First Trust

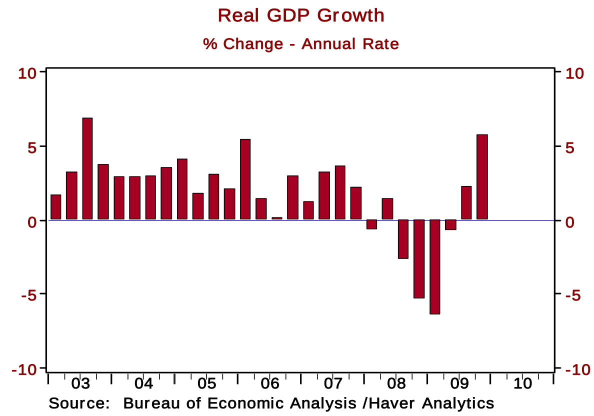
Data Watch

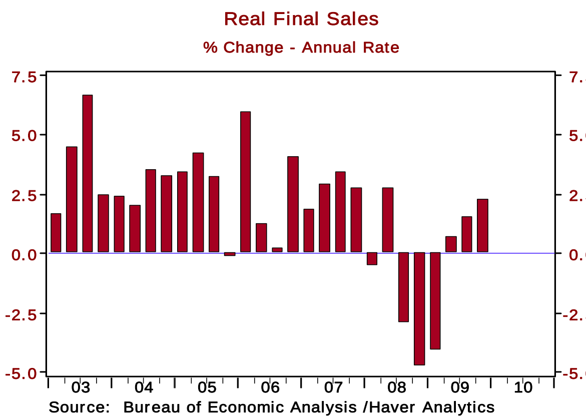
January 29, 2010 • 630.322.7756 • http://www.ftportfolios.com

4TH QUARTER GDP (ADVANCE)

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA

- The first estimate for Q4 real GDP growth is 5.7% at an annual rate, easily beating a consensus expected 4.7%.
- The largest positive contributions to the real GDP growth rate, in order, were inventories, personal consumption, and business investment in equipment and software.
- The weakest components of real GDP were business investment in structures (like offices and retail space) and government spending.
- The GDP price index increased at a 0.6% annual rate in Q4. Nominal GDP – real GDP plus inflation – rose at a 6.4% rate in Q4 and is now higher than a year ago.





Implications: Real GDP boomed in Q4 and suggests continued strong growth in 2010. The expansion is being driven by a natural cyclical recovery from the panic, an end to mark-to-market accounting (which has helped heal the financial sector), and low interest rates from the Federal Reserve. If this is a "weak recovery" or "the new normal," please give us more. The "siege" is over, but some pessimistic analysts seem to have caught a case of "economic Stockholm Syndrome" afraid to admit improvement. Although inventories accounted for a large share of growth in Q4, this was due to fewer inventory reductions, not an actual increase in goods on the shelf. As a result, inventories will keep adding substantially to growth in 2010. Meanwhile, final sales (GDP excluding inventories) have increased three quarters in a row and the gains have accelerated each quarter. Notice what has not accounted for recovery: government spending. Government was a drag on the economy in Q4 and only added 0.3 points to the real GDP growth rate in 2009, no different than the long-term average. On the inflation front, GDP prices increased at only a 0.6% annual rate in Q4. However, prices for the things we buy (gross domestic *purchases*) increased at a 2.1% rate. Nominal GDP (real GDP growth plus inflation) is now up 0.8% versus last year and will be going up quickly in the near future. This means zero percent interest rates are now too low and, therefore, inflationary. In other news this morning, the Chicago PMI, a measure of manufacturing in the Midwest, increased to 61.5 in January versus 58.7 in December, bucking a consensus-expected decline. The employment index increased to 59.8, the first positive number since 2007 and the highest level since 2005. This supports our forecast that payrolls increased in January.

4th Quarter GDP *Seasonally Adjusted Annual Rates*	*Q4-09*	*Q3-09*	*Q2-09*	*Q1-09*	*4-Quarter Change*
Real GDP	**5.7%**	2.2%	-0.7%	-6.4%	0.1%
GDP Price Index	**0.6%**	0.4%	0.0%	1.9%	0.7%
Nominal GDP	**6.4%**	2.6%	-0.8%	-4.6%	0.8%
PCE	**2.0%**	2.8%	-0.9%	0.6%	1.1%
Business Investment	**2.9%**	-5.9%	-9.6%	-39.2%	-14.6%
Structures	**-15.4%**	-18.4%	-17.3%	-43.6%	-24.7%
Equipment and Software	**13.3%**	1.5%	-4.9%	-36.4%	-8.7%
Contributions to GDP Growth (p.pts.)	**Q4-09**	**Q3-09**	**Q2-09**	**Q1-09**	**4Q Avg.**
PCE	**1.4**	2.0	-0.6	0.4	0.8
Business Investment	**0.3**	-0.6	-1.0	-5.3	-1.7
Residential Investment	**0.1**	0.4	-0.7	-1.3	-0.4
Inventories	**3.4**	0.7	-1.4	-2.4	0.1
Government	**0.0**	0.6	1.3	-0.5	0.3
Net Exports	**0.5**	-0.8	1.7	2.6	1.0

Source: Commerce Department