

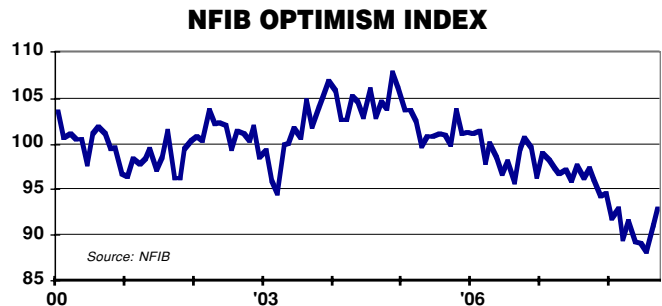


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### ECONOMIC HIGHLIGHTS

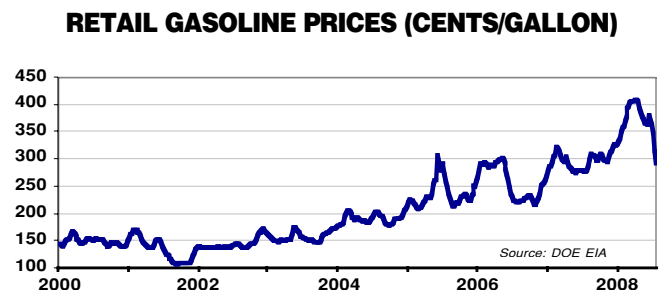
#### SMALL BUSINESS OPTIMISM RISES

The National Federation of Independent Business' September Optimism Index crept up to 92.9 from 91.1 in August. Several key gauges registered considerable improvement, including the Outlook for Expansion Index and the Outlook for General Business Conditions. While many components reside in or near recessionary levels, it is encouraging to see that they are trending higher rather than lower. Small businesses represent roughly 99.7% of all U.S. employer firms and 80% of all new jobs.



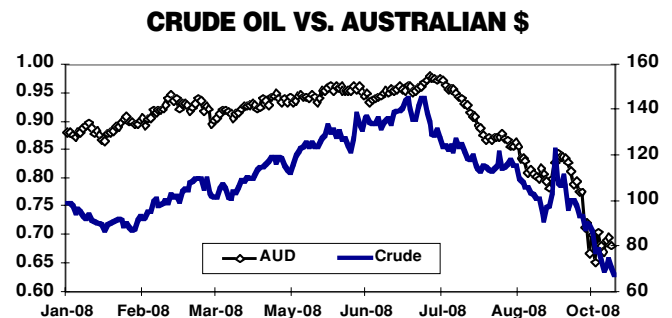
#### CONSUMERS GET MASSIVE STIMULUS

There's a massive stimulus plan underway and it's coming from Big Oil. Just as record prices at the pump restricted consumer spending, the price reversal is now having a positive effect. There's a generally accepted rule that every \$10 decline in crude oil boosts spending by \$70 billion in a year. Oil is off roughly \$70, which would equate to a boost of \$490 billion. Even if that's half correct, it would be an impressive stimulus.



#### SURGING DOLLAR, SLOUCHING CRUDE

The U.S. dollar has rallied significantly since July — particularly against the major currencies. More importantly, it has surged against commodity sensitive countries such as Canada and Australia, and so prices of dollar-denominated commodities such as crude oil have fallen. If the price of crude continues its descent, then the fate of several other countries — Russia, Venezuela, and Mexico — may also be compromised. If this is sustained, weaker economies may experience a currency crisis.

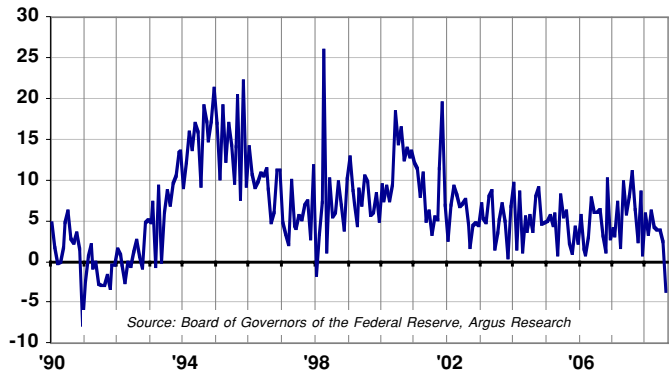


# MONETARY HIGHLIGHTS

## CONSUMERS TIGHTEN PURSE STRINGS

Total outstanding consumer borrowing contracted by an annualized 3.7% in August – the first decline in over a decade — the result of a 0.8% drop in revolving, or credit card, debt and a 5.4% plunge in nonrevolving debt. Miserable auto sales explain the decline in nonrevolving activity. This release is the first, unofficial, sign of the credit crisis hitting the household sector. It doesn't matter if you have great credit scores, banks are spooked and will not lend at any price. This is where the crisis hits the economy. The word credit is derived from the Latin "credere" and mean "to believe." Sadly, no one believes or trusts anyone in this environment. In essence, there is no credit market.

