

Dan Hamilton
August 5, 2009

The Bureau of Economic Activity's recent release of their initial estimate of the United States second quarter GDP growth implied that the U.S. economy had improved dramatically. Economic growth was still negative, but it had improved from -6.4 in the 1st quarter to -1.0 percent in the 2nd quarter. This growth rate is close enough to zero that one might think that the economy is within striking distance of positive growth by the 3rd quarter.

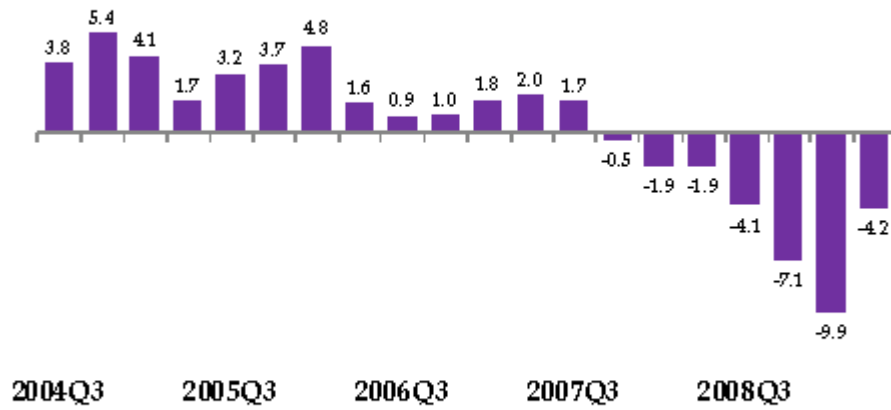
Maybe not. One of the key drivers of the 2nd quarter's improvement was an increase in Government spending of more than 800 basis points over the previous quarter. That sort of growth in government spending is clearly unsustainable.

A way to focus more specifically on the health of the domestic economy is to look at domestic demand which is defined by consumption and investment. (See chart below). 2nd quarter domestic demand was -4.2 percent, a long way from zero, i.e. a long way from sustainable economic growth.

These data do not indicate that households, 86 percent of domestic demand, will increase their spending soon. Newer data reinforce that conclusion. Consumer bankruptcies surged in July to their highest level since October 2005. Jobs are still contracting at four percent year-over-year. Indicators of notices of default, foreclosures, and short-sales suggest that the residential real estate market is still suffering.

All this would indicate that banks still have plenty of challenges and aren't ready to start lending again; businesses are not ready to invest, and most importantly, consumers are not ready to increase their spending.

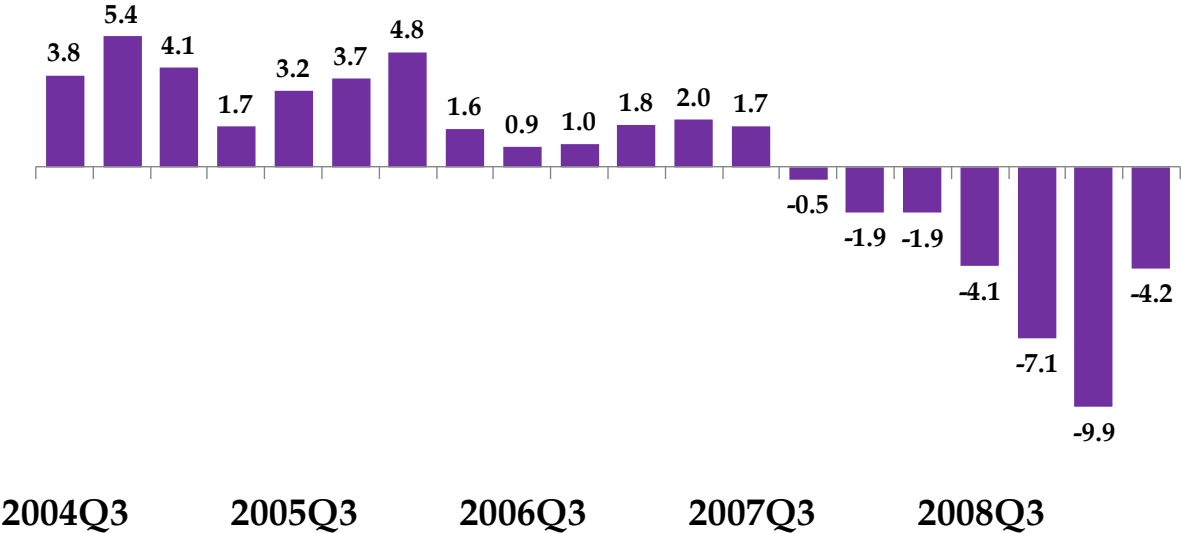
United States Real Domestic Demand



■ Center for Economic Research and Forecasting
 United States - (seasonally adjusted annual rate quarter-on-quarter percent change)

Dan Hamilton
 August 5, 2009

United States Real Domestic Demand



■ Center for Economic Research and Forecasting
United States - (seasonally adjusted annual rate quarter-on-quarter percent change)