

Market Comment *Economic Highlights for the week ended February 4, 2011*

Economic Week in Review: Jobs front and center

Vanguard 2/4 - The jobs picture was mixed this week, while the Fed chairman punctuated employment's prominence in any economic recovery. January payrolls increased far less than forecast, but unemployment fell to its lowest level in nearly 2 years. Other indicators were positive, with increases in consumer spending, manufacturing and factory orders, the service sector, and productivity. For the week ended February 4, the S&P 500 Index rose 2.7% to 1,311 (for a year-to-date total return of about 4.4%). The yield of the 10-year U.S. Treasury note increased 32 basis points to 3.68% (for a year-to-date increase of 38 basis points).

Employment Report – January: Fewer Jobs Created, But Lower Unemployment Rate

Vanguard 2/4 - Nonfarm payrolls rose by 36,000 in January, far below expectations. Yet the unemployment rate decreased to 9.0%, its lowest level since April 2009. Although the two results appear to conflict, many analysts contend that the drop in unemployment was likely because severe winter weather kept people from seeking jobs (thus removing them from the workforce temporarily). Among those who are employed, about 900,000 people reported they weren't at work at some point in January, more than double the average for that month. The U.S. unemployment rate has been 9% or higher since May 2009.

Federal Reserve Chairman Ben Bernanke noted that it may take years for employment to return to normal levels. "Until we see a sustained period of stronger job creation, we cannot consider the recovery to be truly established," he said.

AFP 2/7 - Data revisions added another 40,000 jobs to previously reported job gains for November and December. Yet, the same revisions show that there were 483,000 fewer people working at the end of 2010 than previously estimated. Industries with the biggest job gains in January were manufacturing (+49,000), retail (+28,000) and health care (+11,000). There were job losses in transportation (-38,000) and construction (-32,000).

WSJ Economists React 2/4 (Excerpts) – January Employment Report (Non-Farm Payrolls)

- In our judgment, the economy is picking up and we expect a strong employment report once the weather effects unwind. Second, if there were nearly 900,000 who didn't work because of the weather (many of whom appear to be construction workers and transportation workers), there must have been a large number who were unemployed but didn't look for a job because of the weather (and are thus considered out of the labor force). In support of this view, we note there were a record 1.02 million in January who wanted a job but didn't look because of 'other' reasons. –*RDQ Economics*
- There is considerable lingering weakness in the economy, as seen in the decline in financial services and little recovery in better quality professional services. –*Sophia Koropeckyj, Moody's Economy.com*
- The BLS also incorporates the results of its benchmark revisions in this report. The level of employment in December 2010 was revised down by a total of 483,000. Before the revisions, the estimates suggested that over the past year 1.1 million of the 8.3 million jobs lost during the recession had returned. Now it appears that only 950,000 of the 8.7 million jobs lost have been recovered. –*Paul Ashworth, Capital Economics*

Consumer Spending – December: Consumers Continue to Increase Spending

Vanguard 2/4 - Consumer spending increased for the sixth consecutive month, rising by 0.7% in December, which was higher than expected. Personal income rose 0.4% in December as wage growth kept in line with the average for the second half of the year: 0.3%. As spending moved higher, the savings rate dipped to 5.3% in December from 5.5% in November. Real spending—which disregards the effects of price changes—grew 0.4%, led by durable goods. Core prices—excluding food and energy—were essentially unchanged for the fifth time in the last 6 months, indicating that inflation remains in check.

AFP 2/7 - Personal income grew by \$54.5 billion (+0.4%) while disposable personal income expanded by \$47.3 billion (+0.4%). Consumer spending grew 0.7% to \$10.58 trillion (SAAR). Spending on durable goods increased 0.7% while they shot up 1.5% for non-durable goods (think higher gas prices).

ISM Manufacturing – January: Manufacturing Jumps to 6-year High

Vanguard 2/4 - The Institute for Supply Management (ISM) Manufacturing Index climbed to 60.8 in January from 58.5 in December. (A reading above 50 indicates that the manufacturing economy is generally expanding.) The

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larger-than-anticipated gain put the index at its highest level since 2004. Manufacturing employment also rose, and January was the second straight month new orders rose more than 5 points.

AFP 2/7 - The manufacturing index hit a 6.5 year high. Of the index's components: new orders jumped a healthy 5.8 points to 67.8 while the production index increased 3/10ths of a point to 63.5. The inventories index grew 6/10ths of a point to 52.4 while the employment index was up a strong 2.8 points to 61.7. The index for supplier deliveries increased 1.8 points to 58.6. 14 of 18 tracked manufacturing industries expanded in January.

Barclays 1/31 - January's ISM report uniformly indicates acceleration in manufacturing activity at the start of the new year, consistent with our view that overall economic activity will sustain a higher pace in 2011 than 2010. Especially encouraging is the employment index, which signals a pace of hiring not seen since the early 1970s and suggests that we may see some further cyclical gains in the sector's payrolls.

ISM Services Index – January: Service Sector Shows Some Strength

Vanguard 2/4 - The ISM non-manufacturing (service sector) survey jumped 2.3 points to 59.4 in January, its highest point since 2005. The largest contributor to the new high was new orders, which rose 3.5 points to 64.9. The employment index also climbed to a new recovery high. Meanwhile, new export orders fell by 2.5 points while imports rose by the same amount. Nonmanufacturing is catching up to manufacturing, signifying that the recovery is becoming more balanced.

