



THE ECONOMY AT A GLANCE

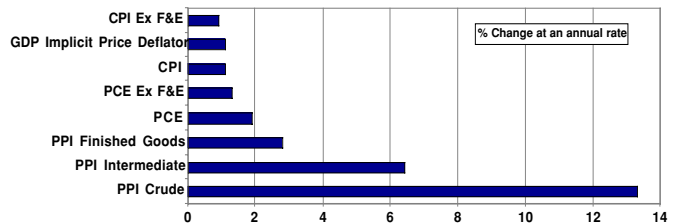
ECONOMIC HIGHLIGHTS

August 9, 2010
Vol. 77, No. 115

INFLATION RATES TRENDING LOWER

Consumer prices have been rising at a 1%-2% annual rate through June. The rates are generally lower after volatile categories such as Food & Energy are excluded. Producer Price Inflation for finished goods has increased at a 2.8% rate over the past year. Though this rate is higher than consumer inflation, the rate was 5.3% a month ago. For crude goods, inflation has jumped 13.3% over the past year — troublesome, but down from a 21.2% rate in May.

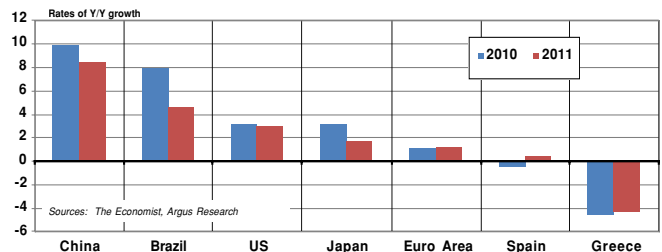
MEASURES OF INFLATION



GLOBAL ECONOMIES FORECAST TO EXPAND

Economies in 2010 are generally forecast to grow in 2011. The greatest rate of growth is anticipated in China, which economists expect will report GDP growth of up to 8.3% for 2011. Estimates for growth in the U.S. have declined in the past month. In the Euro area, overall expectations for GDP are stable but low — with growth forecasts only in the 1%-1.5% range through 2011. Forecasts are now negative in Spain (2010) and Greece (2010 and 2011). Hungary and Venezuela are other trouble spots.

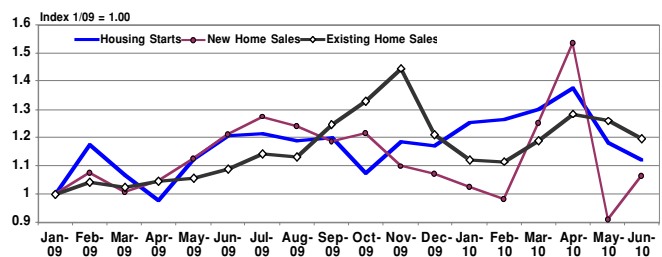
GLOBAL GDP FORECAST



HOUSING RECOVERY VOLATILE

The housing market has proceeded unevenly since January 2009. Even though mortgage rates are near all-time lows, it is too early to call the housing crisis over. Banks have an inventory of approximately 1.1 million homes. This shadow market, unleashed on the main market, could depress prices and lengthen sales cycles. The housing market led the U.S. economy into recession, and we expect the Federal Reserve to keep rates low long enough to stabilize housing trends and avoid a double-dip.

HOUSING INDUSTRY METRICS

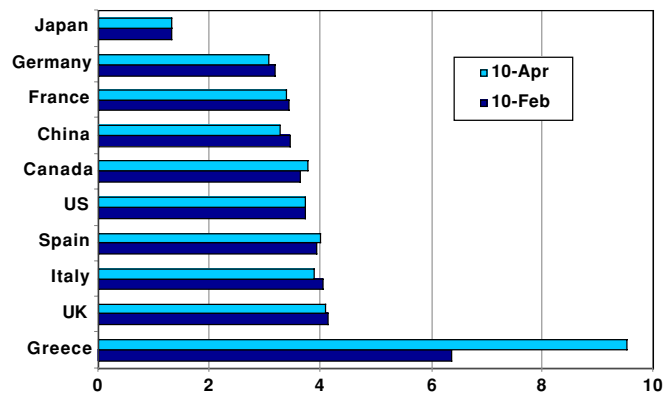


ECONOMIC HIGHLIGHTS (CONTINUED)

DEFICIT SPENDERS

According to our analysis, the United Kingdom is pumping up the local economy at the fastest rate on a relative basis — with a deficit spending rate equal to 10.5% of GDP. Greece and Spain are in second place, at 9.9% — and the U.S. is not too far behind, with an 8.8% deficit-spending rate. Greece is in further trouble as its current account balance is also weak, with a deficit of 7.2%. Little wonder that long-bond yields in Greece are above 10%, versus 3%-4% in other nations. On the positive side of the spectrum, resource-rich countries such as Russia and Saudi Arabia both have steep current account balance surpluses. If the global economy fails to revive, resource-rich nations (including China) may well see their economic influence grow.

