THE ECONOMY AT A GLANCE

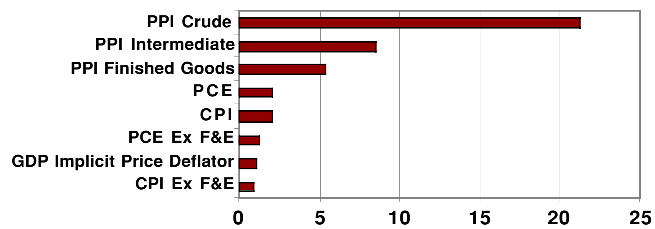
ECONOMIC HIGHLIGHTS

July 12, 2010
Vol. 77, No. 100

HEADLINE INFLATION UNDER CONTROL

Numerous gauges of consumer inflation paint a benign pricing picture, but below the surface problems may be brewing. According to the Labor Department, Producer Price Inflation for finished goods has increased at a 5.3% rate over the past year. The Fed won't be able to ignore the PPI data forever, as it will likely start to bubble to the surface later in 2011. We look for the Fed to move preemptively and raise rates in 1Q11.

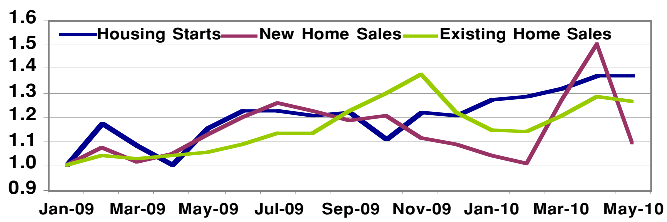
MEASURES OF INFLATION
(% CHANGE, ANNUAL RATE)



HOUSING RECOVERY VOLATILE

The housing market recovery has been, in a word, bumpy. Still of the 12-month trends we follow, each is higher than the trough reached in February-April 2009. But it is premature to call the housing crisis over. According to data from LPS Applied Analytics, banks have an inventory of approximately 1.1 million homes, up 20% from a year ago. This shadow market, unleashed on the main market, could depress prices and lengthen sales cycles.

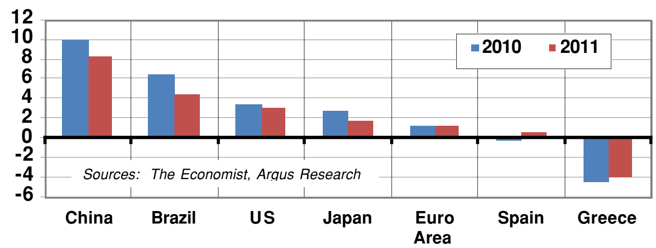
HOUSING INDUSTRY METRICS
(INDEX 1/09 = 1.00)



GLOBAL GDP ESTIMATES ON THE RISE

Overall expectations for GDP are stable, with growth forecasts in the 1%-1.5% range through 2011. But the outlook is dismal in Greece, and forecasts are now negative in Spain as well. The price of oil has generally been a good proxy for overall economic growth. As the global economy recovered during 2003-2007, the price of a barrel of oil rose from $20 to $80 before spiking higher. In recent weeks, oil rose from the $60s to $76, suggesting global growth may be poised to continue.

GLOBAL GDP FORECAST
(RATES OF Y/Y GROWTH)



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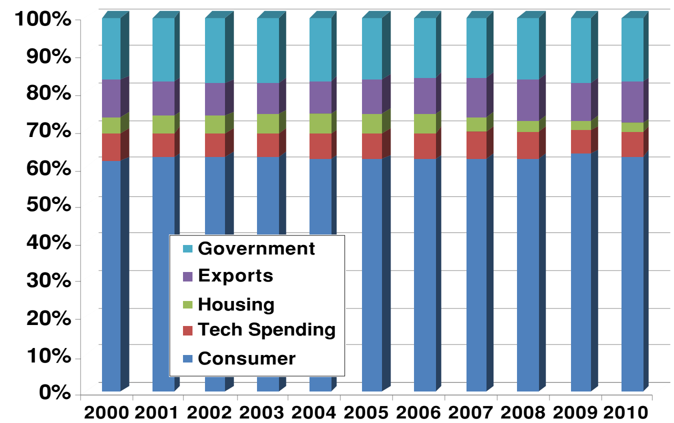
ECONOMIC HIGHLIGHTS (CONTINUED)

CONSUMER, EXPORTS DRIVING GDP

During the past decade, the primary drivers of GDP have been the Consumer and Export sectors. Over that time, we estimate that Consumer Spending has increased from 61.5% of GDP to 62.8% (for this exercise, we exclude inventories and non-residential fixed investment from our calculation of GDP imports) and Exports have increased from 9.6% of GDP to 10.8%. They have taken share from Housing (down to 2.4% from 4.7%) and Tech Spending (down to 6.4% from 7.2%). Looking ahead, the good news is that both Tech spending and Housing appear to be at a cyclical bottom (Housing) or in the early stages of an upswing (Tech). The economy will need these key drivers to contribute, as consumer spending may struggle to advance with unemployment near 10% and export growth limited as the Euro remains weak.

