figure. But that number excludes federal debt held by financial institutions. Let's assume federal debt held by financial institutions is equal to the difference between the Treasury and the Federal Reserve numbers for total government debt:

| | |
|---|-------------|
| Treasury – Fed | \$1,786.47 |
| Federal Reserve govt. debt plus Debt Held by Banks | \$12,597.08 |
| Total Federal Debt/GDP | 83.56% |

Conclusion

The debt-to-GDP ratio is too high. The U.S. is not Greece or Italy – yet. But if we stay on the current path, at some point an auction of Treasury securities will fail in the sense that there will be no bidders from the private sector. The Fed could bail out Treasury by purchasing the entire new issue.

But that is a policy choice that the Fed must make. The really scary part of all this is that nobody knows the debt-to-GDP ratio at which an auction will fail. There will be warnings, however. Watch for rising interest rates on [TIPS \(Treasury Inflation Protected Securities\)](#).



Real Interest Rates

There was a hint of this in early 2011 when rates rose briefly

(For a few months, all real interest rates were positive).

This was interpreted as a sign that the markets were expecting economic recovery. A much more frightening hypothesis is that the rise in interest rates was caused by investors fleeing Treasury securities because of a perceived increase in risk. All we know is that the equilibrium interest rate rose and the equilibrium price of these bonds fell. As always, this could have been caused by shifts in either demand or supply. Assuming Treasury is reporting the yields on new-issue securities, the supply is completely controlled by the government. Therefore, demand factors as outlined earlier must be the determining factor. We can speculate all we want, but the interest rates will tell the story.

[Update Jan. 19, 2013, 15:45 GMT-8: I corrected several errors in the Excel workbook, added a new worksheet to accompany [my new article on the subject](#), and improved several explanations.]

As always, my data and methods are transparent. You can download the Excel workbook for real interest rates by [clicking here](#). And you can download the workbook for the government debt and GDP by [clicking here](#).

National Income Accounting and the Most Recent NPR Fail

Sometimes a self-appointed economist gets it so wrong that their statement fails the laugh-out-loud test. Today's subject is the fascinating world of national income accounting

and the most recent NPR fail. Along the way we'll learn how gross domestic product is measured. Even if you're a real economist, I suspect you can learn a thing or two from this.

Why is this important? Because gross domestic product is equal to national income.[\[1\]](#) When GDP rises, so does national income. Even if you don't think GDP is important, I'm pretty sure national income matters to you.

[Writer Dave Barry](#) once famously said, "gross domestic product would be an excellent name for a band." While that may be true, we're going in a different direction today.

Background: NPR Strikes Again

Today's egregious error is from Public Radio International's *The World*. The segment was titled "[How Should We Judge Our Economy](#)." And the guest clown pseudo-economist was "Eric Zencey, a political economist with the Gund Institute for Ecological Economics at the University of Vermont." Forthwith, Mr. Zencey's argument (lifted straight from the PRI page for this story).

"I think GDP should re-named, so that we don't mistake it for a measure of well-being. I think we should call it gross domestic transactions," said Zencey. "That's all it is, it totes up the monetary value of all the transactions. And if it had that name that would help break the association people have with the idea that more GDP is better. It's like hmmm, more transactions are better? Well it depends on what you're transacting." [All quotation marks and other punctuation unchanged from original story.]

The easy criticism is that, even if GDP equaled spending, it would not equal the total volume of transactions in the economy. For starters, GDP excludes transactions involving assets. If you buy or sell shares in a mutual fund, that is not included in GDP. Also excluded are transactions involving

previously-owned items. That antique pepper mill you bought at a garage sale? Not in GDP. That car you bought from a soon-to-be-ex-friend? Also not included. So the total volume of transactions in any economy would be a huge multiple of GDP.

The more subtle issue is a complete misunderstanding of what GDP measures. Most principles of economics texts get this pretty much: gross domestic product is the market value of all goods and services produced in a country during a calendar year. Read that again and see if you can find the words “spending” or “transactions.” You can’t because GDP measures neither of those. GDP measures production, not spending.

“Wait,” says the knowledgeable reader. “In macroeconomics I learned that GDP was the sum of consumption spending, investment spending, and government spending. Why isn’t GDP the same as total spending? What about $C + I + G$?”