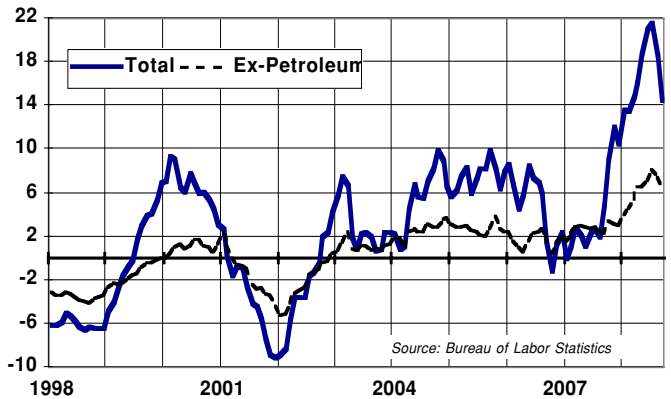
## CONSUMER OUTSTANDING CREDIT %



## IMPORT INFLATION DECLINES

The inflation picture is improving dramatically given the recent increase in the value of the U.S. dollar and tumbling commodity prices. In September, total import prices fell 3.0% — but are still 14.5% higher than year-ago levels. Excluding volatile energy prices, ex-petroleum import prices fell 0.9% over the last month and are 6.5% higher than in September 2007. According to the Bureau of Labor Statistics, the combined decline in August and September in the total import price index was the greatest two-month drop since the index was first published in 1988. Looking ahead, we anticipate a continuation in this lower inflation trend as slower global economic conditions force commodities prices downward, and the value of the dollar slowly creeps higher.

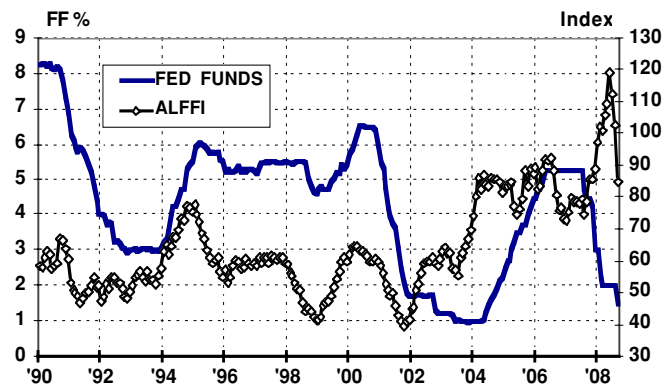
## IMPORT PRICES (YOY%)



## ARGUS FED INDEX SLUMPS

The Argus Leading Fed Funds Index (ALFFI), our internal barometer of changes in the Fed Funds rate, fell more than 17 points in September after an almost 10 point decline in August. The ALFFI stands at 85.10 compared to the historical high of 119.46 in June. This trend is comforting to a Fed that once again reduced its overnight borrowing target in early October (to 1.50%). The U.S. dollar has escalated in recent months as deterioration, particularly in Europe, has sent the value of other currencies southward. This has reduced U.S. import inflation, and sent the value of dollar-denominated commodities like crude oil, metals and other basic materials to less-troubling levels.

## ARGUS LEADING FED FUNDS INDEX



# FINANCIAL MARKET HIGHLIGHTS

## GETTING PAID FOR RISK

Spreads between junk bonds and Treasuries have soared to historic highs, so junk bond investors are clearly pricing in a deep recession. Though it is weakening, corporate credit quality outside of homebuilders and other real-estate industries continues to hold up relatively well. According to S&P, default rates on junk bonds are still just about 3% versus a long-term average of 4.5%. The rate was 8% when the last two recessions began in 2001 and 1991, and default rates ultimately exceeded 10% in those cases. Again, while major banks just reported another quarter of severe credit-quality deterioration, the pain was largely confined to real estate, and mostly consumer loans. So investors hungry for yield and willing to take risk may consider increasing their allocation to junk bonds.

