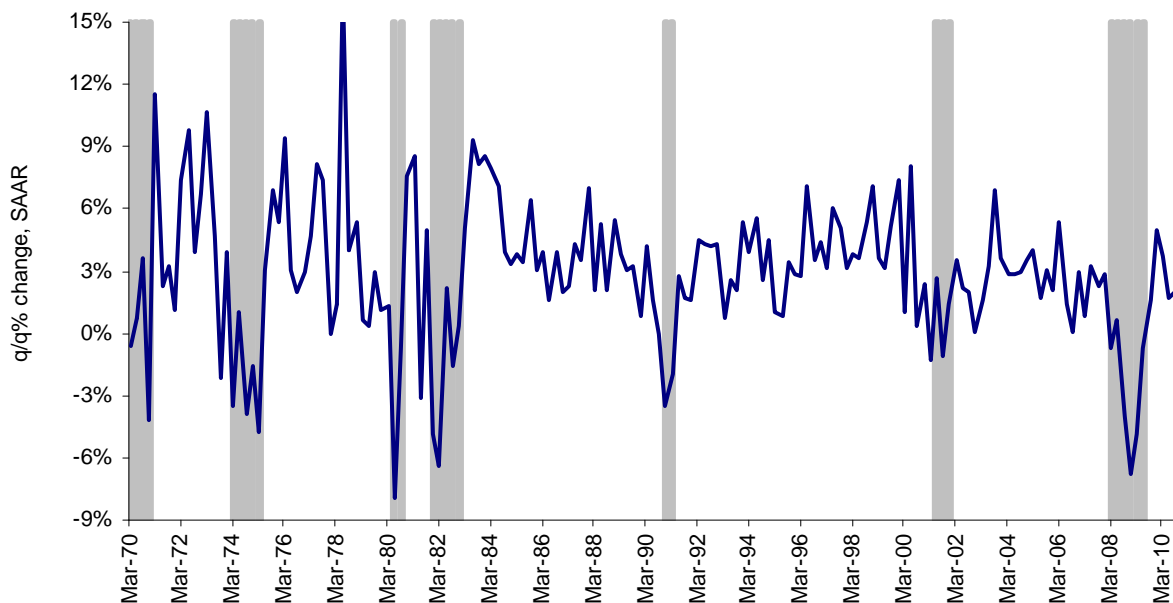


October 29, 2010

GDP Report Shows Slow Growth

Third quarter GDP showed relatively weak 2% real growth, but stronger than the second quarter's 1.7%. We expect a further pickup in the fourth quarter to 3.5% based on an acceleration in income to avoid the likely January tax increase, our expectation of a good Christmas season due to pentup demand, the gradual improvement in the labor environment and strong corporate profits.

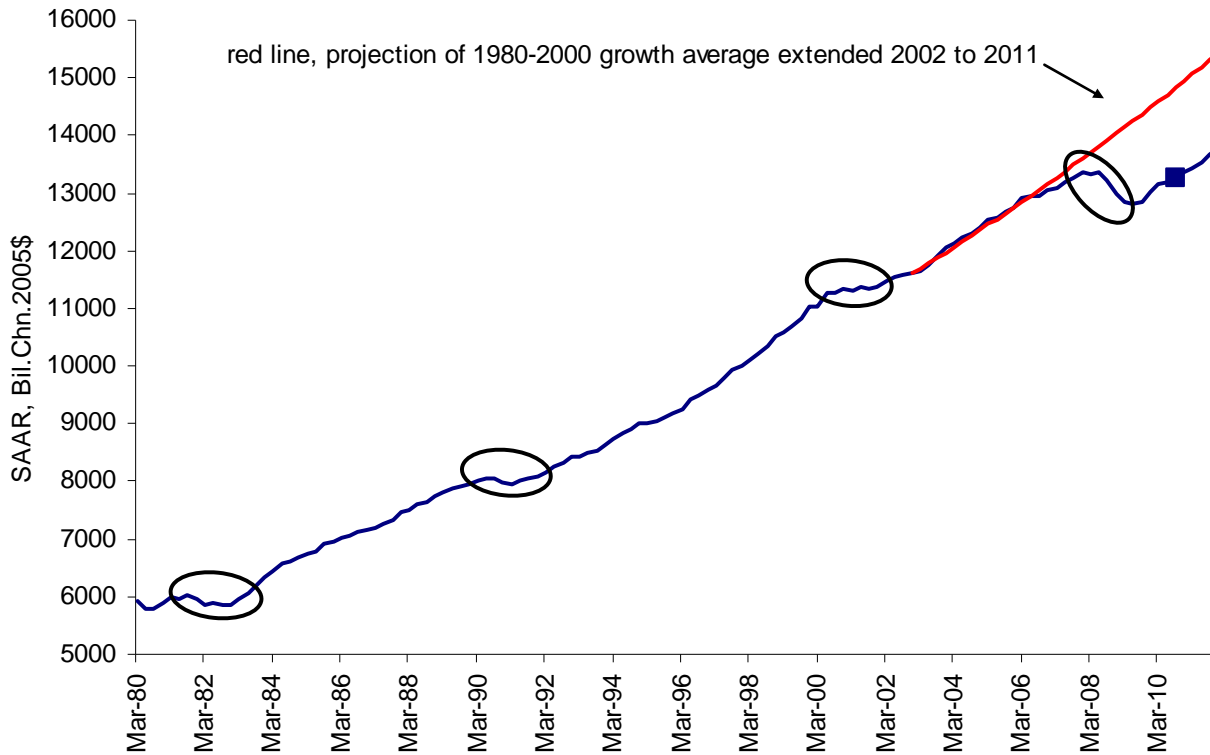
US Real GDP Growth (q/q change, last obs. Q3 2010)