Read on. The answer is far simpler than you can imagine.

GDP and Spending

Think carefully about what you learned in that economics course. In the definition of GDP wasn’t there something about exports and imports? And if your memory is better than mine, you may recall something about the net change in business inventories being part of gross private domestic investment (“investment spending”). Each of these three items is important in its own way. Let’s begin with a basic fact: $C + I + G$ measures total domestic spending on newly-produced goods and services. Asset transactions and purchases of previously-owned goods are still excluded.[\[2\]](#)

GDP, Domestic Spending, and Domestic Production

Let’s first discuss a country that operates in complete

autarky. This lovely word [autarky](#) describes a country that does not interact economically with the rest of the world.[\[3\]](#) In such a country, total domestic spending on domestically produced goods is, in fact, total spending.[\[4\]](#) What happens if there is a difference between spending and production in such an economy?

This is actually pretty simple. John Maynard Keynes discussed it at length in his *General Theory of Employment, Interest, and Money*. When spending is less than production, business inventories rise. The unsold goods flow into inventories. And when spending is greater than production, business inventories fall. The only way businesses can sell goods they have not produced is to draw them from inventory.

A simple example may help. Consider a company that makes ordinary wooden pencils. They try to produce to meet demand. When thinking about how many pencils to produce in July (for example), they consult their economist who assures them that there will be demand for 5 million pencils in July. The company produces 5 million pencils in July. But the forecast was incorrect. Only 4.8 million pencils were actually sold. What happens to the remaining 200,000 pencils? They end up in inventory for the beginning of August.

Note the relationship here: $\text{output} - \text{sales} = \text{inventory change}$. We can rewrite this simply as $\text{output} = \text{sales} + \text{inventory change}$.

But wait – we're trying to measure output (GDP). We start by adding up total spending: consumption plus government plus business fixed investment. We then correct for any output that was not sold by adding the net change in business inventories. Adding inventory change converts total spending into total output.

That was pretty easy. Believe it or not, the next section is even easier.

GDP, Domestic Spending, and Domestic Production in an Open Economy

Now let's open our economy to international trade. Our GDP equation now becomes $C + I + G + (X - M)$. Exports are X , imports are M . Together, $X - M$ is called *net exports*.

If you read several principles textbooks you will find many convoluted explanations of why exports are added and imports are subtracted. That's unfortunate because the explanation is very easy. Exports are goods and services produced in our country and sold elsewhere. We add exports to domestic spending because those goods and services are not included in domestic spending *but they are included in domestic production*. Workers producing those exports earn income even though the products they are producing are not sold within the country where they are produced.

What about imports? Goods and services that are produced in other countries but sold in our country fall into this category. Therefore, those goods and services are part of domestic spending. *But they are not part of domestic production*. Imports are subtracted to correct domestic spending into domestic production.

Consider a couple of examples. Suppose you buy a new BMW for \$50,000. The car was produced in Germany. But it's sold here, which means domestic spending rises by \$50,000. But domestic production has not changed. We need to subtract that \$50,000 from domestic spending to move the total in the direction of domestic production.

Similarly, consider German tourists visiting the U.S. They are buying tourism services from the U.S. which count as exports. The services are produced here but sold (in effect) in another country. Therefore we must add the value of those exported services to total spending to move the total in the direction of domestic production.

Conclusion

So here's the story. We begin with domestic spending (roughly $C + I + G$ ignoring the fact that inventory change is included in I). We then add the net change in business inventories to this total to correct for any difference between domestic spending on domestically produced goods and domestically produced goods sold within the country. Next we add exports, products that are produced here but sold in other countries.

Finally we subtract imports, products that are produced in other countries but sold here. Remember, the central idea is to convert domestic spending into domestic production.

At its most basic, this stuff is not difficult. It's always been a mystery to me why economists insist on making it difficult. I hope this explanation has been helpful. Please feel free to ask questions in the comments.

[\[1\]](#) Please don't quibble. I know there are differences between GDP and national income. This is a blog, not the *American Economic Review*.

[\[2\]](#) No one has yet figured out how to sell previously-owned services, so we don't have to worry about that.