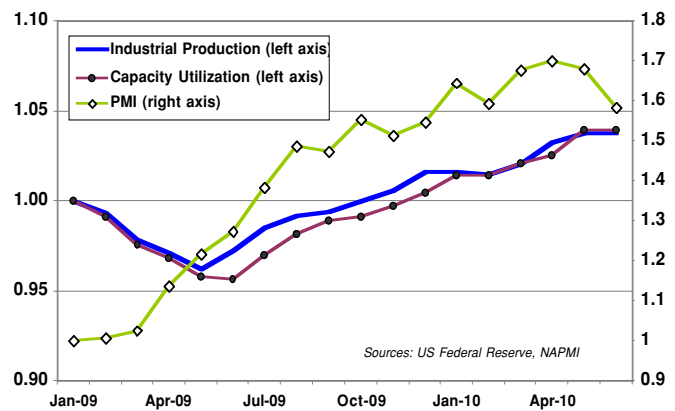
SOVEREIGN DEBT REVIEW (10-YR. BOND YIELD, %)



INDUSTRIAL RECOVER SLOWS

The Industrial sector of the U.S. economy continues to recover, but at a slower pace in recent months. Three of the key sector indicators we follow – capacity utilization, industrial production and the Purchasing Managers Index – are signaling expansion. But readings of the PMI—a survey of 250 businesses conducted monthly by the National Association of Purchasing Managers – have recently dipped from above 60 to the 56 level. A reading above 50 signals expansion; back in the dark days of winter 2009, the index dropped to 35. The PMI is typically a leading indicator for industrial production and capacity utilization. All three are leading indicators for employment. If they continue to trend higher, we should start to see better Nonfarm Payrolls reports in the second half of the year.

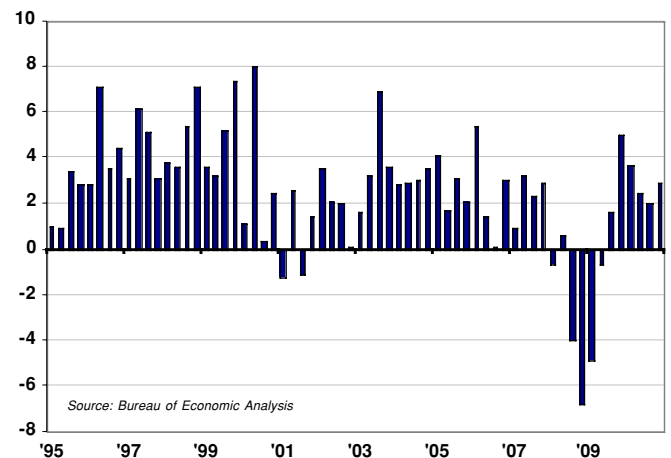
INDUSTRIAL SECTOR METRICS (INDEX 1/09 = 1.00)



2Q GDP GROWTH SLOWS TO 2.4%

The U.S. economy expanded at a 2.4% annual pace in the second quarter of 2010, according to the U.S. government. This “advance estimate” was slightly lower than consensus – but we note that 1Q GDP was upwardly revised from 2.7% to 3.7%, as the Commerce Department released its annual revision to the data. Blending the two rates, GDP in the first half grew at about a 3% pace, which is the normal growth rate for the economy. Our forecasts call for 2%-3% GDP growth through the balance of the year — slightly below the recent trend, reflecting the likelihood that government spending remains constrained, consumers continue to exert caution and the housing sector slows. We look for corporate IT spending to remain robust and for export growth to continue.

REAL GDP

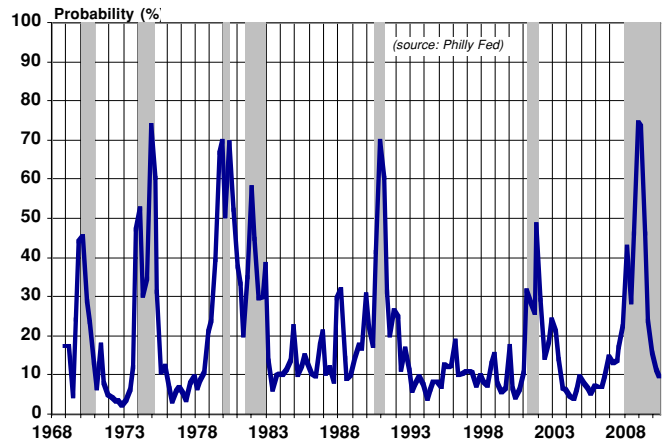


FINANCIAL MARKET HIGHLIGHTS

THE ANXIOUS INDEX

The Federal Reserve Bank of Philadelphia regularly publishes a Survey of Professional Forecasters, asking panelists to estimate the probability that real GDP will decline in the quarter in which the survey is taken and in each of the following four quarters. We charted the Anxious Index over time, beginning in the fourth quarter of 1968. The index often goes up just before recessions begin. For example, the index value was 32% in the first quarter survey for 2001 (taken in February 2001); the National Bureau of Economic Research subsequently declared the start of a recession in March 2001. The Anxious Index peaks during recessions, then declines when recovery seems near. For example, the index fell to 14% in the second quarter of 2002, when economic indicators began improving.

