Market Comment *Economic Highlights for the week ended February 18, 2011*

Economic Week in Review: Recovery Momentum Continues

Vanguard 2/18 - The Federal Reserve grew more confident in the strength of the U.S. economy, but not enough to pull back from its second round of quantitative easing. High unemployment remained a challenge. Rising commodity prices began to tug at the pockets of consumers and producers, but general inflation in the United States was not yet a concern. For the week ended February 18, the S&P 500 Index rose 1.0% to 1,343 (for a year-to-date total return of about 7.2%). The yield of the 10-year U.S. Treasury note fell 5 basis points to 3.59% (for a year-to-date increase of 29 basis points).

Retail Sales – January: Retail Sales Continue Upward Trend

Vanguard 2/18 - Retail sales rose again in January, although not as strongly as in recent months. Sales increased 0.3% for the month after jumping 0.5% in December.

Gas stations, grocery stores, and non-store retailers led the pack with the highest sales. Meanwhile, building supply stores saw the sharpest drop, most likely because of the snow that affected a large part of the country throughout the month. Sales also fell at sporting goods and hobby stores and at restaurants.

Barclays 2/15 - Within the headline, growth among the individual components was mixed. Sales at motor vehicles dealers gained 0.6%, in line with the strength in auto sales recently, and sales at gasoline stations also rose 1.4%, consistent with the increases in energy prices. Building materials, however, fell 2.9% in January.

Today's report indicates that consumer spending continues to grow in early 2011, but that it has decelerated somewhat in Q1 from the elevated rate in Q4.

Econoday 2/15 - Consumers are pausing after a robust November as holiday sales were front loaded due to early discounting by retailers. Also, sales in January likely were softened by severe winter weather in parts of the U.S. Still, the numbers were disappointing.

AFP 2/21 - While January's winter weather may have dampened activity a bit, this was the 7th straight month of retail sales growth.

Business Inventories: Business Inventories Up Slightly

Vanguard 2/18 - Business inventories rose 0.8% in December from a month earlier, slightly more than analysts expected. Manufacturing and wholesale inventory levels increased 1.1% and 1.0%, respectively. Retail inventories increased 0.4%. Total business sales advanced 1.1% for the month. The total inventory-to-sales ratio, a measure of how long it would take to deplete current levels of inventory at current levels of demand, remained steady at 1.25.

Econoday 2/15 - The nation's inventory build continued at a steady rate in December with business inventories up 0.8% for a year-on-year build of 8.0%. This year's outlook for solid economic growth points to further inventory building ahead in what hopefully will be a key plus for future employment growth.

Import and Export Prices

Econoday 2/15 - Import prices jumped 1.5% in January to extend a long string of similar gains. But inflation pressures continue to be isolated to energy and food where year-on-year rates are moving into the mid teens, at plus 14.3% for petroleum imports and at plus 14.8% for food/feed/beverages. These rates are up from December's 13% handles. The year-on-year rate for food/feed/beverages on the export side is at plus 18.0%. Monthly change shows a 2.6% rise for food/feed/beverage imports and a 3.6% gain for exports with petroleum imports at plus 3.4%.

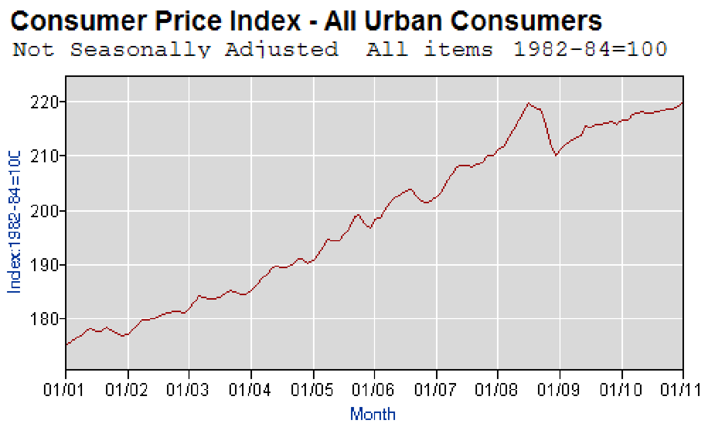
All this pressure, however, remains confined to energy and food. Prices for finished goods remain subdued showing a second straight 0.1% monthly gain for capital-goods imports and a 0.2% gain on the export side. Year-on-year, capital-goods imports are up only 0.2% with consumer import prices at zero.

