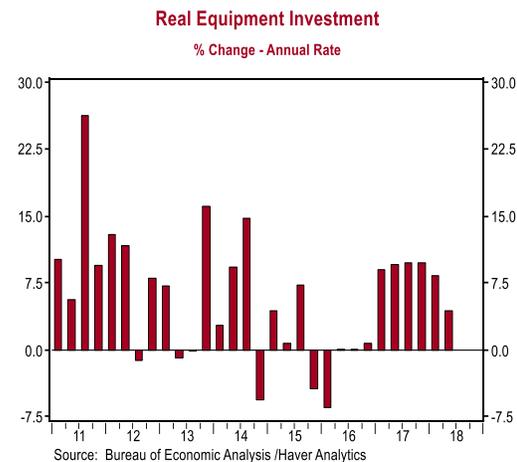
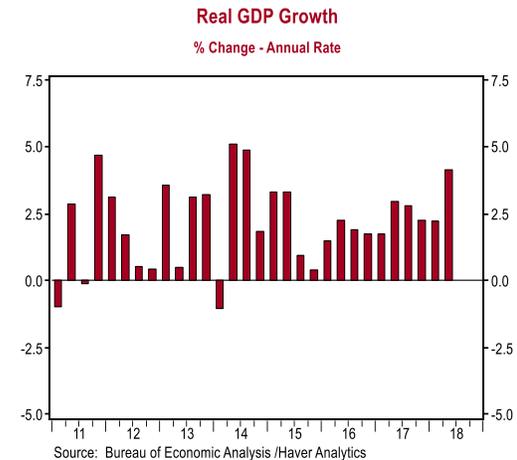


2nd Quarter GDP (Final)

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- Real GDP growth in Q2 was unrevised, coming in at a 4.2% annual rate, matching consensus expectations.
- A downward revision to inventories was offset by small upward revisions to most other GDP components.
- The largest positive contribution to the real GDP growth rate in Q2 came from consumer spending. The weakest component, by far, was inventories.
- The GDP price index was unrevised at a 3.0% annual rate. Nominal GDP growth – real GDP plus inflation – rose 7.6%, unchanged from the prior estimate. Nominal GDP is up 5.4% versus a year ago.

Implications: Today’s final GDP report for the second quarter showed the same strong pace of growth that was estimated last month, but with a smaller increase in corporate profits compared to prior readings. Real GDP grew at a 4.2% annual rate in Q2, unchanged from last month’s estimate. The mix of revisions from the previous estimate were a bit more positive as well, with inventories declining by more than expected, while most other categories were revised slightly higher. In turn, weaker inventories means more room for stocking shelves and showrooms in the third quarter. “Core” real GDP, which strips out inventories, net exports, and government purchases rose at a healthy 4.3% annual rate in the second quarter and is up at a 3.1% annual rate in the past two years. And with just a few days left in September, we’re estimating that real GDP grew at around a 4.0% annual rate in Q3. The impacts of Hurricane Florence will be felt in the Q3 GDP data, but it should not have been a major drag on production in spite of the property damage as well as human toll. It’s not unusual to see a bump in real GDP following major storms as rebuilding and replacement of damaged property begins, though, [as we mentioned after Harvey](#), that doesn’t mean the short-term pickup in growth is good news. Regardless, today’s reading on growth, an unemployment rate at 3.9%, and inflation readings hovering over 2% show that the Fed’s signaling of an additional rate hike in December is clearly warranted. Nominal GDP growth – real GDP growth plus inflation – is up 5.4% from a year ago and up 4.6% annualized in the past two years, much too high for short-term interest rates at or below 2.25%. In addition to the strong growth rate in the economy, today’s report also provided a second look at overall corporate profits, but unlike the GDP reading, corporate profits were revised modestly lower. Profits rose 3.0% in Q2 compared to an originally reported increase of 3.3%. However, profits are still up a healthy 7.3% in the past year. Plugging this data into our capitalized profits model suggests that, even with 10-year Treasury rates at 3.5% (compared to sub-3.1% rates today), stocks are still cheap. As a whole, economic growth in Q2 was very strong, and Q3 looks likely to continue this trend. In other news this morning, new claims for unemployment benefits rose 12,000 last week to 214,000, while continuing claims declined 16,000 to 1.66 million. Expect Hurricane Florence to temporarily depress payroll growth in September, followed by a rebound for October.



2nd Quarter GDP Seasonally Adjusted Annual Rates	Q2-18	Q1-18	Q4-17	Q3-17	4-Quarter Change
Real GDP	4.2%	2.2%	2.3%	2.8%	2.9%
GDP Price Index	3.0%	2.0%	2.5%	2.2%	2.4%
Nominal GDP	7.6%	4.3%	5.1%	4.8%	5.4%
PCE	3.8%	0.5%	3.9%	2.2%	2.6%
Business Investment	8.7%	11.5%	4.9%	3.4%	7.1%
Structures	14.5%	13.9%	1.3%	-5.8%	5.6%
Equipment	4.6%	8.5%	9.9%	9.8%	8.2%
Intellectual Property	10.5%	14.1%	0.7%	1.7%	6.6%
Contributions to GDP Growth (p.pts.)	Q2-18	Q1-18	Q4-17	Q3-17	4Q Avg.
PCE	2.6	0.4	2.6	1.5	1.8
Business Investment	1.2	1.5	0.6	0.5	0.9
Residential Investment	-0.1	-0.1	0.4	0.0	0.1
Inventories	-1.2	0.3	-0.9	1.0	-0.2
Government	0.4	0.3	0.4	-0.2	0.2
Net Exports	1.2	0.0	-0.9	0.0	0.1