

# Market Comment *Economic Highlights for the week ended March 2, 2012*

## **Economic Week In Review: Patchy but positive**

Vanguard 3/2 - The bevy of reports released this week generally reflected a stable or growing economy, with the durable-goods report being the odd man out. Fourth-quarter gross domestic product (GDP) was revised upward, while manufacturing activity remained sustained and both business and consumer sentiment improved. For the week ended March 2, the S&P 500 Index rose 0.3% to 1,370 (for a year-to-date total return—including price change plus dividends—of about 9.68%). The yield on the 10-year U.S. Treasury note rose 1 basis point to 1.99% (for a year-to-date increase of 10 basis points).

## **Pending Home Sales Index - January**

Econoday 2/27 – Contract signings for existing home purchases rose 2.0 percent in January and point to strength ahead for final sales. January's strength is centered in the South which is by far the largest region for home sales. Year-on-year, the region shows a very strong 10.5 percent gain which points to building strength for already solid national year-on-year growth of 8.0 percent.

Though contract signings often don't make it to closing due to credit and appraisal snags, today's report hints at a rising economic contribution from the housing sector.

Barclays 2/27 - Overall, the direction of the various revisions, along with the January estimate, point to a choppy, though steadily improving trend. As pending home sales progress, existing home sales tend to follow with a month or two lag, which suggests the modest improvement in the housing market is likely to continue.

## **Durable Goods Orders - January: Orders likely to rebound from sharp decline in January**

Vanguard 3/2 – New orders for long-lasting manufactured goods fell 4.0% in January. A decline was expected for several reasons: Orders for commercial aircraft, which tend to be bulky and volatile, were strong in both November and December; a tax incentive allowing 100% depreciation of equipment purchases expired at year-end; and, historically, orders have tended to be lower in the first month of a quarter. But even though automobiles continued to gain ground, orders and shipments of "core" capital goods such as equipment, machinery, and computers (widely considered a proxy for business investment) fell sharply.

Econoday 2/28 – The durables orders indicator is living up to its reputation as the most volatile monthly series among major indicators. It appears to be two steps forward and then one step backward. While disappointing, today's report should be interpreted cautiously as the overall picture for manufacturing still looks good.

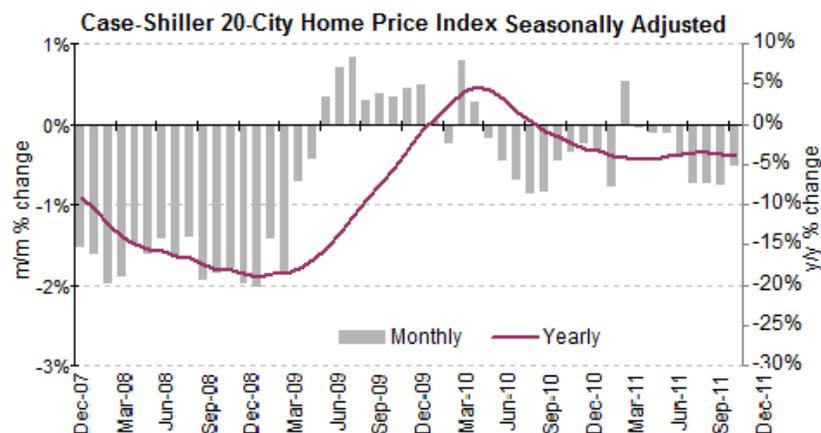
## **Case-Shiller Home Prices -December: Prices slip, though a greater number of cities show gains**

Econoday 2/28 – Home prices are falling, indicated by S&P Case-Shiller data for December that show a very steep 0.5 percent adjusted monthly decline for the 20-city index. The year-on-year rate ended 2012 with a minus 4.0 percent, the worst reading since the housing crisis began in mid-2006.

Unadjusted readings for the 20-city index tell the same story with the year-on-year rate down 4.0 percent and the monthly down 1.1 percent. A look across individual cities shows 12 of the 20 cities with adjusted monthly declines, some quite severe.

Supply has been coming down in the housing sector which should help prices. Lower prices are a negative for homeowners but will stimulate sales.

Barclays 2/28 - On a regional level, 8 of the 20 metropolitan statistical areas experienced gains. The broadening of increases across cities stands in contrast to last month, when only three cities had price gains. Overall, we view the larger number of cities that experienced price gains to be a positive indicator that more cities are turning the corner and will likely experience stable, to slightly rising, home prices in the year ahead.



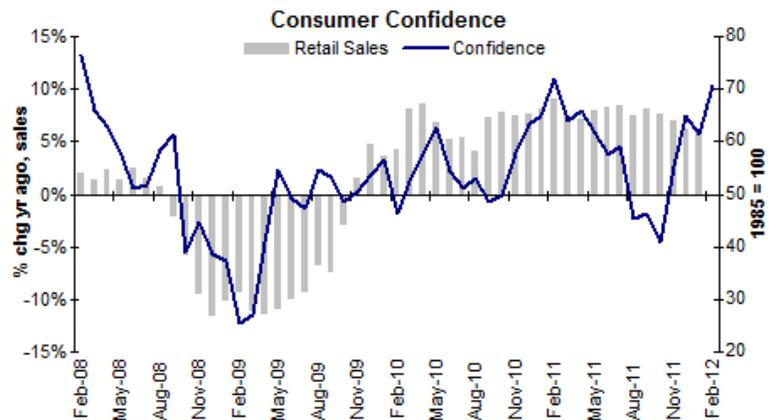
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## Consumer Confidence - February: Consumer confidence surges higher in February

Vanguard 3/2 –The Conference Board's index of consumer confidence beat expectations, climbing more than 9 points to 70.8 in February. The level is the highest in a year but still well below a typical nonrecession reading.