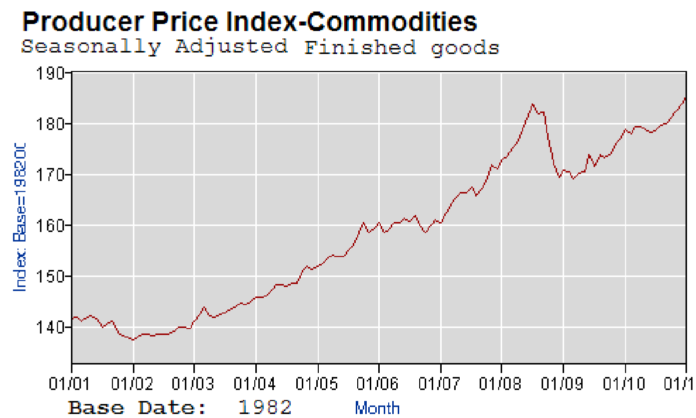
Inflation Indexes – January: Producer and Consumer Prices Rise

Vanguard 2/18 - Higher food and energy prices pushed up the cost of producing and purchasing goods and services. The **producer price index**, which measures how much manufacturers and wholesalers pay for finished goods and materials, jumped 0.8% in January. Core producer prices—which don't take volatile food and energy prices into account—were up 0.5% for the month. The increase in core prices was mostly attributable to higher pharmaceutical prices, which rose 1.4% in January.

The **consumer price index**—a measure of a basket of products and services, including housing, electricity, food, and transportation—rose 0.4% in January. Core consumer prices, excluding food and energy, advanced 0.2%, a 1.0% increase from a year ago. Although the risk of inflation is still low, the rise in prices suggests that the economic recovery is picking up speed.

"There are real concerns about inflationary pressures building in emerging markets; however, this in itself may not become a significant risk factor for U.S. inflation because the pass-through of emerging-market inflation to U.S. import prices is pretty low," said Vanguard economist Roger Aliaga-Díaz. "That is, exporters from emerging markets generally may not want to risk their U.S. market share by charging higher prices. Also, some of the countries that are showing the largest inflationary threats represent only a small portion of total U.S. imports."





Consumer Price Index

Econoday 2/17 - Headline CPI inflation continues its trend of outpacing core inflation-largely on strong gains in energy costs but with food price hikes also contributing. The CPI in January increased 0.4%, following a 0.4% jump in December. The consensus had called for a 0.3% gain in January. Excluding food and energy, CPI inflation in January posted at a 0.2% rise, compared December's increase of 0.1% and exceeding expectations for a 0.1% gain.

By major components, energy increased 2.1% after jumping 4.0% in December. Gasoline rose 3.5%, after spiking 6.7% the previous month. Food price inflation picked up the pace to 0.5% from 0.1% in December. Hikes in energy commodities and food accounted for over two thirds of the all items increase.

The firming in the core rate was led by a 1.0% jump in apparel and 2.2% boost in airline fares.

Year-on-year, overall CPI inflation increased to 1.7% (seasonally adjusted) from 1.4% in December. The core rate rose to 0.9% from 0.6% on a year-ago basis. On an unadjusted year-ago basis, the headline number was up 1.6% in January while the core was up 1.0%.

Overall, today's report shows a firming in inflation pressures and points to upward pressure on interest rates.

Barclays 2/17 - All in all, today's report gives us greater conviction that the core CPI troughed on a % y/y basis in October and will gradually rise during 2011 with small gains in core services likely to remain underpinned by gradual gains in shelter costs and increasing evidence that disinflation in core goods prices has now run its course. Meanwhile food and energy prices are likely to continue to put greater upward pressure on headline CPI.

Producer Price Index

Econoday 2/16 - Inflation is heating up at the producer level for both headline and core numbers. The overall PPI inflation rate posted at a still strong 0.8% increase, following December's revised 0.9% boost and 0.7% jump in November. At the core level, the PPI jumped 0.5%, following a 0.2% increase the month before.

By components, food prices increased 0.3%, after a 0.8% boost in December. The energy component remained red hot, jumping 1.8% after surging 2.8% in December. Nearly forty% of the January advance can be traced to the index for pharmaceutical preparations, which moved up 1.4%. Higher prices for plastic products also contributed to the rise in the finished core index. Passenger car prices dipped 0.1% while light trucks rose a moderate 0.2%. And tobacco edged up only 0.1%.

