Market Comment *Economic Highlights for the week ended April 15, 2011*

Economic Week in Review: The Fed Faces Economic Crosswinds

Vanguard 4/15 - The U.S. economic engine continues to chug along at a moderate pace, with the latest data showing strong industrial production, reasonable sales growth, and an uptick in inflation. For the week ended April 15, the S&P 500 Index fell 0.6% to 1,320 (for a year-to-date total return—including price change plus dividends—of about 5.5%). The yield of the 10-year U.S. Treasury note fell 16 basis points to 3.43% (for a year-to-date increase of 13 basis points).

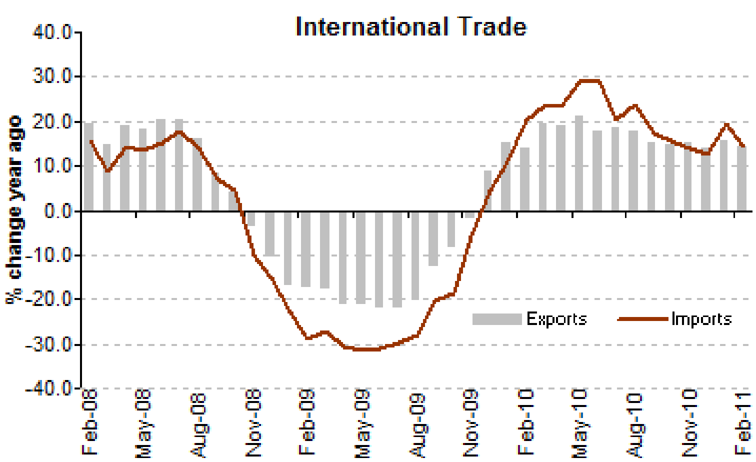
Breaking News: Monday, April 18: S&P Releases a Negative Outlook on the U.S. Sovereign Debt Rating

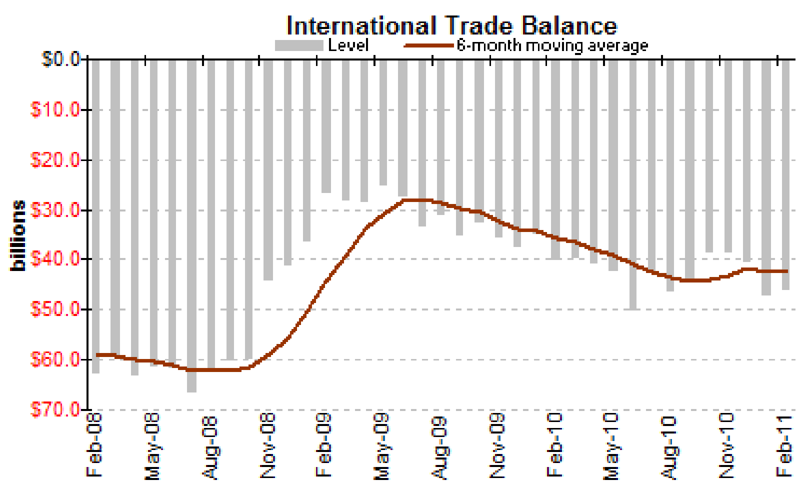
Trade Balance: February - U.S. Imports and Exports Decline Slightly

Vanguard 4/15 - The U.S. trade deficit narrowed to $45.8 billion in February from a revised $47.0 billion in January. Both exports and imports fell slightly. Consumption-based trade is growing, except for automobiles. Both car imports and exports slowed, which was attributed to worries about higher oil prices. The dollar depreciated against most major currencies in February, with the Federal Reserve's broad trade-weighted dollar index depreciating 0.8% over January.

Econoday 4/12 - Exports were also lower, down $2.4 billion. The export side shows declines for autos, industrial supplies and, despite a jump in civilian aircraft, a decline for capital goods exports. The decline in capital goods activity in this report points to slowing for business investment.

Today's data are for February which is even more ancient history than March. Oil at $110 is 30% more expensive than it was in February, a factor that will deepen the trade deficit. One factor that could narrow the trade gap is an unwanted one, that is supply disruption tied to Japan.