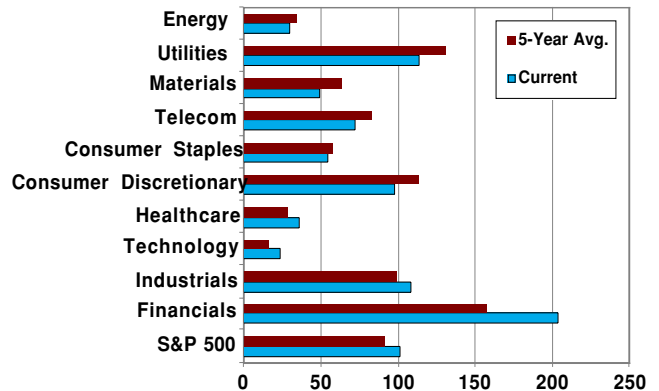
## JUNK BOND SPREADS OVER TREASURIES (%)



## DEBT LEVERAGE DOWN IN MOST INDUSTRIES

The deleveraging of the finance sector has been painful thus far, with likely more bad news ahead. However, an analysis of debt ratios across other sectors reveals that leverage is currently well below the five-year average for several. The ratio of long-term debt to common equity is above the recent averages in Technology and Healthcare, but debt ratios in these sectors remain in the 20%-30% range, well below those of most other sectors. On the flipside, with the economy slowing and with credit less available (and on less-favorable terms), the above-average current leverage in the Industrial sector bears watching. Still, it's clear from our analysis that most of the increase in the S&P 500's overall leverage comes from the Financial sector.

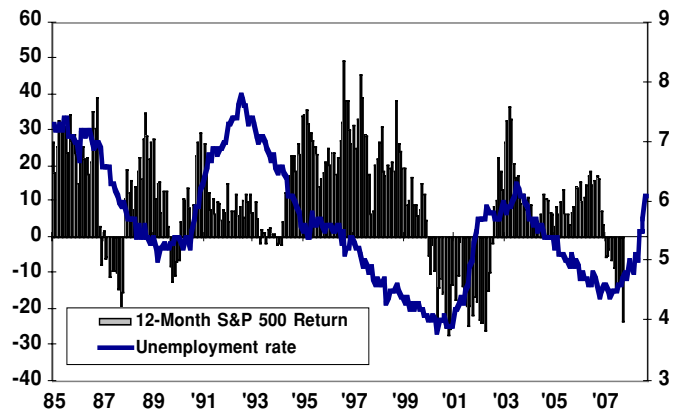
## LONG-TERM DEBT/COMMON EQUITY (%)



## UNEMPLOYMENT & STOCK RETURNS

The stock market anticipated the 1990-1991 recession as early as September 1989, and started to decline. But the unemployment rate didn't start to rise until June 1990. By the time the unemployment rate peaked at 7.8% in June 1992, stocks were back to delivering positive 12-month returns. The same pattern held up in the 2001 recession. This time around, the markets started weakening in the summer of 2007 and unemployment readings began heading up earlier this year. To be sure, unemployment seems likely to increase further. So we can't see a peak in that number yet. But businesses are aggressively cutting costs and the plunge in commodity costs should begin to help margins. With stocks already down nearly 50% from their peak, weak earnings may already be largely priced in.

