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November 7, 2013 • 630.517.7756 • www.ftportfolios.com

Third Quarter GDP (Advance)

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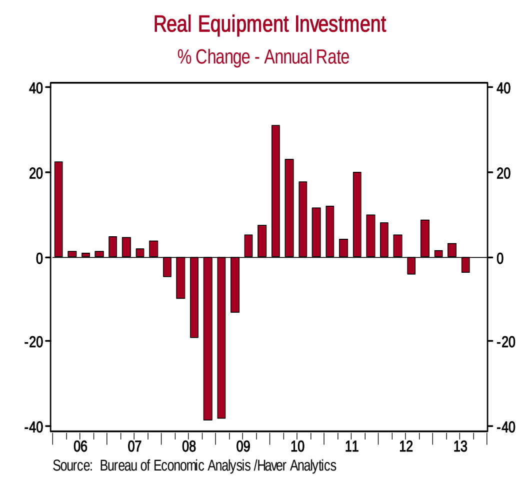
- The first estimate for Q3 real GDP growth is 2.8% at an annual rate, beating the 2.0% the consensus expected. Real GDP is up 1.6% from a year ago.
- The largest positive contributions to the Q3 real GDP growth rate were consumer spending and inventories. The only drag was business investment in equipment.
- Personal consumption, business investment, and home building were all positive in Q3, growing at a combined rate of 2.0% annualized. Combined, they are up 2.4% in the past year.
- The GDP price index increased at a 1.9% annual rate in Q3. Nominal GDP – real GDP plus inflation – rose at a 4.8% rate in Q3 and is up 3.1% from a year ago and up at a 3.9% annual rate from two years ago.

Implications: Real GDP growth surprised to the upside in Q3, growing at a 2.8% annual rate. But don't get too excited about the report; the upside surprise was mostly due to higher inventories. As a result, we're marking down our forecast for real GDP growth in Q4 to the 1 – 1.5% range from a prior forecast of 2%. In other words, the economy was a plow horse yesterday and remains one today. Confirming this, real GDP outside of government, trade, and inventories grew at a modest 2% pace in Q3. The best news in the report was the continued recovery in home building, up at a 14.6% annual rate in Q3. The worst news was that business investment in equipment declined at a 3.7% annual rate in Q3. Given record profits, ample cash on corporate balance sheets, and loose monetary policy, we expected equipment investment to be better by this point in the recovery, although, for those same reasons, we still expect equipment investment to pick up in the year ahead. Today's report certainly gives the Federal Reserve something to think about. Nominal GDP – real GDP plus inflation – rose at a 4.8% rate in Q3 and is up at a 3.9% annual rate in the past two years, versus an average of 3.8% in the past decade. This is too fast for a short-term interest rate target near zero and suggests the Fed could quickly end quantitative easing without hurting the economy. Regardless, we expect the Fed to maintain the current pace of long-term asset purchases through March and then take its sweet time tapering QE through late next year. In other news today, new claims for unemployment insurance fell 9,000 last week to 336,000. Continuing claims for regular state benefits rose 4,000 to 2.87 million. The Labor Department releases the October payroll report tomorrow morning and our final forecast is a gain of 90,000 non-farm, 125,000 private. Not bad considering the partial government shutdown and, if we're right, we expect a sharp acceleration in job growth in November.



3rd Quarter GDP Seasonally Adjusted Annual Rates	Q3-13	Q2-13	Q1-13	Q4-12	4-Quarter Change
Real GDP	**2.8%**	2.5%	1.1%	0.1%	1.6%
GDP Price Index	**1.9%**	0.6%	1.3%	1.1%	1.3%
Nominal GDP	**4.8%**	3.1%	2.8%	1.6%	3.1%
PCE	**1.5%**	1.8%	2.3%	1.7%	1.8%
Business Investment	**1.6%**	4.7%	-4.6%	9.8%	2.7%
Structures	**12.3%**	17.6%	-25.7%	17.5%	3.6%
Equipment	**-3.7%**	3.2%	1.6%	8.9%	2.4%
Intellectual Property	**2.2%**	-1.5%	3.8%	5.7%	2.5%
Contributions to GDP Growth (p.pts.)	**Q3-13**	**Q2-13**	**Q1-13**	**Q4-12**	**4Q Avg.**
PCE	**1.0**	1.2	1.5	1.1	1.2
Business Investment	**0.2**	0.6	-0.6	1.1	0.3
Residential Investment	**0.4**	0.4	0.3	0.5	0.4
Inventories	**0.8**	0.4	0.9	-2.0	0.0
Government	**0.0**	-0.1	-0.8	-1.3	-0.5
Net Exports	**0.3**	-0.1	-0.3	0.7	0.2