Source: Bureau of Economic Analysis; Encima Global

- We think the economy is in a sustainable but sluggish expansion starting from a much deeper recession than the previous three (1980s, 1990s, 2000s). It's not a double dip because of cyclical factors like auto demand, monetary stimulus and relatively strong foreign growth. It's not a normal V-shaped rebound because of anti-growth Washington policies – small business credit, weak dollar, likely tax increase, regulatory confusion, housing mess, etc. **Slow growth from a low base means painfully high unemployment and a series of rolling debt crises.**

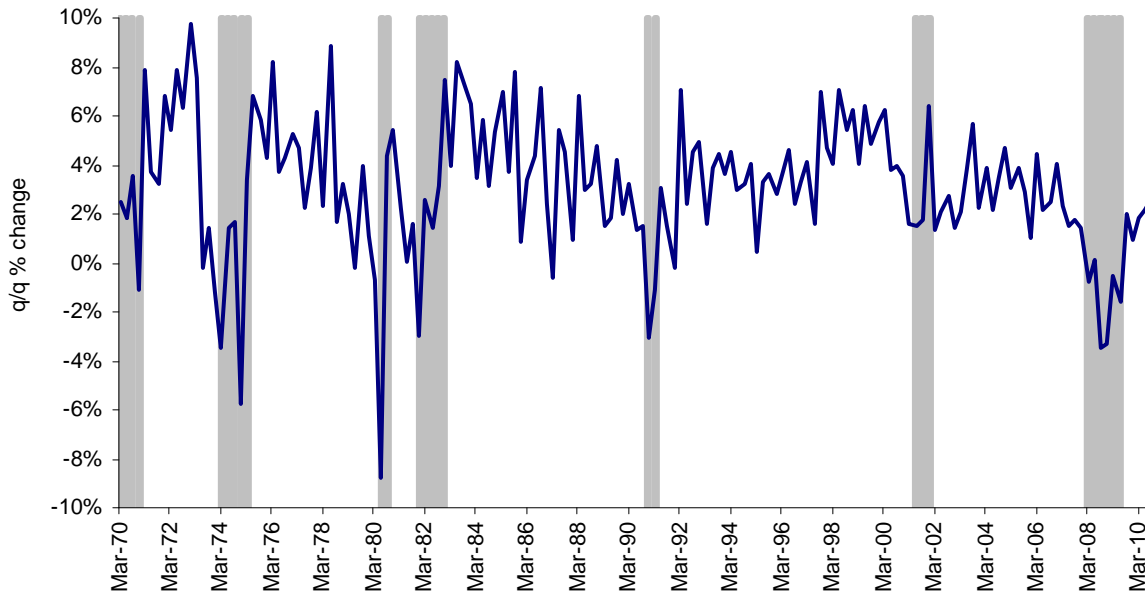
Real GDP (recessions circled)
(blue line real GDP, last obs. square is Q3 2010, forecast to Q4 2011)



Source: Bureau of Economic Analysis; Encima Global

- On the positive side, business investment is strengthening from the very low base set in 2009. We expect pent-up demand for both investment and consumption to leave shortages and pricing power in many sectors. Global growth and corporate profits are strengthening, arguing for improved private sector job growth in coming months.
- Growth in real personal consumption rose to 2.6% in the third quarter reflecting some improvement in the labor environment. This is the fifteenth consecutive quarter (since Q4 2006) that real PCE growth hasn't reached 3.0%. We think consumption growth will strengthen further in the fourth quarter, but will then respond to the tax and labor situation as it develops in 2011.