## UNEMPLOYMENT & STOCK RETURNS



# THE ARGUS ECONOMIC OUTLOOK

	2006 A				2007 A				2008 E				2009 E				October 28, 2008
	I	II	III	IV	I	II	III	IV	I	II	III	IV	I	II	III	IV	
Real Gross Domestic Product	4.8	2.7	0.8	1.5	0.0	4.8	4.8	-0.2	0.9	2.8	0.0	-0.5	0.6	1.7	0.9	1.9	
Annual:				2.4			2.4					0.8				1.3	
Personal Consumption	4.3	2.8	2.2	3.7	3.9	2.0	1.0	0.9	0.9	1.2	0.0	-0.7	0.4	0.6	-0.2	0.5	
Durables	18.9	1.8	3.5	4.2	9.2	5.0	0.4	-4.3	-4.3	-2.8	-8.1	-2.5	0.3	1.0	1.9	1.4	
Non-Durables	4.4	3.1	2.3	3.1	3.5	1.9	0.3	-0.4	-0.4	3.9	-0.4	0.2	1.1	1.0	0.3	0.3	
Services	1.6	2.8	2.0	3.9	3.1	1.4	1.4	1.4	2.4	0.7	0.8	-0.8	0.2	0.3	0.3	0.4	
Gross Domestic Investment	6.2	-0.4	-5.3	-15.0	-9.6	6.2	3.5	-11.9	-5.8	-11.5	0.7	-2.1	-0.9	4.4	2.6	5.9	
Fixed Investment	8.3	-2.5	-4.8	-7.6	-3.4	3.0	-0.9	-6.2	-5.6	-1.7	-5.6	-2.0	-0.9	0.8	1.4	3.5	
Non-Residential	15.9	6.4	5.4	-1.0	3.4	10.3	8.7	3.4	2.4	2.5	-3.3	0.3	1.8	1.4	2.7	4.1	
Structures	15.5	19.7	14.3	2.5	11.2	18.3	20.6	8.6	8.7	18.4	0.6	0.7	5.5	2.1	4.2	6.3	
Equip. & Software	16.3	1.8	2.0	-2.4	0.0	6.9	3.6	1.0	-0.5	-5.0	1.6	0.1	0.6	1.1	2.2	3.3	
Residential	-3.6	-16.6	-21.5	-19.5	-16.2	-11.6	-20.6	-27.0	-25.0	-13.3	-10.0	-10.6	-11.0	-1.5	-4.3	0.6	
Change in Pvt. Inventories	45.9	56.9	53.3	13.1	-15.0	-2.8	16.0	-8.1	-10.2	-50.6	-25.0	-25.0	-25.0	-10.0	-5.0	5.0	
Net Exports	16.7	5.4	3.5	15.6	0.6	8.8	23.0	4.4	5.1	12.3	7.7	5.7	5.6	6.1	6.0	5.9	
Exports	18.1	6.6	3.6	10.4	2.1	6.8	21.8	5.1	4.6	16.3	8.3	6.1	4.4	4.6	4.6	5.5	
Goods	13.5	2.7	3.2	28.6	-2.7	13.3	26.0	2.7	6.4	3.7	6.2	4.7	8.6	9.7	9.4	6.9	
Services	10.3	0.1	3.1	2.0	7.7	-3.7	3.0	-2.3	-0.8	-7.3	5.0	2.5	2.3	2.0	1.7	1.6	
Imports	9.0	0.5	3.8	-0.8	8.4	-4.0	2.4	-2.6	-1.9	-7.1	5.4	2.2	1.5	1.5	1.3	1.3	
Goods	17.8	-2.0	-0.3	18.4	4.2	-2.0	6.3	-0.8	5.5	-8.1	1.6	4.2	6.5	4.6	4.1	3.0	
Services	3.9	1.3	1.7	1.6	0.9	3.9	3.8	0.8	1.9	3.9	-0.6	0.3	0.3	0.6	0.6	0.9	
Gov't Purch. of Goods & Svcs.	10.0	-1.6	1.9	1.8	-3.7	6.7	7.2	-0.5	5.8	6.6	-0.8	1.0	0.6	1.0	1.1	2.1	
Federal	8.8	1.9	-0.9	7.1	-5.9	8.4	10.1	-0.9	7.2	7.3	0.3	0.7	0.5	0.9	0.9	2.4	
National Defense	12.4	-8.1	7.6	-8.1	1.3	3.1	1.1	0.5	2.7	5.0	-2.0	1.6	0.8	1.3	1.4	1.4	
Non-Defense	0.5	3.0	1.6	1.5	3.6	2.4	1.9	1.6	-0.3	2.5	-0.6	-0.2	0.2	0.3	0.3	0.2	
State & Local	5.1	2.3	0.9	2.9	1.1	4.3	4.0	0.8	0.9	4.4	-0.9	-0.5	0.6	1.1	0.7	1.6	
Final Sales of Domestic Prod.	4.8	1.6	1.0	1.5	2.2	2.5	1.9	-0.1	0.1	1.3	-0.8	-0.8	0.2	0.6	0.2	1.0	
Final Sales to Dom. Purch.																	
Addendum:																	
Nominal GDP	8.6	5.5	3.6	3.7	4.3	6.9	6.4	2.3	3.5	4.1	4.3	3.3	4.2	4.8	4.5	5.0	
Personal Con Exp Deflator	1.8	3.3	3.1	-0.5	3.4	3.6	2.5	4.3	3.6	4.3	4.0	3.6	3.3	2.9	3.2	2.9	
GDP Price Deflator (implicit)	3.6	2.7	2.7	2.2	4.2	2.0	1.5	2.5	2.6	1.3	4.3	3.8	3.6	3.1	3.5	3.0	

Richard Yamarone, Director of Economic Research

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