[\[3\]](#) From the ancient Greek *autarkeia*: self-sufficiency, or nonattachment. See this page from Britannica online for more details.

[\[4\]](#) Consistent with national income accounting assumptions, I continue to exclude spending on assets and previously-owned goods.

GDP Growth Was Revised Down

The second estimate is in for the third quarter and – no surprise – GDP growth was revised down. The preliminary estimate had been 2.5 percent, but the revised estimate is 2.0 percent. Remember, you read it [here](#) first.

It's the Advance GDP Estimate, Stupid!

Happy talk media today are whooping it up because real GDP grew by 2.5% in the third quarter. News flash: it's the advance GDP estimate, stupid!

Don't take my word for it. Read the first two paragraphs of the press release from the [Bureau of Economic Analysis](#):

“Real gross domestic product – the output of goods and services produced by labor and property located in the United States – increased at an annual rate of 2.5 percent in the third quarter of 2011 (that is, from the second quarter to the third quarter) according to the “advance” estimate released by the Bureau of Economic Analysis. In the second quarter, real GDP increased 1.3 percent.

The Bureau emphasized that the third-quarter advance estimate released today is based on source data that are incomplete or subject to further revision by the source agency (see the box on page 3). The “second” estimate for the third quarter, based on more complete data, will be released on November 22, 2011.”

Prediction: this estimate will be revised downward twice –

once at the end of November and a second time just as we're about to welcome in 2012.

U.S. Government Debt

On March 30, 2011, I went looking for data on total U.S. federal government indebtedness. In the not-too-distant past you could find this information pretty easily on the [U.S. Treasury Department website](#). No more. It took me the better part of two hours to find and assemble the data I was looking for. And the editing basically involved converting a text table (which was not formatted as a table even though it was displayed on a website) into an Excel workbook. Tedious, boring, and requires a pretty good attention to detail. You think maybe Treasury has something to hide?

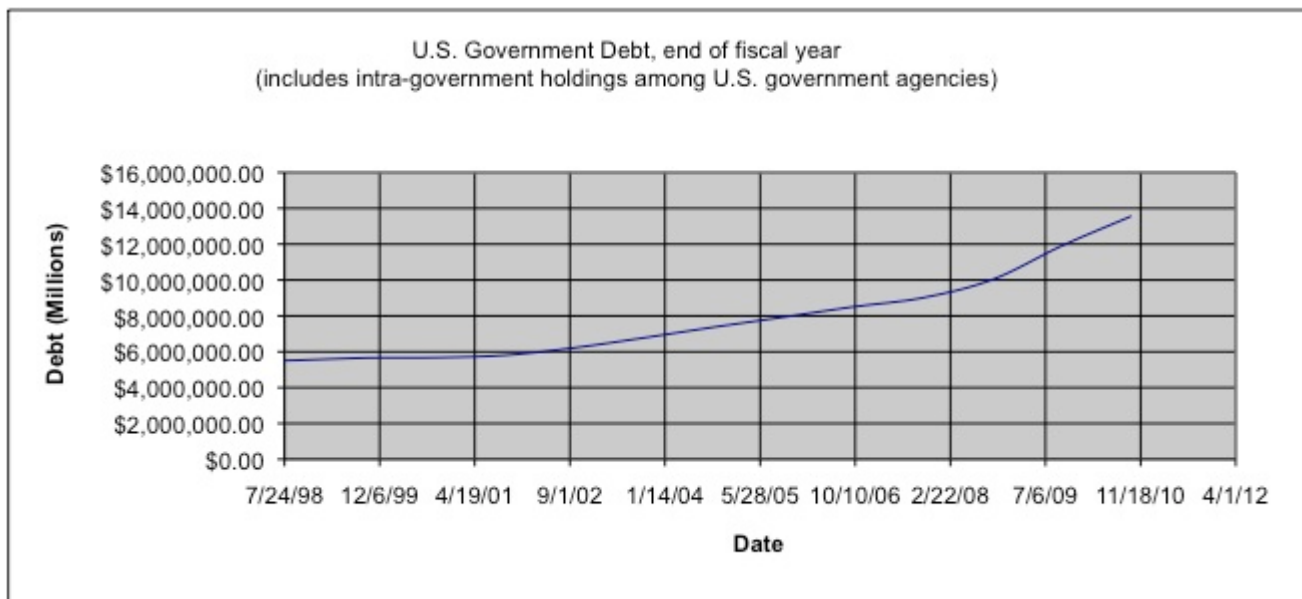
This all stems from an incident in one of my classes yesterday. I was looking around the Treasury site searching for debt information. One of my students went to [TreasuryDirect.gov](#) and reported the debt as \$14 trillion. "That can't be," I exclaimed. "That's about 100 percent of GDP."

