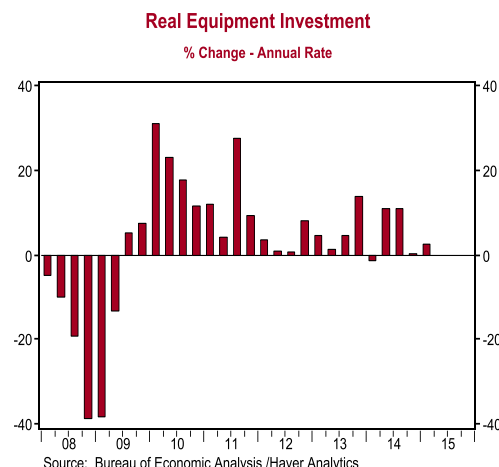
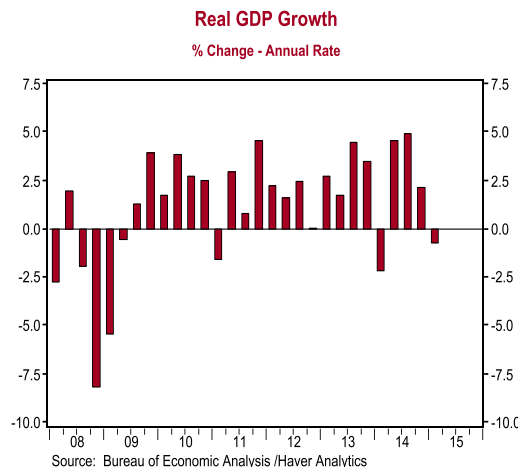


1st Quarter GDP (Preliminary)

Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Dep. Chief Economist
Strider Elass – Economist

- Real GDP was revised to a -0.7% annual rate in Q1 from a prior estimate of +0.2%. The consensus expected -0.9%.
- The largest downward revisions were for net exports and inventories. Business investment in equipment and home building were revised higher.
- The largest positive contribution to the real GDP growth rate in Q1 was personal consumption. The weakest component, by far, was net exports.
- The GDP price index was unrevised at a -0.1% annual rate. Nominal GDP growth – real GDP plus inflation – was revised down to a -0.9% annual rate from a prior estimate of 0.1%.

Implications: Look out for the Pouting Pundits of Pessimism calling for a recession. Today’s GDP report showed contraction, but the report is for Q1, the last days of which ended two months ago, so it’s a “rearview mirror” picture of the economy and very likely a distorted one. Real GDP growth was revised down to a -0.7% annual rate from an original estimate of +0.2%. But as we have always argued, there were three main temporary culprits behind the Q1 weakness: plummeting energy prices, bad weather, and West Coast port strikes – all of which have dissipated. Also, part of the downward revision was due to lower inventories, which leaves more room for growth in future quarters. There also seems to be a fourth factor that held down growth in Q1 and it has nothing to do with actual output, but how the government seasonally adjusts the data. A study from the Federal Reserve shows that the government hasn’t been adjusting the data correctly based on the time of year. In turn, the wrong adjustments have meant growth looks artificially low in the first quarter, and artificially high in other quarters. The average for the year is the same, but it should be spread out more evenly than the government data now show. Luckily, the government is aware of the problem and will release new seasonal adjustment methods for GDP in late July. This puts the Fed in an interesting place. If the data are really better than what the government now says, and if the economic data continue to show a pick-up in activity, a June rate hike does not seem like much of a stretch. Today’s report also provided the first glimpse at overall corporate profits, and just like GDP, the headline was ugly. Corporate profits fell 5.9% in Q1, but the drop in both real GDP and profits resembles what happened in the first quarter of last year, after which profits rebounded sharply. Keep in mind that despite the drop in Q1, corporate profits are still up 3.7% from a year ago. In other news yesterday, pending home sales (contracts on existing homes) increased 3.4% in April, hitting a nine-year high. This report suggests existing home sales, which are counted at closing, will show a solid gain in May. Also yesterday, initial claims increased 7,000 last week to 282,000 and continuing claims increased 11,000 to 2.22 million. Plugging these figures into our payroll models suggests a nonfarm gain of 234,000 in May. (The forecast will change as we get more data in the next week on claims, the ADP index, and consumer spending.)



1st Quarter GDP <i>Seasonally Adjusted Annual Rates</i>	Q1-15	Q4-14	Q3-14	Q2-14	4-Quarter Change
Real GDP	-0.7%	2.2%	5.0%	4.6%	2.7%
GDP Price Index	-0.1%	0.1%	1.4%	2.1%	0.9%
Nominal GDP	-0.9%	2.4%	6.4%	6.8%	3.6%
PCE	1.8%	4.4%	3.2%	2.5%	3.0%
Business Investment	-2.8%	4.7%	8.9%	9.7%	5.0%
Structures	-20.8%	5.9%	4.8%	12.6%	-0.2%
Equipment	2.7%	0.6%	11.0%	11.2%	6.3%
Intellectual Property	3.6%	10.3%	8.8%	5.5%	7.0%
Contributions to GDP Growth (p.pts.)	Q1-15	Q4-14	Q3-14	Q2-14	4Q Avg.
PCE	1.2	3.0	2.2	1.8	2.0
Business Investment	-0.4	0.6	1.1	1.2	0.6
Residential Investment	0.2	0.1	0.1	0.3	0.2
Inventories	0.3	-0.1	0.0	1.4	0.4
Government	-0.2	-0.4	0.8	0.3	0.1
Net Exports	-1.9	-1.0	0.8	-0.3	-0.6

This report was prepared by First Trust Advisors L. P., and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.