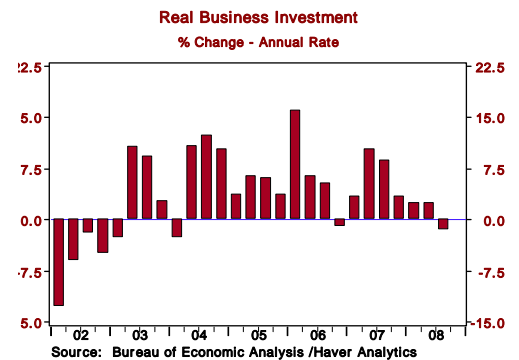
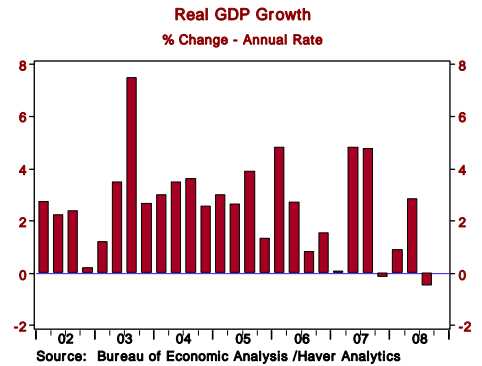


3RD QUARTER GDP (PRELIM)

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA

- Real GDP was revised down slightly to a -0.5% annual growth rate in Q3, matching consensus expectations. Real GDP is up 0.7% versus a year ago.
- Almost all major categories of GDP were revised downward, with the largest adjustment to personal consumption. Consumption subtracted 2.7 points from real GDP growth in Q3, versus the original estimate of -2.3. The lone exception to the downward adjustments was inventories, which added 0.9 points to real GDP growth rather than the original estimate of 0.6.
- The largest drag on real GDP in Q3 was personal consumption. The largest positive contributors to GDP were net exports, government spending, and inventories.
- The GDP price index was unrevised at a 4.2% annual rate in Q3. Nominal GDP growth – real GDP plus inflation – was revised down to a 3.6% growth rate in Q3 versus an original estimate of 3.8%.

Implications: Real GDP growth was revised down slightly to a -0.5% annual rate from the -0.3% rate estimated last month. However, the overall report on the economy had a mixed message. The only major component of GDP that was revised upward was inventories, which reinforces our view that the fourth quarter may be the worst for real GDP growth since 1982. The silver lining is that domestic profits outside the financial sector (pre-tax, with inventory and capital consumption adjustments) increased at a 26.8% annual rate in Q3, the fastest increase in two years. All the decline in overall profits is attributable to the financial sector, which we already knew was in deep trouble. Once the current “risk aversion hysteria” passes, higher profits among non-financial firms will translate into more capital investment and hiring. In other news this morning, the Richmond Fed Index, a measure of manufacturing in that Federal Reserve Bank region, dropped to -38 in November, the lowest level on record going back to the early 1990s. Meanwhile, the Case-Shiller index showed that as of September home prices in 20 major metropolitan areas around the country were down 17.4% versus last year. We expect more steep home price declines in these areas in the year ahead, although home prices are starting to flatten out in some regions.



3rd Quarter GDP <i>Seasonally Adjusted Annual Rates</i>	Q3-08	Q2-08	Q1-08	Q4-07	4-Quarter Change
Real GDP	-0.5%	2.8%	0.9%	-0.2%	0.7%
GDP Price Index	4.2%	1.1%	2.6%	2.8%	2.7%
Nominal GDP	3.6%	4.1%	3.5%	2.3%	3.4%
PCE	-3.7%	1.2%	0.9%	1.0%	-0.2%
Business Investment	-1.5%	2.5%	2.4%	3.4%	1.7%
Structures	6.6%	18.4%	8.7%	8.6%	10.5%
Equipment and Software	-5.6%	-5.0%	-0.5%	1.0%	-2.6%
Contributions to GDP Growth (p.pts.)	Q3-08	Q2-08	Q1-08	Q4-07	4Q Avg.
PCE	-2.7	0.9	0.6	0.7	-0.1
Business Investment	-0.2	0.3	0.3	0.4	0.2
Residential Investment	-0.7	-0.5	-1.1	-1.3	-0.9
Inventories	0.9	-1.5	0.0	-1.0	-0.4
Government	1.1	0.8	0.4	0.2	0.6
Net Exports	1.1	2.9	0.8	0.9	1.4

Source: Commerce Department