For the overall PPI, the year-on-year rate slipped to 3.7% from 4.1% in December (seasonally adjusted). The core rate edged up to 1.6% from 1.4 the previous month. Despite Fed comments to the contrary, there are signs of building inflation pressures.

Barclays 2/16 - The upside surprise in the core PPI cannot be attributed to a single temporary factor, but rather strong gains across a range of consumer goods. …it supports our view that disinflation has run its course and upward price pressures at the consumer level now outweigh downward pressures.

Housing Starts – January: Apartment Construction Takes Off

Econoday 2/16 - Housing construction was mixed in January and remained at a very soft level. Starts advanced while permits fell back. Housing starts in January jumped 14.6% after slipping 5.1% the month before. The January annualized pace of 0.596 million units beat analysts' forecast for 0.540 million units and is down 2.6% on a year-ago basis. January's pace is the highest since 0.601 million seen in September 2010. The latest gain was led by a monthly 77.7% surge in multifamily starts, following a 10.8% rise the month before. The single-family component slipped 1.0% after declining 8.4% in December.

By region, gains in starts were seen in the Northeast, up 41.8%; the Midwest, up 36.4%; and South, up 15.8%. For the West, starts declined 9.7%.

Housing permits, in contrast, fell 10.4% in January after improving 15.3% in December. Overall permits came in at an annualized rate of 562,000 units and are down 10.7% on a year-ago basis.

Two key issues: First, strength (albeit soft strength) is in the multifamily component. Homebuilders are still very cautious about the single-family sector with inventory overhang still high. Second, seasonal factors are large during winter months and it is difficult to really sort out the marginal changes. The bottom line is that housing is still anemic although some apparently are a little optimistic about the multifamily sector.

Vanguard 2/18 - Housing starts were up more than expected in January, increasing by an annualized 14.6%—or 596,000 homes—from December. The multifamily home sector, which includes apartment buildings, led the way with an increase of almost 80% for the month.

Barclays 2/16 - The Commerce Department reported last month that building code changes took effect in California, Pennsylvania, and New York, and that this had contributed to a surge in permit activity in the Northeast and the West in December. Looking beyond this volatility, housing starts remain within the range they established in early 2009 and should remain at these levels until excess new home inventories are further reduced.

Industrial Production – January: Industrial Production Dips

Vanguard 2/18 - Industrial production fell 0.1% in January after jumping 1.2% in December, when unusually cold weather and heating demand boosted production at utility companies. In January, when temperatures moved closer to normal, utility output dropped 1.6%. Mining output dropped 0.7%. Factory production was a bit stronger, with a 0.3% gain, thanks to increased demand for motor vehicles and parts.

Barclays 2/16 - The downside surprise partly reflected declines in the volatile utilities and mining components, the former down 1.6%, the latter 0.7%. All in all, the softer tone in January likely reflects the monthly volatility in the data, and perhaps some payback for a very strong December. We expect the recovery in manufacturing output to continue at a solid pace, consistent with the recent strong readings on more timely surveys, particularly the ISM.

Federal Open Market Committee Minutes, Jan 25-26: Fed Improves Growth Forecast

Vanguard 2/18 - Minutes from the Federal Open Market Committee meeting on January 25–26 indicated that the U.S. economic recovery was "firming" but not yet sufficient to make a significant dent in the unemployment situation. The committee planned to maintain its asset purchase program because it expected the labor market to remain soft and inflation below target. Still, it was more optimistic about the economy this year and revised upward its earlier GDP growth forecast from 3.0%-to-3.6% to 3.4%-to-3.9%. The inflation forecast was essentially unchanged at 1.3%-to-1.7%. Despite higher commodity prices, the committee said underlying measures of inflation remained "subdued" and left interest rates unchanged at near zero.

Econoday 2/16 - The Fed's minutes of the January 25-26 policy meeting show an upgrade in the Fed's forecast for economic growth for 2011. The forecast for headline PCE inflation was nudged up for this year while the core PCE number was nudged down. FOMC members stated that they have "greater confidence" in the recovery with some suggesting that the steeper yield curve shows a strengthening economy.