Well, there's debt and then there's debt. It turns out the total U.S. government debt is, indeed, \$13.561 trillion (as of Sept. 30, 2010, the end of the federal government's fiscal year). But \$4.539 trillion is intragovernment debt – government debt issued by one agency but owned by another branch of government. It seems to me that intragovernment debt should not be counted as part of the government's net indebtedness. So I've pulled together data from several sources. (See below for details.)

Total Debt

As of September 30, 2010, total U.S. federal government debt was \$13,561,623,030,891.70. That's a pretty big number. In 2010, U.S. gross domestic product was \$14,660,400,000,000.

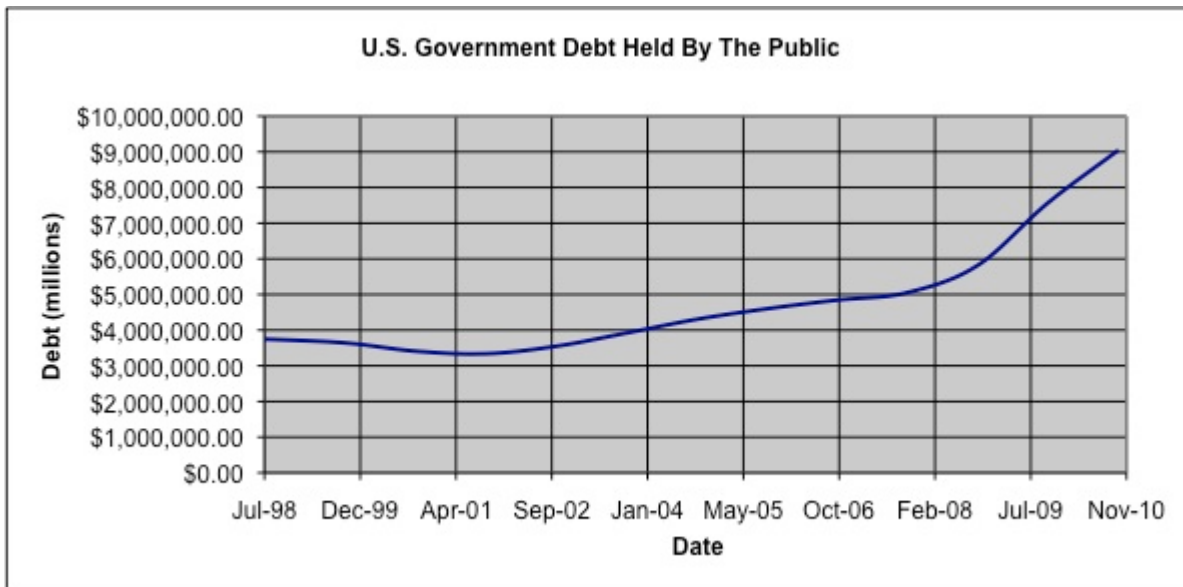
Total debt was 92.51% of GDP. The chart below shows how total debt has grown since 1998.



U.S. Total Government Debt

Debt Held By the Public

By contrast, debt held by the public (excluding intragovernment holdings) at the end of 2010 was \$9,022,808,423,453.08. Well, that's comforting – “only” 61.55% of GDP. The chart below shows the growth of privately-held government debt.



