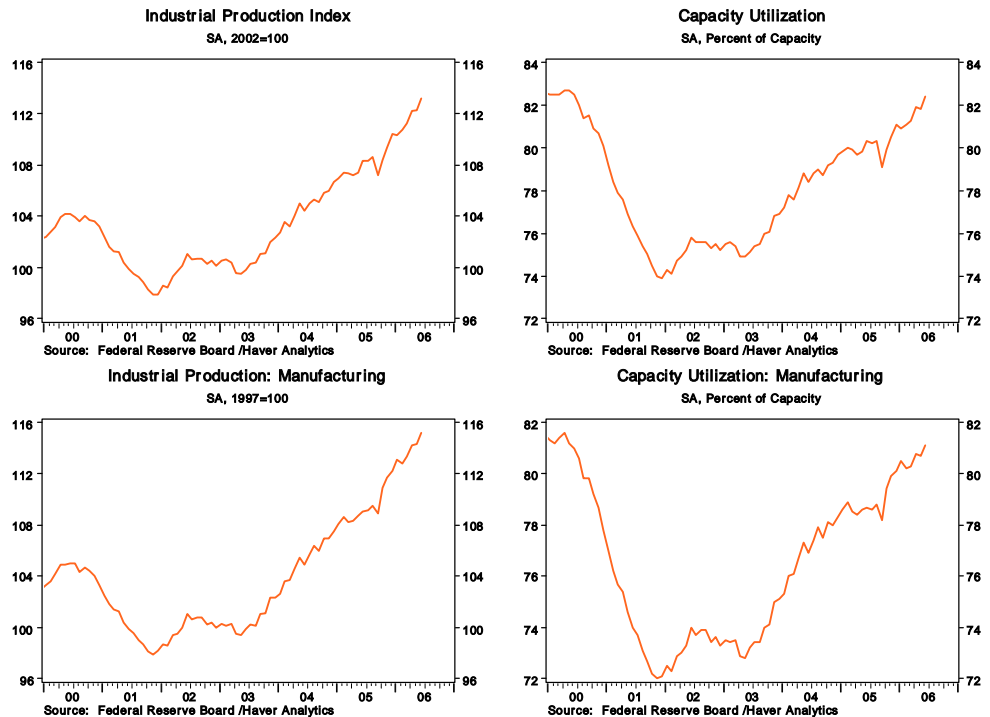


JUNE INDUSTRIAL PRODUCTION / CAPACITY UTILIZATION

Brian S. Wesbury
Chief Economist
Bill Mulvihill
Senior Economist

- Industrial production increased 0.8% in June after an upwardly revised 0.1% gain in May (originally -0.1%). Industrial production is up 7.4% at an annual rate in the past three months and 4.5% in the past year.
- Manufacturing production also increased 0.8% in June, while manufacturing production excluding motor vehicles rose 0.5%. In the past year, manufacturing production is up 5.7%; or 5.9% when motor vehicle output is removed. Mining output rose 1.2% and utility output increased 0.7%.
- Capacity utilization jumped to 82.4% in June, the highest in six years.

Implications: Industrial production surpassed consensus expectations in June, led by a 2.2% surge in durable consumer goods production. Moreover, business equipment production rose 0.7% in June and is up 12.3% in the past year, the second fastest YOY gain since 1998 (only the 12-months ending in April was faster). This supply-side of the economy is booming, which suggests that any weakness in Q2 real GDP will be temporary. Both overall industrial production and manufacturing output rose to record high levels in June. Even in an environment of high energy costs and competition from China, US manufacturers have *never* produced more “stuff.” This surge in production is boosting capacity utilization – which has now back at levels not seen since 2000. These developments put the Fed in a quandary. While we do not believe tight capacity leads to inflation (capacity is not fixed as the surge in business equipment spending demonstrates), the Fed’s Phillips Curve models do make this assumption. With capacity utilization high and unemployment low, the Fed is likely to remain in a tightening mode. The business media is currently fixated on the notion that something in the economy has changed and that the 3-year period of robust growth is nearing an end. But today’s data shows that nothing has really changed at all. Economic growth is strong, manufacturing is booming and inflationary pressures continue to build.



Industrial Production Capacity Utilization <i>All data seasonally adjusted</i>	Jun-06	May-06	Apr-06	3-mo % Ch <i>annualized</i>	6-mo % Ch. <i>annualized</i>	Yr over yr % Ch.
Industrial Production	0.8%	0.1%	0.8%	7.4%	5.1%	4.5%
Manufacturing	0.8%	0.1%	0.8%	6.9%	5.4%	5.7%
Manufacturing Ex. Motor Vehicles	0.5%	0.3%	0.9%	6.9%	5.0%	5.9%
Business Equipment	0.7%	-0.2%	2.2%	11.6%	10.7%	12.3%
Durable Consumer Goods	2.2%	-0.5%	-0.5%	5.2%	5.8%	3.3%
Nondurable Consumer Goods	0.4%	0.4%	0.2%	3.9%	0.8%	1.1%
High-Tech Equipment	1.1%	2.0%	1.6%	20.2%	14.9%	22.0%
Total Ex. High-Tech Equipment	0.7%	0.1%	0.7%	6.5%	4.5%	3.7%
Mining	1.2%	0.4%	1.4%	12.8%	12.3%	0.4%
Utilities	0.7%	0.3%	0.3%	5.0%	-4.2%	-1.3%
Capacity Utilization	82.4	81.8	81.9	82.0	81.6	80.9
Manufacturing	81.1	80.7	80.8	80.9	80.6	79.9
Mining	91.1	89.9	89.4	90.1	89.0	86.7
Utilities	86.8	86.3	86.1	86.4	85.0	86.2

Source: Federal Reserve Board

*CapU data: % of capacity & 3, 6, 12 month averages

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.