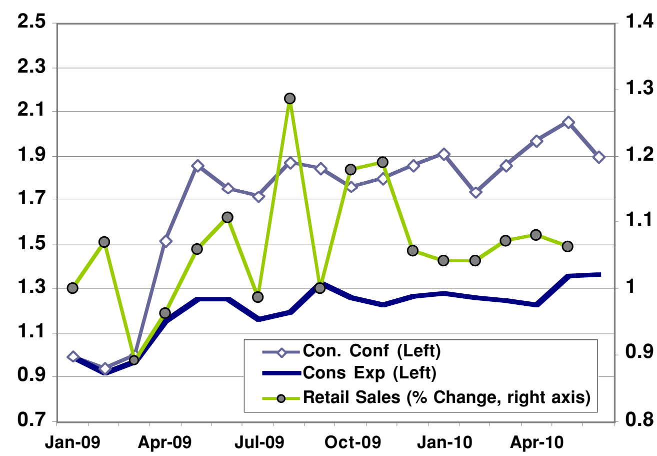
PERCENTAGE OF GDP



CONSUMER SECTOR COOLS OFF

The signs from the Consumer segment of the economy have cooled. Consumer Confidence, which had spiked higher in May, fell sharply in June. It must be said that confidence has been recovering from the depths of the recession, though the measure still remains far from the highs of 2006-2007. According to the Conference Board, Consumer Confidence was measured at 62.7 in May but fell to 52.9 in June. These readings are sharply higher than the 25.3 reported in March 2009. Looking ahead, we expect the Consumer sector to continue to lead the expansion, though we expect GDP growth to slow in the second half of 2010. Consumer Confidence in some respects is a lagging or contrarian indicator; once it climbs back above 100, the recovery may well be complete.

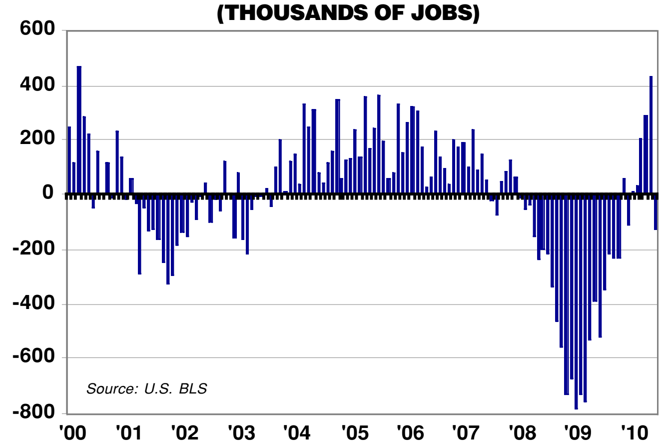
CONSUMER SECTOR METRICS
(INDEX 1/09 = 1.00)



PRIVATE SECTOR PAYROLLS RISE

The U.S. economy lost 125,000 jobs in June, as temporary census workers were dropped from payrolls. However, excluding the impact of the government hiring, payrolls increased 83,000 and the unemployment rate dropped to 9.5%. Other metrics were less encouraging: the number of long-term unemployed remained at 6.8 million; these people accounted for 45.5% of the total unemployed. The civilian labor force participation rate fell by 0.3 percentage points in June, to 64.7%. The number of persons employed part time for economic reasons, at 8.6 million, was little changed over the month — but was down by 525,000 over the past two months. The employment environment remains challenging.

MONTHLY NONFARM PAYROLLS CHANGE
(THOUSANDS OF JOBS)



BANK STOCK VALUATION

Bank stocks are more volatile than before the financial crisis, capital requirements are heading higher and revenues are under pressure. Given these factors, we looked at multiple scenarios for ROE, growth and cost of equity capital to derive fair values for the price-to-book value multiple. The fundamental price-to-book value ratio simply takes projected ROE less projected growth and divides by the cost of equity capital less projected growth. Like all simplified models, this one is very sensitive to the various assumptions used. Nevertheless, we think the most-likely scenario is #3 in our graphic (ROE returning to double-digits, growth in the high single-digits, and beta close to 1 again), which results in a price-to-book value ratio of 1.3 and suggests 30% upside from current levels.