Import and Export Prices - March

Econoday 4/12 - Import prices jumped 2.7% in March but were heavily skewed by a 10.5% surge in prices of petroleum imports. Excluding petroleum, import prices rose 0.3%, a step down from the prior four months which saw a 0.9% peak in January. The year-on-year rate for total import prices is definitely picking up steam, back near the double digits at a plus 9.7% rate in March.

Export prices are also on the rise, up 1.5% and at the high end of trend. The year-on-year rate is also nearing the double digits, at plus 9.5%. Here food inflation is at work with agricultural prices up 2.3% in the month.

Inflation in today's report is definitely hot but it's confined to energy and food. Today's data point to high non-core readings for Thursday's producer price report and possibly Friday's report on consumer prices as well.

Treasury Budget

Econoday 4/12 - The Treasury deficit in March came in about as expected at $188.2 billion. Half way through the fiscal year, the government's deficit is $829.4 billion for a year-on-year deepening of more than 15%. Outlays are running nearly 11% higher this fiscal year and, in a special item for March, include $5.9 billion for housing and economic recovery programs. Net interest expense, up 10% this fiscal year, shows the most pressure of the outlay side. Growth in receipts is only seven percent but individual taxes, up 21%, are a special strength.

Retail Sales: March – Retail Sales Still Growing, But At A Slower Pace

Vanguard 4/15 - Growth in retail sales slowed in March, in part because of a decline in auto sales. Overall retail sales grew 0.4%, the slowest rate since June. However, excluding autos, sales growth was a more robust 0.8%, testifying to the health of underlying spending. Growth was led by the energy sector and also by housing-related sectors. Sales were 7.1% above their year-ago level.

Econoday 4/13 - Importantly, sales excluding autos and gasoline in March advanced 0.6%, following a 0.9% increase in February. Some of components that are strong include furniture & home furnishings (3.6%), building materials (2.2%), electronics & appliance stores (2.1%), clothing (0.6%), general merchandise (0.4%), and food services & drinking places (1.0%).

While the headline number came in below expectations, it also was strong. And even after discounting higher gasoline prices, spending is healthy. The cost of filling up at the gas station may be cutting into discretionary income-but not yet spending.

Business Inventories: February - Business Inventories Rise Less Than Expected

Vanguard 4/15 - Total business inventories increased 0.5% in February. The softer growth was mainly due to an outright decline in retail inventories. The total business inventories-to-sales ratio was 1.24, but the retail figure was 1.31, indicating retail inventories are the leanest they've been on record, dating back to early 1990s.

Econoday 4/13 - Among the three components, inventory accumulation at wholesalers held steady and strong, accumulation at manufacturers slowed, while retailers shed inventory in the month. The pace of build for business inventories slowed during January and February, and a big build will be needed for March to keep first-quarter inventory growth in line with fourth-quarter growth.

Crude Inventories – Week Ended April 8

Econoday 4/13 - A major draw in gasoline, seven million barrels, headlines EIA's petroleum inventory data for the April 8 week. Refinery output has been soft with the 81.4% capacity rate the lowest in seven weeks. This time last year refineries were busier, then operating above 85%. The slowing in refinery output may be due to demand which, in reaction to high prices, is softening, now at minus 1.6% for the worst year-on-year rate of the recovery. In contrast to the product draws, oil inventories rose 1.6 million barrels to 359.3 million barrels.

Fed's Beige Book - Fed report says the recovery is broadening

Vanguard 4/15 - The recovery continued to broaden in March, according to the Federal Reserve's latest Beige Book survey of nationwide conditions. All of the Fed's 12 districts reported at least modest improvement in economic activity. Manufacturing continues to be strong, consumer spending continues to grow, and more than half the districts reported improvement in commercial real estate. Potential clouds on the horizon include possible supply-chain disruptions caused by the Japanese disaster and rising prices for energy and commodities, which could eventually exert upward pressure on wages.

Econoday 4/13 - The latest Beige Book shows the economy continuing to improve. Leading the economy is manufacturing with consumers also contributing. Labor markets are gradually improving. However, higher commodity costs are putting upward pressure on prices. Wage inflation remains subdued.

