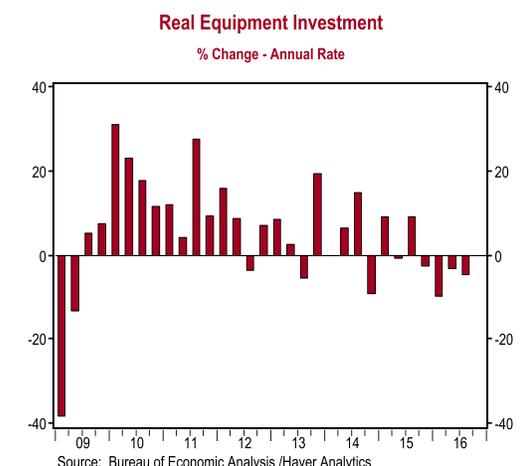
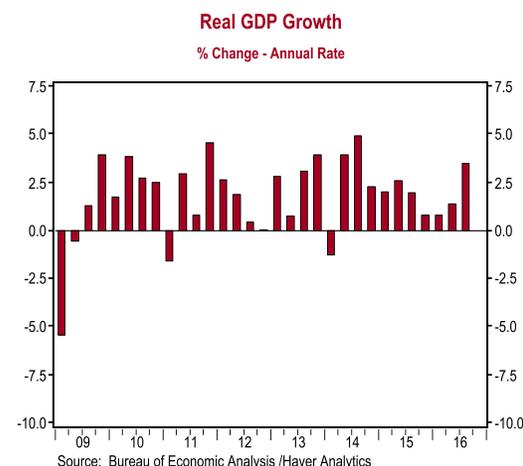


3rd Quarter GDP (Final)

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- Real GDP growth in Q3 was revised to a 3.5% annual rate from a prior estimate of 3.2%, beating the consensus expected 3.3%.
- The upward revision was due to stronger business investment and personal consumption. Other categories were either unchanged or changed only slightly.
- The largest positive contribution to the real GDP growth rate in Q3 came from consumer spending. The weakest component of real GDP was residential investment.
- The GDP price index was unrevised at a 1.4% annualized rate of change. Nominal GDP growth – real GDP plus inflation – was revised up to a 5.0% annual rate versus a prior estimate of 4.6%. Nominal GDP is up 2.9% versus a year ago and up at a 3.1% annual rate in the past two years.

Implications: Today’s final GDP report for the third quarter showed real economic growth at a 3.5% annual rate, slightly better than consensus expectations, and the fastest growth in two years. The upward revisions were due to business investment and personal consumption, which means the “mix” of growth was favorable for the year ahead. Although corporate profits were revised down slightly, they were still up 5.8% in Q3 and up 2.1% from a year ago. The lull in profits over the past year and a half has been an energy story. But as energy prices are well off their lows from earlier this year, we expect higher profits in the quarters to come. Meanwhile, plugging the new profits data into our capitalized profits model suggests US equities remain cheap, not only at today’s interest rates but even using a 10-year Treasury yield in the 3.5% - 4% range. In terms of monetary policy, the Fed should see today’s report as a confirmation that they made the right decision to raise short-term rates last week. Nominal GDP growth (real growth plus inflation) was revised to 5% annual rate in Q3 from a prior estimate of 4.6%. Nominal GDP is up 2.9% in the past year and up at a 3.1% annual rate in the past two years, leaving the Fed plenty of room for rate hikes in 2017. Monetary policy will not be restrictive until the federal funds rate is moved close to nominal GDP growth. That’s still a long way off. In other news today, the FHFA index, which measures prices for homes financed with conforming mortgages, increased 0.4% in October. In the past year, these home prices are up 6.2% versus a 6.0% increase in the year ending in October 2015. Look for continued gains in home prices in the year ahead, as jobs keep expanding, wage growth accelerates, and any headwind created by an increase in mortgage rates is offset by expectations of faster future economic growth.



| 3rd Quarter GDP <i>Seasonally Adjusted Annual Rates</i> | Q3-16 | Q2-16 | Q1-16 | Q4-15 | 4-Quarter Change |
|---|--------------|--------------|--------------|--------------|-------------------------|
| Real GDP | 3.5% | 1.4% | 0.8% | 0.9% | 1.7% |
| GDP Price Index | 1.4% | 2.3% | 0.5% | 0.8% | 1.3% |
| Nominal GDP | 5.0% | 3.7% | 1.3% | 1.8% | 2.9% |
| PCE | 3.0% | 4.3% | 1.6% | 2.3% | 2.8% |
| Business Investment | 1.4% | 1.0% | -3.4% | -3.3% | -1.1% |
| Structures | 12.0% | -2.1% | 0.1% | -15.2% | -1.8% |
| Equipment | -4.5% | -3.0% | -9.5% | -2.6% | -4.9% |
| Intellectual Property | 3.2% | 9.0% | 3.8% | 4.5% | 5.1% |
| Contributions to GDP Growth (p.pts.) | Q3-16 | Q2-16 | Q1-16 | Q4-15 | 4Q Avg. |
| PCE | 2.0 | 2.9 | 1.1 | 1.5 | 1.9 |
| Business Investment | 0.2 | 0.1 | -0.4 | -0.4 | -0.1 |
| Residential Investment | -0.2 | -0.3 | 0.3 | 0.4 | 0.1 |
| Inventories | 0.5 | -1.2 | -0.4 | -0.4 | -0.4 |
| Government | 0.1 | -0.3 | 0.3 | 0.2 | 0.1 |
| Net Exports | 0.9 | 0.2 | 0.0 | -0.5 | 0.1 |

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