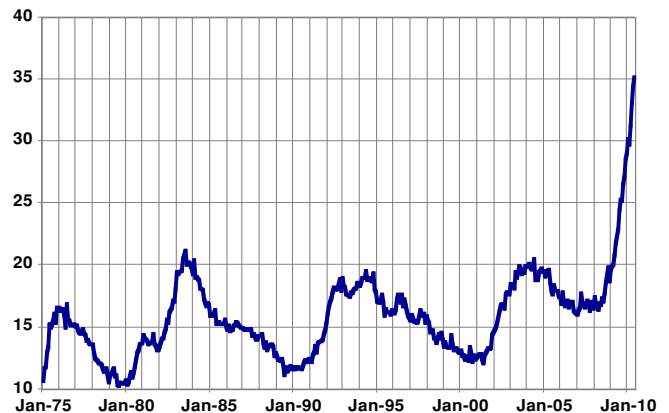
PROBABILITY OF DECLINE IN REAL GDP IN THE FOLLOWING QUARTER (QUARTERLY, 1968:Q4 TO 2010:Q2)



LENGTH OF UNEMPLOYMENT STILL RISING

Investors have been busy over the past few years comparing the current state of the U.S. economy with previous periods of recession and depression. The U.S. economy started creating jobs again several months ago and the unemployment rate, which seemed destined to pass 10%, has actually ticked down to 9.5%. However, the average length of unemployment has continued to hit new highs and is already at an unprecedented level of 35.2 weeks as of the end of June. For historical perspective, the previous peak of unemployment (outside of the Depression era) occurred in November and December 1982 — when the rate hit 10.8%. Even then, however, the average length of unemployment was only 18.1 weeks, or about half as long.

AVERAGE DURATION OF UNEMPLOYMENT (# OF WEEKS)



STOCK MARKET P/E RATIO

Many of the ingredients for a bull run are in place — balance sheets are in great shape, profits are growing again and interest rates and inflation are very low. However, valuation measures for the broad market are closer to their long-run averages right now than to the levels that existed in the 1970's and 1980's. True, high inflation and high interest rates were coupled with sluggish economic growth in those days. But dividend payouts were much greater than today as well. The trailing P/E ratio for the S&P 500 has generally been on an upward trajectory since the mid-1970's. The current P/E of 15-times is just below the 16.7-times average for that entire period. So which way will multiples break from here? The answer may depend on the direction of interest rates and inflation..

S&P 500 P/E RATIO (ON TTM EARNINGS)



ECONOMIC CALENDAR

Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
Mon 8/2	ISM Manufacturing Survey	July	56.2	55	54.5	55.5
	Construction Spending	June	-1.0%	0.0%	-0.5%	0.1%
Tue 8/3	Personal Income	June	0.3%	0.2%	0.2%	0.0%
	Consumer Spending	June	0.1%	0.1%	0.1%	0.0%
	Factory Orders	June	-1.8%	0.1%	0.5%	-1.2%
	Total Vehicle Sales	July	11.08M	11.0M	11.60M	N/A
Wed 8/4	ISM Non-Manufacturing Survey	July	53.8	54	53.6	N/A
Fri 8/6	Nonfarm Payrolls	July	-125k	50k	-100k	N/A
	Unemployment Rate	July	9.5%	9.5%	9.6%	N/A
	Manufacturing Payrolls	July	9k	20k	10k	N/A
	Average Hourly Earnings	July	-0.1%	0.0%	0.1%	N/A
	Average Weekly Hours	July	34.1 hrs.	34.1 hrs.	34.1 hrs.	N/A
	Consumer Credit	June	-9.1B	-9.3B	-5.0B	N/A

* Preliminary

** Advance

^Final

Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
Mon 8/16	Empire State Index	August	5.08%	N/A	N/A	N/A
Tue 8/17	Industrial Production	July	0.1%	N/A	N/A	N/A
	Capacity Utilization	July	74.1%	N/A	N/A	N/A
	Producer Prices	July	-0.5%	N/A	N/A	N/A
	Producer Prices Ex F&E	July	0.1%	N/A	0.2%	N/A
	Housing Starts	July	549k	N/A	0.2%	N/A
Thu 8/19	Leading Economic Indicators	July	-0.2%	N/A	N/A	N/A
	Philadelphia Fed BOS	August	5.1	N/A	N/A	N/A

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** Advance

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