U.S. Government Debt Held By Public

Boring Stuff: Data Sources and Formats

End of year debt, 2000 – 2010:
http://treasurydirect.gov/govt/reports/pd/histdebt/histdebt_histo5.htm

End of year debt, 1950 – 1999:
http://treasurydirect.gov/govt/reports/pd/histdebt/histdebt_histo4.htm

Both are text files only. Also this is total debt (privately held plus intragovernment). The only source I could find that separated privately held from intragovernment holdings was daily data from <http://treasurydirect.gov/NP/NPGateway>. The screen capture below shows part of the data. Considerable editing was necessary to compile the annual end-of-fiscal-year data I used.

The Daily History of the Debt Results

Historical returns from 09/30/1997 through 09/30/2010

The data for the total public debt outstanding is published each business day. If there is no debt value for the date(s) you requested, the value for the preceding business day will be displayed.

([Debt Held by the Public](#) vs. [Intragovernmental Holdings](#))

| Date | Debt Held by the Public | Intragovernmental Holdings | Total Public Debt Outstanding |
|------------|-------------------------|----------------------------|-------------------------------|
| 09/30/1997 | 3,789,667,546,849.60 | 1,623,478,464,547.74 | 5,413,146,011,397.34 |
| 10/01/1997 | Not Available | Not Available | 5,420,505,789,573.34 |
| 10/02/1997 | Not Available | Not Available | 5,387,382,191,644.62 |
| 10/03/1997 | Not Available | Not Available | 5,411,881,420,892.37 |
| 10/06/1997 | Not Available | Not Available | 5,413,432,617,300.15 |
| 10/07/1997 | Not Available | Not Available | 5,413,432,617,300.15 |
| 10/08/1997 | Not Available | Not Available | 5,413,432,617,300.15 |
| 10/09/1997 | Not Available | Not Available | 5,409,087,032,816.86 |
| 10/10/1997 | Not Available | Not Available | 5,410,700,313,154.02 |
| 10/14/1997 | Not Available | Not Available | 5,412,698,794,445.84 |
| 10/15/1997 | Not Available | Not Available | 5,414,923,137,712.76 |
| 10/16/1997 | Not Available | Not Available | 5,416,174,203,759.08 |
| 10/17/1997 | Not Available | Not Available | 5,418,064,201,028.31 |
| 10/20/1997 | Not Available | Not Available | 5,418,457,770,302.08 |
| 10/21/1997 | Not Available | Not Available | 5,420,383,941,176.62 |
| 10/22/1997 | Not Available | Not Available | 5,421,844,508,272.92 |
| 10/23/1997 | Not Available | Not Available | 5,424,897,442,383.46 |
| 10/24/1997 | Not Available | Not Available | 5,425,466,348,255.95 |
| 10/27/1997 | Not Available | Not Available | 5,427,907,147,573.22 |
| 10/28/1997 | Not Available | Not Available | 5,429,321,910,123.66 |
| 10/29/1997 | Not Available | Not Available | 5,429,377,880,990.06 |
| 10/30/1997 | Not Available | Not Available | 5,430,869,894,529.83 |
| 10/31/1997 | Not Available | Not Available | 5,427,225,185,059.66 |
| 11/03/1997 | Not Available | Not Available | 5,427,078,768,247.28 |
| 11/04/1997 | Not Available | Not Available | 5,432,371,961,282.81 |
| 11/05/1997 | Not Available | Not Available | 5,433,411,941,085.78 |
| 11/06/1997 | Not Available | Not Available | 5,431,079,031,652.94 |
| 11/07/1997 | Not Available | Not Available | 5,426,731,931,109.43 |

Format of Daily U.S. Government Debt Table

Dissecting the First Quarter GDP Numbers

Friday the [Bureau of Economic Analysis](#) released the preliminary estimate of the first quarter, 2010, U.S. gross domestic product. The good news is that total production of goods and services grew 3.2% in that quarter (seasonally adjusted at an annual rate). For better or worse, nearly half that growth (1.57%) was caused by expansion of business inventories. I'm going to dig into the GDP numbers, an exercise that often puts readers to sleep. Hang in there – I promise it will be worth the effort.

Before I begin, there's one important point to be made. This is the *preliminary* estimate for the first quarter. There will be two revisions released near the end of the next two months. Revisions are often significant. As several writers have discovered, basing significant economic analysis on the preliminary estimate can lead to wildly incorrect conclusions.

