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2ND QUARTER GDP (ADVANCE)

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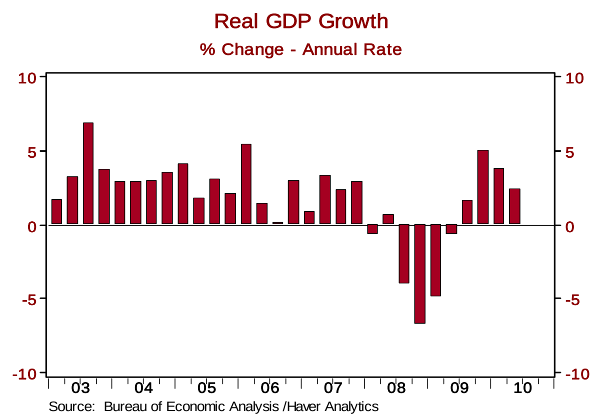
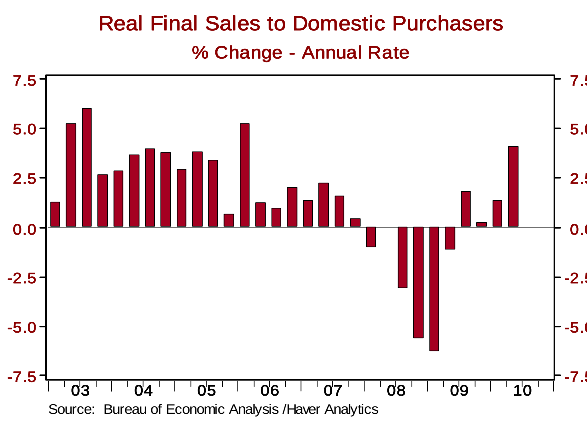
- The first estimate for Q2 real GDP growth is 2.4% at an annual rate, very close to the consensus expected pace of 2.6%.
- The largest positive contributions to the real GDP growth rate, in order, were business investment in equipment & software, personal consumption, and inventories.
- The weakest component of real GDP, by far, was net exports.
- The GDP price index increased at a 1.8% annual rate in Q2. Nominal GDP – real GDP plus inflation – rose at a 4.3% rate in Q2 and is now up 4.0% versus a year ago.





Implications: Real GDP expanded at a 2.4% annual rate in Q2 and is up 3.2% in the past year, undermining the case for a double-dip recession. The modest increase in Q2 came despite the government assuming we had a large surge in imports and a drop in exports in June. This assumption caused international trade to be a drag of 2.8 percentage points on the GDP growth rate. That's the biggest negative for trade in more than 25 years and the key reason why our forecast of 3.4% growth was too high. We think the actual trade data will not be as bad, resulting in upward revisions to real growth. Regardless, the big question for many is whether *domestic* demand is strong enough to sustain a recovery. Today's data show it is. Excluding trade and inventories, real (inflation-adjusted) final sales to domestic purchasers increased at a 4.1% annual rate, the second fastest pace since 2003. Business investment increased at a 17% annual rate, the second fastest gain since 1997. In addition, today's data include a "benchmark revision" that alters numbers going back the last five years. As it turns out, incomes have been higher than previously estimated and the personal saving rate is now at 6.2% of after-tax income, similar to where it was in the early 1990s. On the inflation front, GDP prices increased at a 1.8% rate in Q2 and nominal GDP (real GDP growth plus inflation) is up 4% versus last year, too fast to keep the federal funds rate at zero. While many analysts dwell on the modest GDP number for Q2, the more timely Chicago PMI, a measure of manufacturing in the Midwest, increased to 62.3 in July versus 59.1 in June. Yesterday's news showed new claims for unemployment insurance down 11,000 from the prior week. Continuing claims for regular state benefits increased 81,000 to 4.57 million.

2nd Quarter GDP *Seasonally Adjusted Annual Rates*	*Q2-10*	*Q1-10*	*Q4-09*	*Q3-09*	*4-Quarter Change*
Real GDP	**2.4%**	3.7%	5.0%	1.6%	3.2%
GDP Price Index	**1.8%**	1.0%	-0.2%	0.7%	0.8%
Nominal GDP	**4.3%**	4.8%	4.7%	2.3%	4.0%
PCE	**1.6%**	1.9%	0.9%	2.0%	1.6%
Business Investment	**17.0%**	7.8%	-1.4%	-1.7%	5.2%
Structures	**5.1%**	-17.8%	-29.2%	-12.4%	-14.4%
Equipment and Software	**21.9%**	20.5%	14.6%	4.2%	15.1%
Contributions to GDP Growth (p.pts.)	**Q2-10**	**Q1-10**	**Q4-09**	**Q3-09**	**4Q Avg.**
PCE	**1.2**	1.3	0.7	1.4	1.1
Business Investment	**1.5**	0.7	-0.1	-0.1	0.5
Residential Investment	**0.6**	-0.3	0.0	0.3	0.1
Inventories	**1.1**	2.6	2.8	1.1	1.9
Government	**0.9**	-0.3	-0.3	0.3	0.2
Net Exports	**-2.8**	-0.3	1.9	-1.4	-0.6

Source: Commerce Department