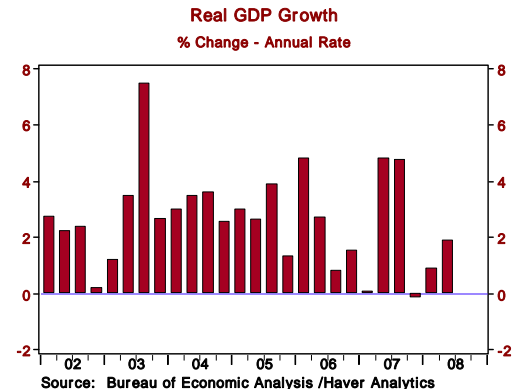


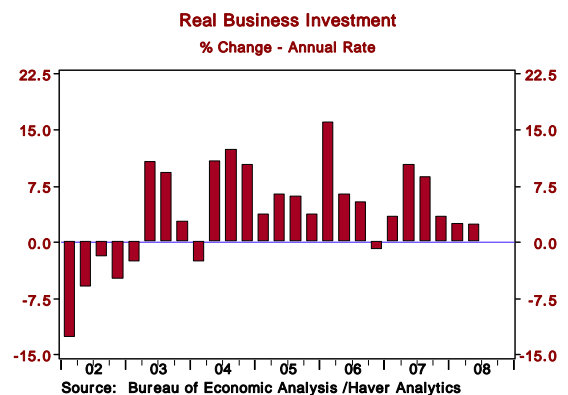
2ND QUARTER GDP (ADVANCE)

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

- The first estimate for Q2 real GDP growth is 1.9% at an annual rate versus a consensus expected 2.3%. Real GDP is up 1.8% versus last year.
- The strongest component of real GDP was net exports, which added 2.4 points to the real GDP growth rate, the most in any quarter since 1980.
- The largest drag on real GDP was inventories, which had the second largest decline in history and subtracted 1.9 points from growth. Real final sales (real GDP ex-inventories) grew at a 3.9% rate in Q2 and are up 2.4% versus a year ago. Home building subtracted 0.6 points from growth in Q2, the smallest drag from this sector in a year.
- The GDP price index rose at a 1.1% annual rate in Q2 and is up 2.0% versus last year. Nominal GDP – real GDP plus inflation – grew at a 3.0% rate in Q2 and is up 3.8% versus a year ago.



Implications: The government’s estimate of a 1.9% real GDP growth rate in Q2 included the assumption of a massive decline in inventories. We believe this decline is overstated and expect large upward revisions. Real final sales – real GDP excluding inventories – grew at a 3.9% annual rate in Q2 and are up 2.4% versus last year. These are nowhere close to recessionary numbers. Many analysts are dwelling on the revision of Q4.2007 real GDP growth to a negative 0.2%. However, the government added a full point to real GDP growth in Q2.2007. So the lone one quarter decline followed two quarters in which real GDP grew at a booming 4.8% annual rate. Since Q4, real GDP has accelerated, growing at a 0.9% rate in Q1 and at a 1.9% rate in Q2. Meanwhile, despite a headline GDP deflator that appears benign, the gross domestic purchases deflator (the measure of prices for what we buy) rose at a 4.2% rate and is up 3.7% versus a year ago. In other news this morning, initial claims for unemployment insurance increased 44,000 last week to 448,000. However, data is typically volatile at this time of year due to auto plant re-tooling and the Labor Department says many extra workers re-applied for benefits due to the recently enacted extension of jobless benefits, so the data are not directly comparable to previous periods. Also reported this morning was an increase in the Chicago PMI to 50.8, showing an expansion of manufacturing activity in that key region, to the highest level in six months.



2nd Quarter GDP <i>Seasonally Adjusted Annual Rates</i>	Q2-08	Q1-08	Q4-07	Q3-07	4-Quarter Change
Real GDP	1.9%	0.9%	-0.2%	4.8%	1.8%
GDP Price Index	1.1%	2.6%	2.8%	1.5%	2.0%
Nominal GDP	3.0%	3.5%	2.3%	6.4%	3.8%
PCE	1.5%	0.9%	1.0%	2.0%	1.3%
Business Investment	2.3%	2.4%	3.4%	8.7%	4.2%
Structures	14.3%	8.7%	8.6%	20.6%	12.9%
Equipment and Software	-3.4%	-0.5%	1.0%	3.6%	0.1%
Contributions to GDP Growth (p.pts.)	Q2-08	Q1-08	Q4-07	Q3-07	4Q Avg.
PCE	1.1	0.6	0.7	1.4	1.0
Business Investment	0.3	0.3	0.4	0.9	0.4
Residential Investment	-0.6	-1.1	-1.3	-1.1	-1.0
Inventories	-1.9	0.0	-1.0	0.7	-0.6
Government	0.7	0.4	0.2	0.8	0.5
Net Exports	2.4	0.8	0.9	2.0	1.5

Source: Commerce Department