First Trust DATAWATCH

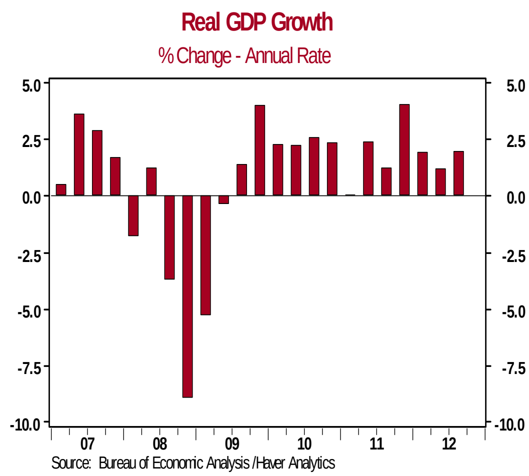
October 26, 2012 • 630.517.7756 • www.ftportfolios.com

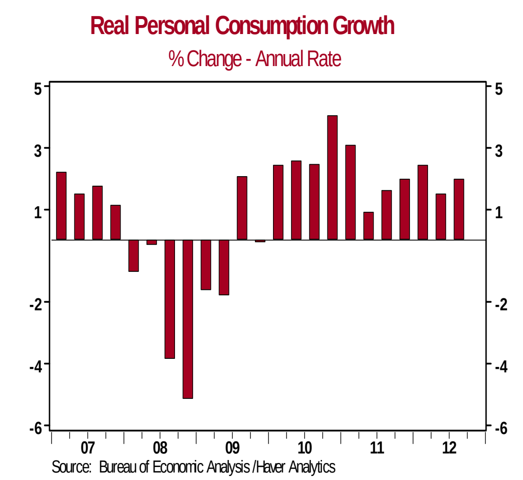
Third Quarter GDP (Advance)

Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Senior Economist
Strider Elass – Economic Analyst

- The first estimate for Q3 real GDP growth is 2.0% at an annual rate, slightly higher than the 1.8% the consensus expected. Real GDP is up 2.3% from a year ago.
- The largest positive contribution to the real GDP growth rate was personal consumption, followed by government purchases.
- Three components of real GDP slowed the pace of growth in Q3: net exports, commercial construction, and inventories.
- The GDP price index increased at a 2.8% annual rate in Q3. Nominal GDP – real GDP plus inflation – rose at a 5.0% rate in Q3 and is up 4.0% from a year ago.

Implications: It would be hard to find a better example of the plow horse economy than today's report on third quarter GDP. Real GDP grew at a modest 2% annual rate in Q3 and is up 2.3% from a year ago, nowhere close to either strong growth or recession. Real "private" GDP (real GDP excluding government purchases) grew at a slower 1.6% rate in Q3, but is up a respectable 3% from a year ago. Real final sales (real GDP excluding inventories) was up at a 2.1% annual rate in Q3 and is up 1.9% from a year ago. In other words, the underlying trend in real GDP growth remains very close to 2%. Notably, this trend continued in Q3 despite a drought that reduced farm inventories by more than in any quarter since 1983. Look for a similar reduction in farm inventories in the fourth quarter followed by a rebound in the first half of 2013. Perhaps the brightest spot in the report was that home building increased at a 14.4% annual rate in Q3, the sixth consecutive quarterly increase. Despite continued tepid growth, the report does not justify the Fed's recent foray into a third round of quantitative easing. The GDP price index was up at a 2.8% annual rate in Q3 and nominal GDP (real GDP plus inflation) was up at a 5% rate. Nominal GDP is up 4% in the past year and also up at a 4% annual rate over the past two years. This is very close to the Fed's long-term forecast of 4.5% and much too fast for a short-term interest rate target near zero percent. Getting the economy growing faster requires changes to fiscal and regulatory policy, not monetary policy. Hopefully, the election in eleven days will get us moving in that direction.





3rd Quarter GDP *Seasonally Adjusted Annual Rates*	*Q3-12*	*Q2-12*	*Q1-12*	*Q4-11*	*4-Quarter Change*
Real GDP	**2.0%**	1.3%	2.0%	4.1%	2.3%
GDP Price Index	**2.8%**	1.6%	2.0%	0.4%	1.7%
Nominal GDP	**5.0%**	2.8%	4.2%	4.2%	4.0%
PCE	**2.0%**	1.5%	2.4%	2.0%	2.0%
Business Investment	**-1.3%**	3.6%	7.5%	9.5%	4.7%
Structures	**-4.4%**	0.6%	12.8%	11.5%	4.9%
Equipment and Software	**0.0%**	4.8%	5.4%	8.8%	4.7%
Contributions to GDP Growth (p.pts.)	**Q3-12**	**Q2-12**	**Q1-12**	**Q4-11**	**4Q Avg.**
PCE	**1.4**	1.1	1.7	1.5	1.4
Business Investment	**-0.1**	0.4	0.7	0.9	0.5
Residential Investment	**0.3**	0.2	0.4	0.3	0.3
Inventories	**-0.1**	-0.5	-0.4	2.5	0.4
Government	**0.7**	-0.1	-0.6	-0.4	-0.1
Net Exports	**-0.2**	0.2	0.1	-0.6	-0.1

Source: Commerce Department