Caveat emptor. You have been warned. Read on at your own risk!

Far and away the most interesting data for the first quarter comes from the B.E.A.'s table 1.1.2 ("Contributions to Percent Change in Real Gross Domestic Product"). From that we learn that 2.55% of the 3.24% growth came from consumer spending. About 40% of that (1.15%) was attributed to growth in consumer spending on services. This is actually a good sign. It means that consumers are, among other things, going out to restaurants and beginning to purchase services they might have performed themselves a year ago. Not surprisingly durable goods spending contributed 0.79%, down sharply from the 2009

second quarter of 1.36%. The “cash for clunkers” program did exactly what economists predicted. It shifted consumer spending from future quarters into the second quarter of 2009. Mind you, this is a good thing. The economy needs more spending sooner.[\[1\]](#)

Gross Private Domestic Investment

Far more problematic is the behavior of gross private domestic investment. Consumer spending stimulates output this year. Investment spending creates the new physical capital to increase output in the future. The overall contribution of gross private domestic spending was 1.67%. However, only 0.1% was from business fixed investment. The remaining 1.57% was growth in business inventories. Let’s dissect those numbers.

Business fixed investment includes nonresidential structures, nonresidential equipment and software, and residential construction. Nonresidential and residential constructions together *reduced* GDP by 0.73%. That means spending to build new structures fell compared to the fourth quarter of 2009. Blame this on the first-time homebuyer’s tax credit which shifted demand for residential structures into the last two quarters of 2009. However, these decreases were more than offset by increased spending on nonresidential equipment and software which contributed 0.83% to GDP. The net change in gross private domestic investment masks larger changes in the underlying components.

Inventory change

The 1.57% contribution of inventory growth has been hailed by many economists as evidence that businesses are rebuilding inventories anticipating higher future sales. Not so fast, folks. Let’s review J.M. Keynes. He pointed out that there are two sources of inventory change: planned and unplanned. Economic analysts are assuming the inventory increase was

intentional. But suppose the change was unplanned. That would mean production exceeded spending. Remember, businesses have to plan production in advance of spending. When their demand forecasts are too high, production will exceed spending and inventories will rise. But that's not a positive sign for the economy – in fact, it's a negative because businesses will have to liquidate those inventories in future quarters.

Was the inventory increase planned or unplanned? I don't know and I suspect many of the economists mentioned in the previous paragraph don't know, either.

However, another B.E.A. table contains some valuable insights. Table 5.6.6B is the "Change in Real Private Inventories by Industry, Chained Dollars." This table is in billions of constant 2005 dollars, not percentages. The growth in business inventories was \$31.1 billion. As always, inventories in some industries grew while others shrank. The main positive contributions came from Manufacturing, nondurable goods industries (\$10.3 billion), Wholesale trade, nondurable goods industries (\$10.3 billion, no this is not a typo), and Motor vehicle and parts dealers (\$23.1 billion). In other words, nondurables and vehicles were the source of the inventory growth. The growth in motor vehicle inventories is nothing more than rebuilding depleted inventories after the end of the cash for clunkers program. Don't expect that to continue into future quarters. The two nondurable increases are largely a result of the increased consumer demand for services. (Remember, consumer spending on services includes meals eaten away from home. Restaurants hold inventories just like most businesses that make something. Consider this a bit of an anomaly in the national income accounts.)

Let's not bother with foreign trade since exports and imports are mainly included to convert total spending into production. Instead, take a look at government spending.

Government Spending

The contribution of government spending to first quarter growth was -0.37%. You read that correctly. Government spending was actually a drag on the economy.

“Wait,” you’re saying. “What happened to the government stimulus program?”

Good question. Once again we can look at the details to see what happened. Federal government spending contributed +0.11% to GDP growth. But state and local government spending dragged GDP growth down by 0.48%. This lends support to the calls by several economists[\[2\]](#) for the federal government to bail out state governments.

That’s the story. The news is good, but perhaps not as good as the media would have you believe.

[\[1\]](#) See, for evidence, the failure to spend economic stimulus funds from the ARRA program at a fast enough rate.

[\[2\]](#) I believe Paul Krugman has advocated this position, but I’m too lazy to look up the citation.