Especially significant was the drop in respondents who agreed with negative statements, such as that jobs are hard to get, business conditions are bad, and they expect to have less income in six months.

Econoday 2/28 – February has been a very strong month for the jobs market, indicated by sizable declines in jobless claims and by today's consumer confidence report that shows a big decline in those describing jobs as hard to get, down to 38.7 percent, the first reading below 40 percent since November 2008. The strength in job activity is reflected in new optimism for income prospects with optimists, at 15.4 percent, ahead of pessimists, 12.7 percent.



## GDP – Q4: Fourth-quarter GDP revisions show slightly better fundamentals

Vanguard 3/2 – Annualized growth in the nation's fourth-quarter gross domestic product was revised upward to 3.0%, which was better than the pace of the third quarter (at 1.8%). Inventory buildup was a substantial component of business spending and continued to be the primary driver of GDP growth in the quarter, in contrast to the inventory shrinkage of the third quarter. Consumer spending edged up, and revised figures for trade and government spending showed them to be a bit less of a drag on economic performance.

Barclays 2/29 - The household income accounts revealed more sizable revisions, and wholly positive ones. Real disposable income growth was revised up to 1.4%, driven by stronger wage and salary growth. This provides a much healthier backdrop for households than previous estimates suggested - a stronger income and savings picture should support consumer spending growth in Q1 and beyond. Inflation measures were generally revised higher too, the GDP price index to 0.9% q/q (saar), the PCE price index to 1.2% and the core PCE to 1.3%.

Stronger real consumption growth and consumer price inflation than previously estimated was more than trumped by significant upward revisions to household income and savings. The large boost to GDP growth from stock building in Q4 is unlikely to be repeated in Q1 but the household accounts provide a much more encouraging backdrop for consumer spending.

## Beige Book – February: Beige Book indicates 'modest to moderate' growth

Vanguard 3/2 –The Federal Reserve's Beige Book showed overall economic conditions generally improving between January and early February. Manufacturing expansion was a bright spot in all districts. A slight increase in hiring was noted in some districts as well as higher capital spending in the technology and auto sectors. Most districts reported an increase in home sales, and some showed increased construction activity.

Barclays 2/29 - The Federal Reserve's February Beige Book suggested that overall economic activity "continued to increase at a modest to moderate pace", the same pace shown in the last Beige Book. Overall economic expansion ranged from "somewhat slower" to "firm", but none of the districts reported a decline in activity. Manufacturing activity showed encouraging signs and continued to expand in all twelve districts. Activity in nonfinancial services "remained stable or increased," while the retail sector reported positive consumer spending. Banking conditions were "generally improved". Hiring "increased slightly" across most districts, and some reported difficulties in finding skilled workers. Reports of consumer spending were largely positive. Wage pressures were reported as "contained," and prices of final goods were described as "stable." Real estate activity was described as having "increased modestly" in most districts, and the outlook on home sales growth was "mostly optimistic." In our view, this report shows a modest expansion of economic activity.

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## Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week of Feb 25

Press Release 3/1 (excerpts) - In the week ending February 25, the advance figure for seasonally adjusted initial claims was 351,000, a decrease of 2,000 from the previous week. The 4-week moving average was 354,000, a decrease of 5,500.

WEEK ENDING	Feb 25	Feb 18	Change	Feb 11	Prior Year
Initial Claims (SA)	351,000	353,000	-2,000	351,000	375,000
4-Wk Moving Average (SA)	354,000	359,500	-5,500	366,000	392,500

Barclays 3/1 –The four-week moving average fell to 354k, marking another new post-recession low. Overall, the report was again positive, and along with other labor market data, the broader improvement in the labor market is becoming more convincing.

We see the ongoing improvement in the claims data, along with other labor market indicators, suggesting that private employment gains have breadth across sectors and, thus, are likely to rise in line with its recent trend. Favorable weather conditions are also likely to support hiring in construction-related sectors. We expect employment losses at the federal and local levels to continue.

## Personal Incomes and Outlays - January

Barclays 3/1 – The January personal income and spending report revealed a 0.2% m/m increase in consumer spending. With a 0.2% increase in the PCE price index this translated into a flat reading on real consumption. Directly plugging this in to our Q1 GDP tracking estimate has a significant effect - real GDP growth is now tracking 1.5% q/q (saar), down from 2.5%. However, we would note two caveats:

First, the weakness of consumption is at odds with several other indicators for January - strong core retail sales and unit vehicle sales pointed to a much stronger pace of spending, and the improvement in employment and production surveys have suggested a pick up in demand. In addition, the strong upward revisions to household income and savings portray a solid backdrop for household spending.