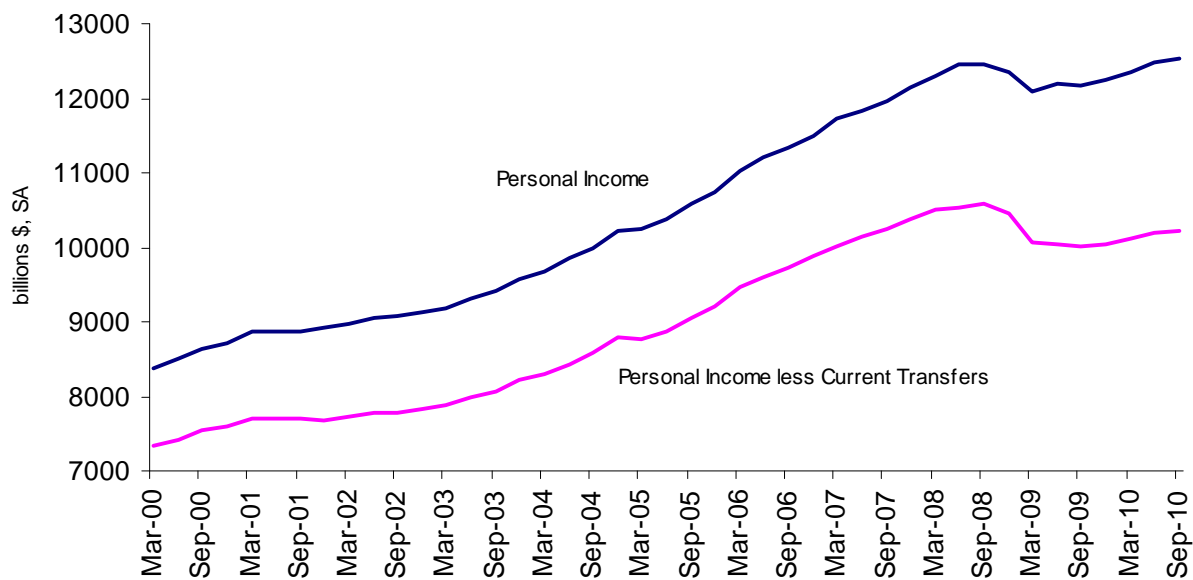
Real PCE (q/q change, last obs. Q3 2010)



Source: Bureau of Economic Analysis; Encima Global

- Nominal personal income grew 2.1% annualized in the third quarter. This implies either a very weak -0.3% in September income or, more likely, downward revisions to July and August personal income data. Transfer payments grew 4.2% in the third quarter, with income less transfers up only 0.6%. **This continues the pattern of weak wage income still dampening the recovery.**

Personal Income; less transfers (last obs. Q3 2010)



Source: Bureau of Economic Analysis; Encima Global

- Third quarter growth was helped by moderate business equipment spending, up 12.0% and 8.8% growth in federal purchases, though both slowed from the second quarter. Residential investment reversed its second quarter bounce.

Real GDP Q/Q SAAR (last obs. Q3 2010)

	3Q 09	4Q 09	1Q 10	2Q 10	3Q 10(a)
Real GDP	1.6%	5.0%	3.7%	1.7%	2.0%
Personal Consumption	2.0%	1.3%	1.9%	2.2%	2.6%
Durables	20.1%	-1.1%	8.8%	6.8%	6.1%
Nondurables	1.7%	3.1%	4.2%	1.9%	1.3%
Services	-0.5%	0.5%	0.1%	1.6%	2.4%
Residential Investment	10.6%	-0.8%	-12.3%	25.6%	-29.1%
Business Structures	-12.4%	-29.2%	-17.8%	-0.5%	3.8%
Business Equipment	4.2%	14.6%	20.5%	24.8%	12.0%
Government Purchases	1.6%	-1.4%	-1.6%	3.9%	3.3%
Federal	5.7%	0.0%	1.9%	9.1%	8.8%
State/Local	-1.0%	-2.3%	-3.8%	0.6%	-0.2%
Note: Final sales	0.5%	2.2%	1.1%	0.9%	0.6%
Nominal GDP	2.3%	4.7%	4.8%	3.7%	4.2%

Source: Bureau of Economic Analysis; Encima Global

- In terms of contributions to real growth: consumption contributed 1.8% while inventory added 1.4%; while increasing imports subtracted 2.6% and residential investment 0.8%.

