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FIRST Trust ADVISORS L.P.

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Monday Morning Outlook

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Energizer Bunny Economy – Take Two

When the first iteration of GDP data is released about one month after the end of any quarter, it includes estimates of construction, inventories and trade for the last month of the quarter. As a result, that first government number is often significantly revised.

So, when third quarter real GDP was reported as growing at an annual rate of 3.9%, many worried that as actual September data became available, economic growth would be revised lower.

Instead, almost all the missing data has exceeded government estimates, while other data for previous months has been upwardly revised.

We now expect that when it is released in about two weeks, revised third quarter real GDP growth will increase sharply to 5.3%, the fastest growth in four years. Excluding housing, real GDP likely grew at a 6.6% annual rate in Q3, faster than in all but one quarter during the entire 1990s.

The only problem is that much of this upward revision will be due to a sharp increase in inventories. Unfortunately, this will likely be reversed in Q4 as businesses de-stock. As a result, we are reducing our forecast for real GDP growth in Q4 to 2.5% from our original forecast of 3%. This is still above the consensus, which expects 1.8% growth.

In essence, some of the economic activity we had expected in Q4 got front-loaded into Q3. To us, the inventory-related dip in Q4 is nothing to be concerned about. Final sales of domestic product – which is GDP less inventories – grew roughly 4.2% in Q3 and will likely grow 3.5% in Q4. Consumer confidence may be falling, but GDP remains robust.

In other words, a widely expected slowdown in Q4 GDP will not herald the onset of a serious economic slowdown or recession. It will reflect a somewhat typical inventory swing. The underlying economy remains strong and we stand by our forecast of 3.5% real GDP growth in 2008.

Those making the case for a prolonged slowdown are banking on weaker consumption due to mortgage resets and a drop in housing prices. But our analysis shows that mortgage re-sets will depress consumption growth by no more than 0.2 percentage points per year. Meanwhile, wages and salaries have grown 2 percentage points faster than GDP in the past year.

In addition, resources that were going into housing have shifted and are now showing up in other areas of the economy, like exports, which are up 13.6% in the past year. This is still the Energizer Bunny economy; it keeps going and going and going.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
11-13 / 1:00 pm	Treasury Budget - Oct	-$58.0 Bil	**-$60.3 Bil**		-$49.3 Bil
11-14 / 7:30 am	PPI - Oct	+0.3%	**+0.3%**		+1.1%
7:30 am	"Core" PPI - Oct	+0.2%	**+0.2%**		+0.1%
7:30 am	Retail Sales - Oct	+0.2%	**+0.3%**		+0.6%
7:30 am	"Core" Retail Sales - Oct	+0.3%	**+0.6%**		+0.4%
9:00 am	Business Inventories - Sep	+0.3%	**+0.6%**		+0.1%
11-15 / 7:30 am	CPI - Oct	+0.3%	**+0.3%**		+0.3%
7:30 am	"Core" CPI - Oct	+0.2%	**+0.2%**		+0.2%
7:30 am	Empire State Mfg Index - Nov	20.0	**20.0**		28.8
7:30 am	Initial Claims - Nov 10	320K	**320K**		317K
11:00 am	Philly Fed Survey - Nov	5.0	**6.8**		6.8
11-16 / 8:15 am	Industrial Production - Oct	+0.1%	**+0.1%**		+0.1%
8:15 am	Capacity Utilization - Oct	82.0%	**82.0%**		82.1%