The unemployment rate for Q4 of this year is expected to fall within a range of 8.8 to 9.0% versus 8.9 to 9.1% anticipated in November.

While not stated, the boost in headline inflation is likely related to higher oil and commodities prices while the core PCE rates is still held down by the housing market weighing on rent and owner-occupied implicit rent.

There was somewhat more debate on how much further quantitative easing is needed. The Fed appears more ready to debate whether to end QE2 early if incoming data suggests that is appropriate.

Barclays 2/16 - The minutes of the January FOMC meeting suggest that participants continued to upgrade their views on current conditions and the economic outlook. Participants pointed towards payroll employment growth, which had been "modest" and, at times, "erratic," and the continued downward trend in initial jobless claims, as indicating that the gradual improvement in labor market conditions remained in place.

Downside risks were seen as stemming from credit risk fears in Europe, softness in state and local government budgets, and the weak housing market. Upside risk was seen as stemming from better-than-anticipated household spending and the impact of higher energy/commodity price pressures and higher import costs. Most participants, however, felt that the pass-through of higher commodity prices was likely to be limited given the elevated level of economic slack.

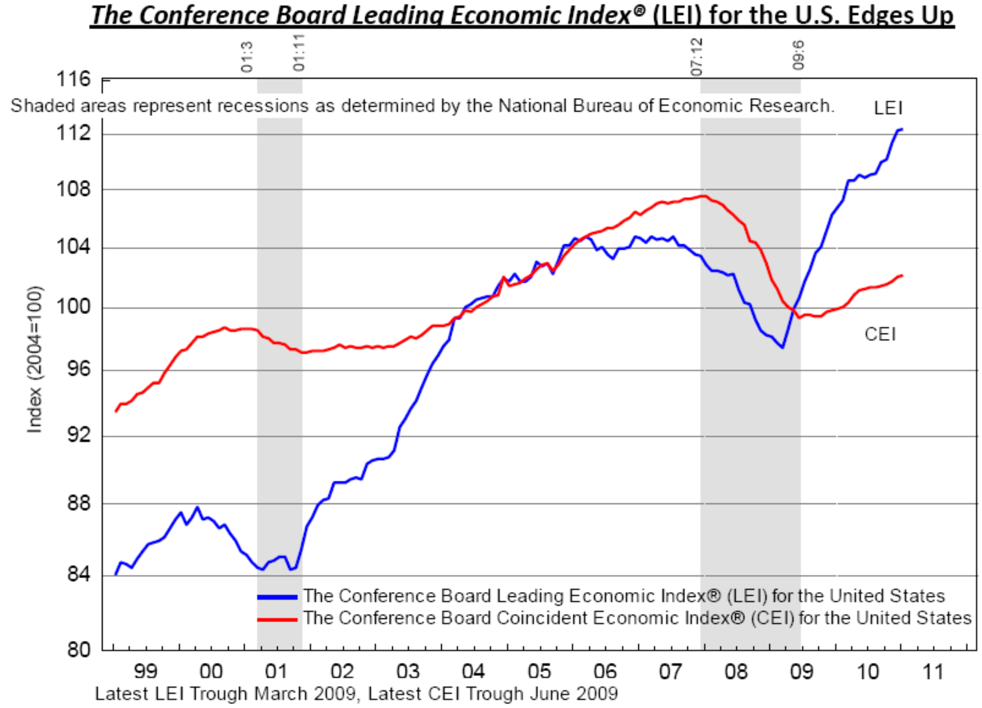
We still see a high threshold for making changes to the asset purchase program (QE2) and see little in the minutes to change our view that the Fed will make good on its intent to purchase the announced $600bn in long-term Treasury securities by the end of the second quarter.

Leading Indicators – January: Leading Indicators Still on the Rise

Vanguard 2/18 - The Conference Board's index of leading economic indicators inched up 0.1% in January—a small gain, but one that extended the upward trend that began in late 2010.

"The economy gained some momentum in late fall, and the latest data suggest that trend will continue," said Ken Goldstein, an economist at The Conference Board. He noted that the increase over the past six months totaled a strong 3%. The index consists of ten financial- and consumer-related measures and is designed to signal peaks and troughs in the business cycle.

The Conference Board Leading Economic Index® (LEI) for the U.S. Edges Up



Six of the ten index components rose during the month. The positive contributions of the financial components were just enough to offset weakness in housing permits and labor-market indicators.

