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**COVID-19 Impacts on Arkansas’**

**Agricultural and Rural Economies**

**UPDATE:**

**Second Quarter Gross Domestic Product**

**Prepared by:**

**John Anderson**

**Department of Agricultural Economics and Agribusiness**

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On July 30, the U.S. Department of Commerce Bureau of Economic Analysis released the first estimate of second quarter gross domestic product (GDP). This is arguably the most comprehensive look yet at the impact of COVID-19 and the response to it on the nation’s economy. Not surprisingly, that impact has been severely negative. In the second quarter of this year, real (i.e., inflation-adjusted) GDP declined by about 9.5 percent compared to the first quarter. Quarter-to-quarter change in GDP is generally reported as a seasonally-adjusted annualized rate. On that basis, the decline in GDP amounts to just under 33 percent in comparison to the previous quarter. As figure 1 shows, that is an historic decline. Quarterly GDP data go back to 1947, and there is no comparable quarter-to-quarter decline over this entire period.

Data Source: St. Louis Federal Reserve Bank, FRED Economic Data

**Figure 1.** Gross Domestic Product: Annualize Percentage Change from Previous Quarter

To review, briefly, GDP is the value of all the goods and services produced in the United States. While GDP is essentially just the aggregation of spending on a huge array of individual items, it is simpler to think of it as the sum of only four major categories of spending: consumer spending on goods and services, government spending and investment, private investment, and net exports. This allows a bit closer scrutiny of the broad sources of any gains or losses in GDP. Clearly, in 2020.Q2, the primary source of the decline in GDP was consumer spending.

Table 1 shows GDP and its major components for the first two quarters of 2020. Note that personal consumption expenditures are by far the largest component of GDP, accounting for just under 70 percent of the total. Thus, the relatively large decline in consumer spending accounts for most of the drop in GDP. Private investment accounts for the remainder of the GDP decline. Both government spending/investment and net exports actually represented positive contributions to the GDP change in the second quarter.

**Table 1.** Real Gross Domestic Product and Major Components: 2020.Q1 and 2020.Q2

(billions of dollars)

|  |  |  |  |
| --- | --- | --- | --- |
|   | 2020.Q1 | 2020.Q2 | Change |
| Gross Domestic Product |  19,010.8  |  17,205.8  | -1,805.0 |
| Personal Consumption Expenditures |  13,118.4  |  11,796.6  | -1,321.8 |
| Gross Private Domestic Investment |  3,334.0  |  2,817.7  | -516.3 |
| Net Exports of Goods & Services |  (788.0) |  (780.7) | 7.3 |
| Government Consumption Expenditures and Gross Investment |  3,347.9  |  3,369.9  | 22.0 |

Notes: totals may not add up due to rounding.

Data Source: U.S. Department of Commerce, Bureau of Economic Analysis

It is important to note that government transfer payments don’t show up directly in GDP figures because they don’t represent the purchase of goods or services. Any goods or services purchased by the recipients of those transfers do show up in GDP. Thus, the big surge in government transfers occasioned by the implementation of the Coronavirus Aid, Relief, and Economic Security (CARES) Act is not the cause of the increase in government spending. That increase reflects increased direct expenditure by the government to purchase goods and services and on investments (e.g., durable equipment). This growth in government spending took place almost exclusively at the federal level. On net, state and local government spending fell rather sharply in 2020.Q2, offsetting over half of the increase in federal spending. This should not be too surprising. State and local government revenue depends heavily on sales taxes, which obviously declined along with personal consumption expenditures. Also, many state governments operate on a balanced budget principle and so must match expenditures to revenues much more quickly than does the federal government.

Personal consumption expenditures fell for both goods and services, but the decline was far more significant in services. Total spending on services fell by a little over 13 percent from the first to the second quarter. The largest declines were in spending on health care, food services and accommodations, and recreation services. It is mildly ironic that one of the largest overall declines in spending during a pandemic occurred with respect to health care. That demonstrates the extent to which non-COVID health services were displaced by COVID-19, either directly because of facility shutdowns or indirectly because people avoided health care facilities for fear of COVID exposure.

Spending on goods was only down about 3 percent, and that was due almost entirely to a decline in spending on non-durable goods. Durable goods spending was down by less than half-a-percent in 2020.Q2. The non-durable goods posting the largest declines in 2020.Q2 were clothing/footwear, gasoline, and food. Again, given the massive runs on grocery stores during the height of the pandemic, it may seem odd that spending on food went down at all. Note, though, that GDP figures account for value and not quantity. Much of the stockpiling that occurred was focused on staple items, which tend to be relatively lower-valued items.

With large transfers from the federal government and an overall slowdown in spending, consumer saving was quite high in the second quarter. For the entire quarter, the personal savings rate worked out to 25.7 percent. This is about three times higher than normal. Such a high savings rate is indicative of the level of uncertainty that consumers were feeling in the second quarter.

In summary, the COVID-19 pandemic delivered a tremendous blow to the U.S. economy in the second quarter of 2020. We certainly have good reason to hope that this will represent the deepest part of the COVID-19 recession. Most state restrictions on businesses began to ease in late-May or early-June. Thus, third quarter figures will reflect a more economically active time period and should be considerably improved from the second quarter. Still, real recovery will require a return of consumer confidence that appears to yet be lacking, particularly as COVID-19 continues to spread actively in many parts of the country, including in Arkansas. These most recent GDP data show the severe economic consequences of COVID-related business shutdowns and thus highlight the urgency of finding effective ways to manage the COVID threat.

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