"Reports from the twelve Federal Reserve Districts indicated that economic activity generally continued to improve since the last report. While many Districts described the improvements as only moderate, most Districts stated that gains were widespread across sectors. Manufacturing continued to lead, with virtually every District citing examples of steady improvement, often with reports of increased hiring. Business services, including freight-related activities, improved in most Districts.

"Reports focusing on the near-term outlook were most often upbeat. Most Districts reported that labor market conditions were generally stronger than in their last reports. Wage pressures were described by most Districts as weak or subdued, but higher commodity costs were widely reported to be putting increasing pressures on prices. Energy prices were cited most often, but raw materials in general were an increasing concern of businesses. The ability to pass through cost increases varied across Districts, with manufacturers generally finding less resistance to price increases than either retail or construction. Input prices rose in most Districts, particularly for cotton and other agricultural commodities, petroleum-based products, and industrial metals. In addition, shippers added fuel surcharges in several Districts"

Overall, the latest Beige Book shows the recovery continuing. The economy is growing but has weak spots. There is still slack in labor markets but commodity prices are boosting inflation pressures.

Unemployment Insurance Weekly Claims Report – week ended April 9

Press Release 4/14 (excerpt) - In the week ending April 9, the advance figure for seasonally adjusted **initial claims** was 412,000, an increase of 27,000 from the previous week's revised figure of 385,000. The 4-week moving average was 395,750, an increase of 5,500 from the previous week's revised average of 390,250.

The advance seasonally adjusted **insured unemployment rate** was 2.9% for the week ending April 2, a decrease of 0.1 percentage point from the prior week's unrevised rate of 3.0%.

The advance number for seasonally adjusted **insured unemployment** during the week ending April 2 was 3,680,000, a decrease of 58,000 from the preceding week's revised level of 3,738,000. The 4-week moving average was 3,728,750, a decrease of 20,750 from the preceding week's revised average of 3,749,500.

WEEK ENDING	April 9	April 2	Change	March 26	Prior Year
Initial Claims (Seasonally Adj)	412,000	385,000	27,000	392,000	477,000
4-Wk Moving Average (SA)	395,750	390,250	5,500	395,250	465,250

Econoday 4/14 - Initial jobless claims for the April 2 week fell 10,000 to 382,000 from 392,000 in the prior week (revised from 388,000). The four-week average of 389,500 is down more than 5,000 from a month ago. Continuing claims edged lower in the March 26 week, to a four-week average of 3.746 million with the month-ago comparison showing a 100,000 decline.

PPI: March – Energy costs boost the producer price index too

Vanguard 4/15 - The Producer Price Index (PPI), a gauge of inflation in the manufacturing process that can be a precursor to inflation in consumer prices, rose 0.7% in March. The increase puts producer prices 5.8% higher than a year earlier. About 90% of the monthly increase was attributed to energy costs. As with the Consumer Price Index, when food and energy costs were excluded, the rise in the "core" PPI was lower, at 0.3%.

Econoday 4/14 - Producer price inflation at the headline level in March remains under heightened upward pressure from higher oil costs. Meanwhile the core was bumped up but not to the same degree. Energy led the latest gain while food edged back from a huge surge in February. The biggest culprits in the core acceleration were light motor trucks and passenger cars.

Consumer Price Index: March - Food and energy costs push up consumer prices

Vanguard 4/15 - The Consumer Price Index (CPI) increased 0.5% in March. The cost of gasoline and food continued to rise and together accounted for almost three-quarters of the overall increase. Compared with a year earlier, consumer prices were 2.7% higher. The core CPI—which excludes more-volatile food and energy costs—remained tame, rising only 0.1% for the month. Year-over-year, the core CPI has gained 1.2%, a rate still lower than the Federal Reserve's comfort zone for core inflation of 2.0%–2.5%.

Econoday 4/15 - Today's CPI report is a tale of two cities-headline is hot while the core is subdued. Excluding food and energy, the CPI eased to 0.1%, following a 0.2% rise.

By major components, energy jumped 3.5% after surging 3.4% in February. Gasoline increased 5.6%. Food price inflation worsened to a 0.8% gain, following a 0.6% boost in February.

