

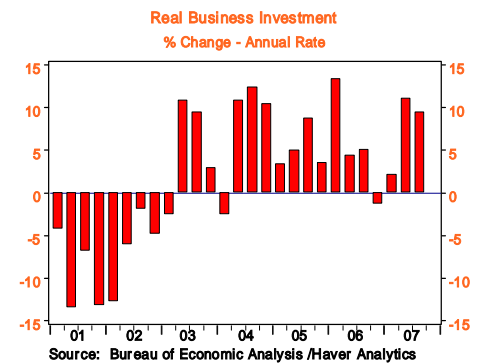
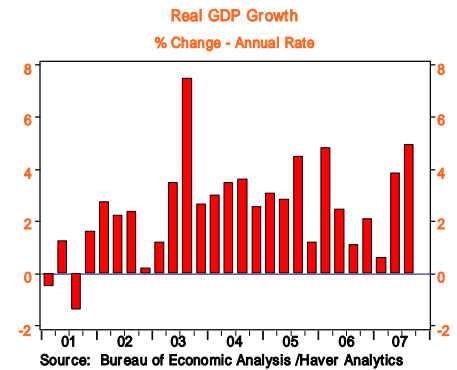
3RD QUARTER GDP (PRELIM)

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- As was widely expected, real GDP in Q3 was upwardly revised to show 4.9% growth at an annual rate, versus the 3.9% originally reported.
- The largest upward revisions were in inventories, which added 1 point to real GDP growth rather than the original estimate of 0.4, and net exports, which added 1.4 points to growth (the largest since 1996) versus the original estimate of 0.9. Business investment was also revised up while personal consumption was revised down to a still healthy 2.7% growth rate.
- Housing was a major drag, lopping off 1 point from real GDP growth. Excluding housing, real GDP grew at a 6.1% annual rate in Q3 and is up 3.8% versus a year ago – the largest one-year expansion since 2000.
- The GDP price index rose at a 0.9% rate in Q3 and is up 2.4% versus last year. Nominal GDP growth – real GDP plus inflation – grew at a 5.9% rate in Q3.

Implications: The economy boomed in Q3, shrugging off any impact from credit market problems. Outside the housing sector, the real economy has been stronger in the past year than at any time since 2000 – when the dot.com boom and Y2K-related spending boosted growth. While some are suggesting that this growth is now in the rearview mirror, this is an oversimplification. Nominal GDP growth – real GDP plus inflation – has climbed at an annual rate of 5.8% in the past three quarters. This is a significant acceleration from the housing-related slowdown of Q3/2006 to Q1/2007, when nominal GDP grew at just a 4% rate.

This kind of acceleration in nominal GDP growth does not happen when the Federal Reserve is tight. Although after-tax corporate profits were unchanged versus Q2 they were up 2.7% versus a year ago and businesses still have more than \$1 trillion in cash on hand. Meanwhile, the annual rate of labor compensation – wages, salaries, and fringe benefits – is running \$475 billion higher than last year, the largest gain in history. With so much purchasing power on the part of businesses and consumers, we continue to believe the year ahead will show strong growth, not weakness.



3rd Quarter GDP <i>Seasonally Adjusted Annual Rates</i>	Q3-07	Q2-07	Q1-07	Q4-06	4 Quarter Change
Real GDP	4.9%	3.8%	0.6%	2.1%	2.8%
GDP Price Index	0.9%	2.6%	4.2%	1.7%	2.4%
Nominal GDP	5.9%	6.6%	4.9%	3.8%	5.3%
PCE	2.7%	1.4%	3.7%	3.9%	2.9%
Business Investment	9.4%	11.0%	2.1%	-1.4%	5.2%
Structures	14.3%	26.2%	6.3%	7.5%	13.3%
Equipment and Software	7.2%	4.7%	0.3%	-4.9%	1.7%
Contributions to GDP Growth (p.pts.)	Q3-07	Q2-07	Q1-07	Q4-06	4Q Avg.
PCE	1.9	1.0	2.6	2.7	2.0
Business Investment	1.0	1.1	0.2	-0.2	0.5
Residential Investment	-1.0	-0.6	-0.9	-1.0	-0.9
Inventories	1.0	0.2	-0.7	-1.3	-0.2
Government	0.8	0.8	-0.1	0.7	0.5
Net Exports	1.4	1.3	-0.5	1.3	0.9