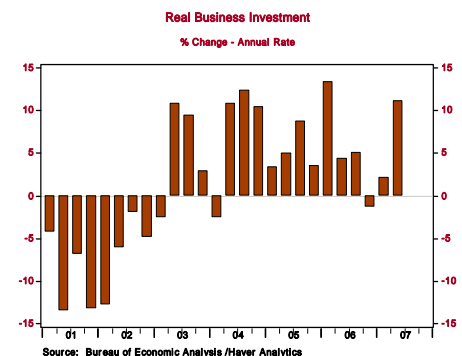
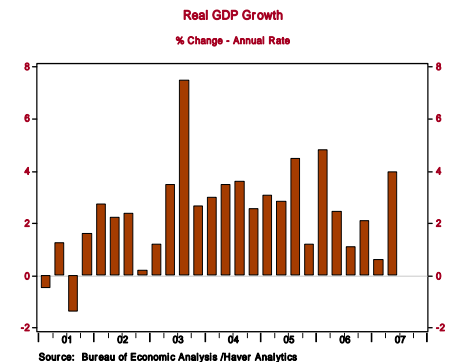


2ND QUARTER GDP (PRELIMINARY)

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA
Economic Research Analyst – Trevor D. Scott

- Real GDP in Q2 was upwardly revised to show 4.0% growth at an annual rate versus the 3.4% originally reported. The consensus expected 4.1%.
- Business investment was the key source of the upward revision, contributing 1.1 percentage points to real GDP growth rather than the 0.8 points originally reported. Business construction grew at a 27.7% rate in Q2, the fastest in more than 25 years. The contribution to real GDP growth from international trade (net exports) was revised up to 1.4 points from 1.2. Personal consumption was revised up slightly while home building was revised down slightly.
- The housing sector continued to drag down GDP growth in Q2. Without housing, real GDP grew 4.7% in Q2.
- The GDP price index rose at a 2.7% annual rate in the second quarter. Nominal GDP growth – real GDP plus inflation – grew at a 6.7% rate. Non-housing nominal GDP growth was 7.8% - a sign that Fed policy is not tight.

Implications: Today's GDP report confirms our view that outside the housing sector the economy is performing very well and growth is likely to continue at a solid pace. Corporate profits increased at a 27.9% annual rate in Q2, the fastest since early 2006. Meanwhile, the boom in exports easily offset the drag from housing and with a weak dollar should continue to do so in the year ahead. Inflation remains our main concern. Although the core consumption (PCE) deflator increased at only a 1.3% annual rate in Q2, the smallest increase in four years, overall PCE prices increased at a 4.2% rate. In other news, initial claims for jobless benefits increased for the fifth straight week to 334,000. We think a large part of the upswing (perhaps all) is due to problems with seasonally-adjusting the data for annual auto retooling. Auto plants usually have temporary layoffs in July to retool plants. There were fewer seasonal layoffs this year as some automakers prepare for potential strikes. So the seasonally-adjusted claims data were artificially low in July and are now probably artificially high.



2nd Quarter GDP <i>Seasonally Adjusted Annual Rates</i>	Q2-07	Q1-07	Q4-06	Q3-06	4 Quarter Change
Real GDP	4.0%	0.6%	2.1%	1.1%	1.9%
GDP Price Index	2.7%	4.2%	1.7%	2.4%	2.7%
Nominal GDP	6.7%	4.9%	3.8%	3.4%	4.7%
PCE	1.4%	3.7%	3.9%	2.7%	2.9%
Business Investment	11.1%	2.1%	-1.4%	5.1%	4.1%
Structures	27.7%	6.3%	7.5%	10.8%	12.8%
Equipment and Software	4.2%	0.3%	-4.9%	2.9%	0.6%
Contributions to GDP Growth (p.pts.)	Q2-07	Q1-07	Q4-06	Q3-06	4Q Avg.
PCE	1.0	2.6	2.7	1.9	2.0
Business Investment	1.1	0.2	-0.2	0.5	0.4
Residential Investment	-0.6	-0.9	-1.0	-1.3	-1.0
Inventories	0.2	-0.7	-1.3	0.1	-0.4
Government	0.8	-0.1	0.7	0.1	0.4
Net Exports	1.4	-0.5	1.3	-0.3	0.5