The core was softened by a 0.5% decline in apparel prices, a 0.1% dip in household furnishings, a flat recreation component, and shelter rising only 0.1%. On the upside, notable gains were seen in new & used vehicles, up 0.8%, and public transportation, up 1.3% largely on airline fares.

Today's report provides a policy quandary for the Fed or at least a public relations bump in the road if some FOMC participants want to keep arguing that all that matters is the core. If that is the case, perhaps consumers should go out and rebuild their wardrobe instead of eating and driving. The bottom line is that this report raises the debate about what counts in making monetary policy.

Empire Manufacturing

Econoday 4/15 - Manufacturing activity in the Empire State region is robust and shows no substantial effect from Japan. New orders surged in the April report as did shipments and, yes, even employment. A look at the supply chain shows no lengthening in delivery times. In a special question, 80% of the sample report little or no impact from the crisis in Japan. The news isn't all good given further acceleration in prices including strong acceleration in prices received, an indication of cost pass through. But this report is very positive.

Industrial Production and Capacity Utilization: March

Vanguard 4/15 - Industrial production—the output of the nation's manufacturers, mines, and utilities—rose 0.8% in March, above expectations and following modest increases in the previous two months. This puts first-quarter output growth at an annual rate of 6.0% compared with 3.2% in the fourth quarter of 2010. A healthy rise in motor vehicle production boosted overall output in the manufacturing sector. At least within the report's scope, Japan's natural disaster woes had not created any significant disruption in the manufacturing process. Capacity utilization rose to 77.4% from 76.9%, well below levels that would strain resources and stimulate inflation.

Econoday 4/15 - The manufacturing sector continues to fuel the recovery. Importantly, manufacturing continued a string of healthy gains, advancing 0.7%, following a 0.6% boost in February. A jump in auto production helped but other manufacturing components also were positive. For other sectors, utilities rebounded 1.7% after dropping 3.6% in February. Mining gained 0.6% in March.

Within manufacturing, durables advanced 1.0% in March, and gains were widespread across its major categories. The output of motor vehicles and parts rose 3.0%. Excluding autos, manufacturing rose 0.6% in March. Nondurables manufacturing rose 0.5% in March. Leading the boost were chemicals and paper.

The manufacturing sector remains robust in March and April is also likely to be a healthy month according to a strengthened Empire State manufacturing report earlier this morning.

Consumer Sentiment

Econoday 4/15 - Consumer sentiment, at 69.6 for the mid-month reading vs March's 67.5, is improving but remains near six-month lows. The gain is centered in the expectations component which is the composite's leading component and which gained more than three points to a 61.2 level that, however, is still near a six-month low. The current conditions component, at 82.7 for a small gain, has been holding up better than expectations. Inflation expectations remain very elevated for the one-year outlook, unchanged at 4.6 percent, but they did fall back three tenths for the five-year outlook to 2.9%. This report is positive, pointing to another bounce off lows for consumer spirits.

The Economic Week Ahead: April 18 – April 22, 2011

Vanguard 4/15 – Next week—a relatively quiet one with the Good Friday holiday—will bring data on new residential construction (Tuesday) and existing-home sales (Wednesday), and the Conference Board's report on economic leading indicators on Thursday.

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

Date	ET	Release	For	Briefing.com	Consensus	Prior
Apr 18	10:00	NAHB Housing Market Index	Apr	17	17	17
Apr 19	08:30	Housing Starts	Mar	500K	520K	479K
Apr 19	08:30	Building Permits	Mar	530K	540K	517K
Apr 20	07:00	MBA Mortgage Purchase Index	04/16	NA	NA	NA
Apr 20	10:00	Existing Home Sales	Mar	5.15M	5.00M	4.88M

Date	ET	Release	For	Briefing.com	Consensus	Prior
Apr 20	10:30	Crude Inventories	04/16	NA	NA	NA
Apr 21	08:30	Initial Claims	04/16	370K	390K	NA
Apr 21	08:30	Continuing Claims	04/16	3650K	3650K	NA
Apr 21	10:00	Philadelphia Fed	Apr	30	33.0	43.4
Apr 21	10:00	Leading Indicators	Mar	0.2%	0.2%	0.8%
Apr 21	10:00	FHFA Housing Price Index	Feb	NA	NA	-0.3%