Second, a significant contribution to the soft pace of growth in January was a sharp decline in household utilities consumption, likely related to the warmer-than-average winter weather. This suggests that greater disposable income will be available for spending in other areas in the coming months.

The income side of the report was also softer than expectations. The details were a little more encouraging, with a 0.4% gain in wages and salaries. Real disposable income declined 0.1% and the savings rate fell to 4.6%. Finally, the core PCE price index rose 0.2% and was unchanged at 1.9% y/y.

## ISM Manufacturing – February: ISM down in February

Vanguard 3/2 – Manufacturing expansion cooled in February. The index reading of 52.4 was lower than forecast. (A reading above 50 indicates expansion.) There were contrasting signals in the results: Growth in new orders and employment slowed, but order backlogs increased, while growth in production and inventories remained virtually flat. The report indicates that the current reading, when annualized, would correspond to a 3.3% increase in real GDP.

Econoday 3/1 – Activity in the manufacturing sector slowed in February based on the ISM's composite index which came in at 52.4, above 50 to indicate monthly growth but below January's 54.1 to indicate a slower rate.

New orders slowed, to 54.9, as did backlogs, at 52.0. Production also slowed, 55.3, as did employment, at 53.2. But February's rates are respectable and not that much different than January.

A speeding up in delivery times is a major factor behind the slowing in the composite index, while a big plus in the report is a jump in new export orders to 59.5. Inventory readings are lean and stable.

This report, especially following Tuesday's dramatic drop in durable goods orders, points to easing momentum for what has proven to be the backbone of the nation's economic recovery.

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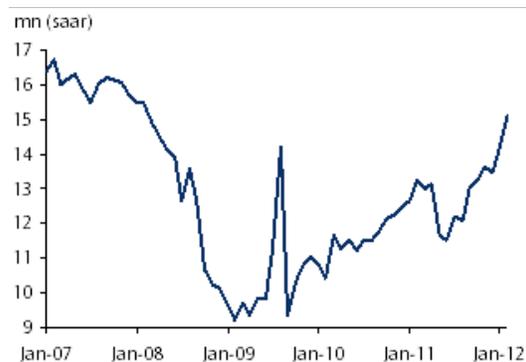
## Construction Spending – January: construction spending softens, trend remains positive

Vanguard 3/2 – Construction spending fell 0.1% in January, but there were large differences by segment. Given the fiscal challenges facing state and local governments, public construction spending was down compared with the previous month and January 2011. Private nonresidential construction spending was down 1.5% in January but up 16.6% compared with a year earlier—owing in part to the auto and natural gas industries. Residential construction spending was up 1.8% in January, with single-family homes, multifamily homes, and residential improvements all making positive contributions. Compared with January 2011, this segment was up 6.7%.

Econoday 3/1 – On a year-ago basis, overall construction gained 7.1 percent in January, compared to 5.7 percent the prior month. The January number was disappointing but follows recently healthy gains. While not robust, construction still appears to be on a modest uptrend.

## Motor Vehicle Sales – February: Surge in US vehicle sales

Barclays 3/1 - Vehicle sales rose to 15.1mn (saar) in February from 14.1mn in January, according to Autodata, This was the strongest since March 2008, beating the pace of sales in August 2009 (boosted by the cash-for-clunkers program). The details showed that the strength was centered in auto sales (which were up to 8.2mn from 7.4mn). Light truck sales rose to 6.9mn. Alongside the gain in January, this represents a very solid start to Q1, with the level of sales well above the average of 13.4mn in Q4, and bodes well for the prospects of broader consumer spending in February following the soft consumption report for January published this morning.



## The Economic Week Ahead: March 5 – March 9, 2012

Vanguard 3/2-Next week's releases include factory orders and the ISM nonmanufacturing index (Monday), consumer credit and productivity and costs (Wednesday), and international trade and the Labor Department's monthly assessment of the employment situation (Friday).

*This Week's U.S. Economic Calendar*

*Source: MarketWatch*

	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
<b>MONDAY, MARCH 5</b>	10 am	ISM nonmanufacturing	Feb.	56.8%	56.8%
	10 am	Factory orders	Jan.	--	1.1%
<b>TUESDAY, MARCH 6</b>		None scheduled			
<b>WEDNESDAY, MARCH 7</b>	8:15 am	ADP employment	Feb.	--	170,000
	8:30 am	Productivity	4Q	0.6%	0.7%
	8:30 am	Unit labor costs	4Q	1.3%	1.2%
	3 pm	Consumer credit	Jan.	--	\$19.3 bln
<b>THURSDAY, MARCH 8</b>	8:30 a.m.	Jobless claims	3/3	N/A	N/A
<b>FRIDAY, MARCH 9</b>	8:30 am	<b>Nonfarm payrolls</b>	Feb.	208,000	243,000
	8:30 am	Unemployment rate	Feb.	8.3%	8.3%
	8:30 am	Trade deficit	Jan.	-\$48.8 bln	-\$48.8 bln
	10 am	Wholesale inventories	Jan.	--	1.0%