MarketWatch

Economy downshifts to 2.6% rate in the fourth quarter

By Greg Robb
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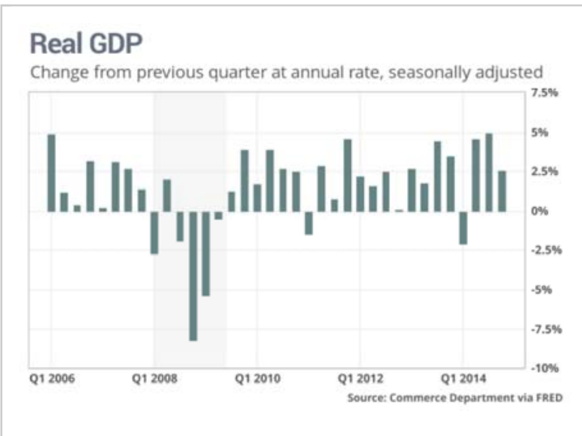
GDP below expectations of a 3.2% gain



WASHINGTON (MarketWatch) — The U.S. economy slowed a bit more than expected in the fourth quarter after expanding at the fastest pace in eleven years during the fall, according to data released Friday.

Gross domestic product — the value of all goods and services produced by the U.S. — grew at a 2.6% annual clip in the fourth quarter, the government said Friday. That's below the 5.0% pace recorded in the July-September period.

Economists polled by MarketWatch forecast GDP would grow by a seasonally adjusted 3.2% in the October-to-December period.

Stock traded lower all day Friday after the data was released. The S&P 500 index SPX, -0.78% was recently down 7 points to 2,014.

For all of 2014, the U.S. economy grew at a 2.4% rate, slightly faster than the 2.2% gain in the prior year.

Consumer spending was a major positive in the fourth quarter, expanding 4.3%, the fastest pace since before the financial crisis.

But growth was pulled down by weaker business spending, a drop in federal government spending and net exports.

Economists say the pattern of strong consumer spending and weak business spending should persist in the first quarter as a result of the sharp drop in oil prices.

"The economy is also showing more signs of lopsided growth, being too reliant on the consumer.," said Chris Williamson, chief economist at Markit.

And the stronger dollar DXY, +0.18% may also weaken the U.S. trade sector in coming quarters.

Economists were divided over what today's report signaled for coming quarters.

"This slowdown is nothing to worry about," said Paul Ashworth, chief U.S. economist at Capital Economics.

But Williamson said it might delay a Fed rate hike until late 2015 or 2016.

Prior to the release, economists polled by MarketWatch forecasted the U.S. will expand by roughly 3% in the first and second quarters. They based their optimism on a surge in hiring that's added 2.95 million new jobs in 2014, the largest gain since 1999.

Inflation as measured by the Federal Reserve's preferred price index, meanwhile, weakened in the fourth quarter to the lowest rate in almost six years, potentially making the central's bank effort at managing the U.S. recovery more difficult.

The PCE index fell at a 0.5% annual rate in the October-to-December period, compared to a 1.2% gain in the third quarter. That's the biggest drop since the first quarter of 2009. The core PCE that excludes food and energy rose at a 1.1% clip, down from 1.4%.

The Fed believes the slowdown in inflation will be temporary, but if the central bank is wrong, it could be forced to hold rates at zero longer than it would like.