BANK STOCKS - BOOK VALUE VALUATION SCENARIOS

Assumptions

ROE	Growth Rate	CAPM Cost of Equity
20%	12%	15%
15%	10%	13%
12.5%	8%	11.5%
10%	7%	10%
8%	5%	

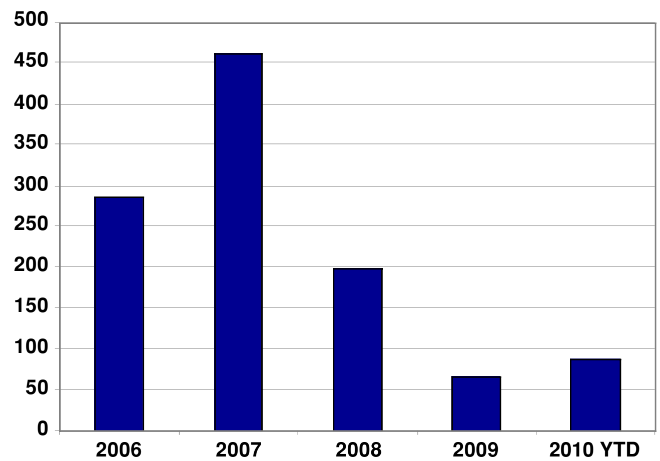
Scenarios		Justified Price-to-Book Ratio
1	High ROE, High Growth, High Beta	2.7
2	15% ROE, 10% growth, beta still above average	2.0
3	12.5% ROE, 8% growth, beta lower still	1.3
4	10% ROE, 7% growth, beta near 1	1.0
6	Low ROE, Low Growth, Beta near 1	0.6

Source: Argus Estimates, CAPM assumes 11% market return and current 10-year T Note Yield

SHARE BUYBACKS MAKING A COMEBACK

Dividends are on the rise again after a painful two years of cuts, mostly from the major bank stocks. However, we point out that investors should take heart in the fact that S&P 500 companies are sitting on record amounts of cash that are yielding next to nothing in their own bank accounts. So share buybacks are starting to make a comeback as well. According to S&P, there have been 88 buyback announcements through June 21 compared with 66 for all of 2009. The dollar amount of share buybacks announced has already surpassed last year's total as well. The next big event will be when the big banks start to restore their dividends and share buybacks — but this won't likely happen until new capital rules are established and until any other impacts of reform legislation have been weighed.

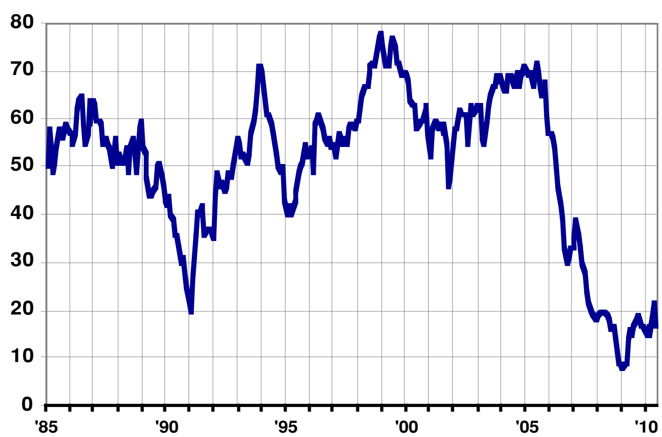
S&P 500 ANNOUNCED SHARE BUYBACKS



HOMEBUILDER SENTIMENT STILL DEPRESSED

The most recent data on housing starts and permits suggest that the new housing market may have been buoyed by the home-buying tax credit that just expired. Thankfully, mortgage rates have remained low. To us, the bigger issue is the amount of unlisted inventory still sitting on bank balance sheets. On the demand side, job and income growth are essential to a sustained recovery in housing. Despite better sales of late, the mood among homebuilders remains sour. The Homebuilder Sentiment Index has remained stuck near the level where it bottomed in the major real estate crisis in the early 1990's. If builders foresee a strong recovery, that sentiment has not come across in this survey.

NAHB HOMEBUILDER SENTIMENT INDEX



ECONOMIC CALENDAR

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
Tue. 7/6	ISM Non-Manufacturing Composite	June	55.4	53.0	N/A	N/A
Thur. 7/8	Consumer Credit	May	$1.0B	$1.05B	N/A	N/A
Fri. 7/9	Wholesale Inventories	May	0.4%	0.3%	N/A	N/A

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
Tue. 7/20	Housing Starts	June	593k	550k	N/A	N/A
Thur. 7/22	Leading Economic Indicators	June	0.4%	0.2%	N/A	N/A
	Existing Home Sales	June	5.66M	5.4M		

** Preliminary*
*** Advance*
^Final