Real GDP Q/Q Contributions (last obs. Q3 2010)

	3Q 09	4Q 09	1Q 10	2Q 10	3Q 10(a)
Real GDP	1.6%	5.0%	3.7%	1.7%	2.0%
Personal Consumption E	1.4%	0.7%	1.3%	1.5%	1.8%
Durables	1.4%	-0.1%	0.6%	0.5%	0.4%
Nondurables	0.3%	0.5%	0.7%	0.3%	0.2%
Services	-0.2%	0.3%	0.0%	0.8%	1.2%
Residential Investment	0.3%	0.0%	-0.3%	0.6%	-0.8%
Business Structures	-0.4%	-1.0%	-0.5%	0.0%	0.1%
Business Equipment	0.3%	0.9%	1.2%	1.5%	0.8%
Government Purchases	0.3%	-0.3%	-0.3%	0.8%	0.7%
Federal	0.5%	0.0%	0.2%	0.7%	0.7%
State/Local	-0.1%	-0.3%	-0.5%	0.1%	0.0%
Inventories	1.1%	2.8%	2.6%	0.8%	1.4%
Net Exports	-1.4%	1.9%	-0.3%	-3.5%	-2.0%
Exports	1.3%	2.6%	1.3%	1.1%	0.6%
Imports	-2.7%	-0.7%	-1.6%	-4.6%	-2.6%

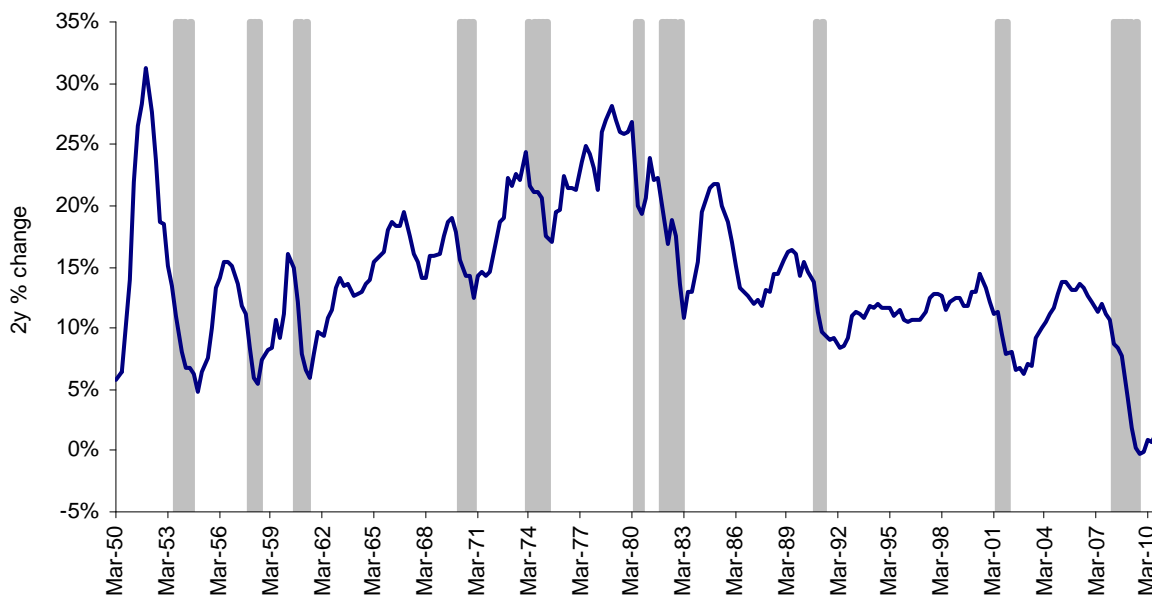
Source: Bureau of Economic Analysis; Encima Global

Nominal GDP continues to Climb Slowly

Nominal GDP topped \$14.7 trillion (annualized rate) in the third quarter, up 4.2% in Q3 and an improvement on the 3.7% nominal growth in the second quarter.

- The nominal two-year growth rate has now advanced for four quarters from its low, reaching 1.7%, but remains way below all the previous troughs. The -0.3% (revised) rate registered at the two-year trough in the third quarter of 2009 was by far the weakest two-year nominal growth since these records started in 1949.

Nominal U.S. GDP: Deep Trough (2-yr change, last obs. Q3 2010)



Source: Bureau of Economic Analysis; Encima Global

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