AFP 2/7 - This was the 14th straight month with the index over the 50.0 expansion/contraction threshold. All four components of the headline index also were in expansionary territory.

Factory Orders – December

Vanguard 2/4 - The Commerce Department reported that new orders for manufactured goods rose 0.2% in December; a decline of 0.5% had been expected. In addition, November's 0.7% gain was revised upward to 1.3%. Excluding transportation, orders were up 1.7%, as declines in orders for civilian aircraft pulled the headline figure lower over the month.

Durable goods orders fell 2.3%, but new orders and shipments of nondurables were each up 2.3%. Rising prices for petroleum and related products supported the increase in nondurable goods shipments.

AFP 2/7 - Factory orders increased for the 5th time in 6 months to \$426.8 billion. Transportation orders were a drag on new orders, however, plummeting 12.7%. Net of transportation, new orders increased 1.7%. Shipments grew for the 3rd time in 4 months, up 1.6% to \$200.8 billion. Unfilled orders declined for the 8th consecutive month (-0.4% to \$822.8 billion). Inventories increased for the 11th month over the past 12, growing 1.1% to \$550.4 billion. The inventories-to-shipments ratio fell a basis point to 1.26.

Productivity – Q4: Productivity Gets Another Boost

Vanguard 2/4 - Nonfarm business productivity rose at an annual rate of 2.6% in the fourth quarter, above consensus. In fact, the average productivity for all of 2010 was 3.6% higher than during 2009—the largest year-to-year increase since 2002.

For the fourth quarter, output increased 4.5% and hours inched up 1.8% (both annualized), although unit labor costs fell 0.6%. In 2010, unit labor costs were down by 1.5% from 2009.

AFP 2/7 - 4th quarter growth in GDP along with a modest increase in hours worked led to a 2.6% jump in productivity. Over the past year, non-farm productivity grew 1.7%.

Construction Spending - November

AFP 2/7 - Construction spending fell for 4th time in 6 months and was down 6.4% from a year earlier. Private construction fell 2.2% from November and was down 9.8% from a year earlier. Spending on private residential construction plummeted 4.1% from November levels while non-residential construction spending fell a more modest 0.5%. Public construction spending decreased 2.8%, including a 3.7% decline in education construction.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week ended Jan. 29

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Press Release 2/3 (excerpts) – In the week ending Jan. 29, the advance figure for seasonally adjusted initial claims was 415,000, a decrease of 42,000 from the previous week's revised figure of 457,000. The 4-week moving average was 430,500, an increase of 1,000 from the previous week's revised average of 429,500.

The advance seasonally adjusted insured unemployment rate was 3.1% for the week ending Jan. 22, a decrease of 0.1 percentage point from the prior week's unrevised rate of 3.2%.

The advance number for seasonally adjusted insured unemployment during the week ending Jan. 22 was 3,925,000, a decrease of 84,000 from the preceding week's revised level of 4,009,000. The 4-week moving average was 3,929,500, a decrease of 50,500 from the preceding week's revised average of 3,980,000.

| WEEK ENDING | Jan. 29 | Jan. 22 | Change | Jan. 15 | Prior Year |
|---------------------------------|---------|---------|---------|---------|------------|
| Initial Claims (Seasonally Adj) | 415,000 | 457,000 | -42,000 | 403,000 | 490,000 |
| 4-Wk Moving Average (SA) | 430,500 | 429,500 | +1,000 | 413,000 | 481,250 |

The Economic Week Ahead: February 7 – Feb. 11, 2011

Vanguard 2/4 - Next week's reports will include consumer credit (Monday) and international trade (Friday).

This Week's U.S. Economic Calendar

Source: Briefing.com

| Date | ET | Release | For | Actual | Briefing.com | Consensus | Prior |
|--------|-------|----------------------------------|-------|--------|--------------|-----------|----------|
| Feb 07 | 15:00 | Consumer Credit | Dec | \$6.1B | \$2.5B | \$2.5B | \$2.0B |
| Feb 10 | 08:30 | Initial Claims | 02/05 | | 410K | 410K | 415K |
| Feb 10 | 08:30 | Continuing Claims | 01/29 | | 3900K | 3900K | 3925K |
| Feb 10 | 10:00 | Wholesale Inventories | Dec | | 1.5% | 0.7% | -0.2% |
| Feb 10 | 14:00 | Treasury Budget | Jan | | -53.0B | -\$59.5B | -42.6B |
| Feb 11 | 08:30 | Trade Balance | Dec | | -\$42.0B | -\$40.4B | -\$38.3B |
| Feb 11 | 09:55 | U of Michigan Consumer Sentiment | Feb | | 75.5 | 75.5 | 74.2 |

FFCB Weekly Debt Issuance Activity

| Week Ended Date | Discount Notes \$million | New Bonds \$millions | Issue Count | Called Bonds Par \$millions | Issue Count |
|-----------------|--------------------------|----------------------|-------------|-----------------------------|-------------|
| 7-Jan | \$ 12,732 | \$ 2,550 | 12 | \$ 260 | 3 |
| 14-Jan | 5,045 | 2,007 | 9 | 370 | 5 |
| 21-Jan | 5,670 | 872 | 13 | 1,185 | 6 |
| 28-Jan | 7,340 | 1,633 | 22 | 200 | 2 |
| 4-Feb | 6,474 | 1,343 | 17 | 470 | 4 |