Econoday 2/17 - A month-to-month swing in building permits made for sharp volatility in the index of leading economic indicators where growth slowed to 0.1% in January vs. 0.8% in December (revised down from 1.0%). Building permits were the leading contributor to December's index but subtracted the most in January.

Permit volume was affected by changes in laws in some localities. In a more telling sign of trouble, the second most negative component was initial jobless claims which, based on the weekly report posted earlier this morning, don't look to be of much help for the February LEI.

January's biggest contributor is the yield spread reflecting low front-end interest rates and what have been rising longer maturity interest rates. A slowing in deliveries was the second biggest indication of future economic strength followed by the stock market and by consumer expectations, the latter having shown tangible improvement so far this year.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week ended Feb. 12

Press Release 2/17 (excerpt) – In the week ending Feb. 12, the advance figure for seasonally adjusted initial claims was 410,000, an increase of 25,000 from the previous week's revised figure of 385,000. The 4-week moving average was 417,750, an increase of 1,750 from the previous week's revised average of 416,000.

The advance seasonally adjusted insured unemployment rate was 3.1% for the week ending Feb. 5, unchanged from the prior week's unrevised rate of 3.1%.

The advance number for seasonally adjusted insured unemployment during the week ending Feb.5 was 3,911,000, an increase of 1,000 from the preceding week's revised level of 3,910,000. The 4-week moving average was 3,941,500, an increase of 3,500 from the preceding week's revised average of 3,938,000.

WEEK ENDING	Feb. 12	Feb. 5	Change	Jan. 29	Prior Year
Initial Claims (Seasonally Adj)	410,000	385,000	25,000	419,000	479,000
4-Wk Moving Average (SA)	417,750	416,000	1,750	43100	471,000

Econoday 2/17 - Jobless claims are not pointing to underlying payroll growth. Initial claims rose a steep 25,000 in the February 12 week to 410,000. Continuing claims have been coming down but only slightly and not in the latest data, up 1,000 to 3.911 in the February 5 week. Weather may be blamed for the failure of initial claims to show improvement so far this year, which does hold out hope for the weeks ahead. Otherwise, the jobs market remains a central risk to the economic recovery.

Barclays 2/17 - We see this move as a continued unwind of the weather-related distortions to the previous weeks of claims data. We expect that upcoming reports on jobless claims figures in the coming weeks should provide a clearer picture of trends in labor market conditions.

Federal Agency Debt Issuance Total – 4Q2010 & Year-over-year

SIFMA 2/15 - Federal agency long-term debt issuance was $240.1 billion in the fourth quarter, a 4.6% drop from the prior quarter’s $251.6 billion. Approximately $1.03 trillion was issued for all of 2010, a 7.6% decline from 2009’s $1.12 trillion issued. Overall average daily trading volume of agency securities was approximately $71 billion in 2010, compared to the $77 billion daily average traded in 2009.

The Economic Week Ahead: February 21 – Feb. 25, 2011

Vanguard 2/18 - The highlight of next week’s economic reports will be Friday’s release of gross domestic product figures for the fourth quarter of 2010. Other reports expected next week include: The Conference Board’s index of consumer confidence (Tuesday), existing-home sales (Wednesday), durable goods orders (Thursday), and new-home sales (Thursday).

This Week’s U.S. Economic Calendar ***Source: Briefing.com***

Date	ET	Release	For	Briefing.com	Consensus	Prior
Feb 22	09:00	Case-Shiller 20-city Home Price Index	Dec	-2.2%	-2.4%	-1.59%
Feb 22	10:00	Consumer Confidence	Feb	67.0	67.0	65.6
Feb 23	10:00	Existing Home Sales	Jan	5.40M	5.23M	5.28M
Feb 24	08:30	Initial Claims for Unempl. Benefits	02/19	410K	410K	410K
Feb 24	08:30	Durable Goods Orders	Jan	3.6%	3.0%	-2.3%

Date	ET	Release	For	Briefing.com	Consensus	Prior
Feb 24	10:00	New Home Sales	Jan	335K	310K	329K
Feb 25	08:30	**GDP - Second Estimate**	Q4	3.4%	3.3%	3.2%
Feb 25	09:55	Michigan Consumer Sentiment - Final	Feb	75.5	75.1	75.1