

# Market Comment *Economic Highlights for the week ended April 27, 2012*

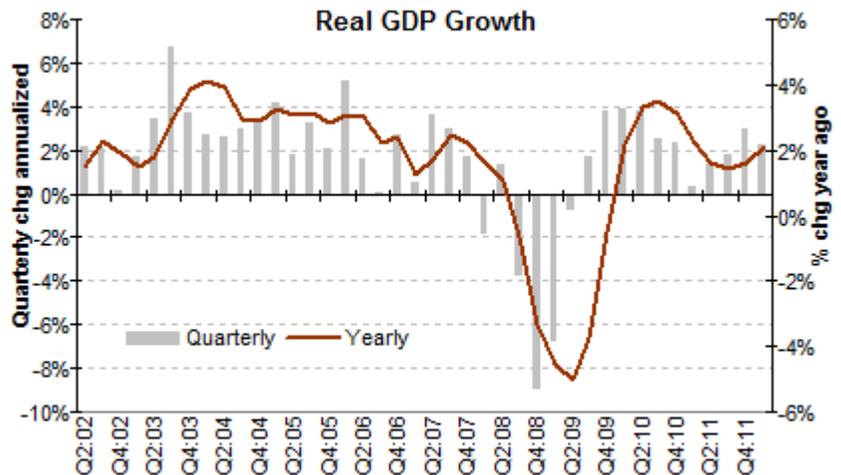
## Economic Week In Review: Growing At A Modest But Uneven Pace

Vanguard 4/27 - The U.S. economy grew at a slower pace in the first quarter of 2012 than in the previous quarter, according to the closely watched gross domestic product (GDP) report. Other economic data supported the view that the recovery continues to advance at a modest but uneven pace. For the week ended April 27, the S&P 500 Index rose 1.8% to 1,403 (for a year-to-date total return of about 12.3%). The yield on the 10-year U.S. Treasury note fell 3 basis points to 1.96% (for a year-to-date increase of 7 bps).

## GDP Grows More Slowly At 2.2% (1Q2012 First Estimate)

Vanguard 4/27 - The U.S. economy's growth slowed a bit in the first quarter of 2012, according to the first estimate from the Commerce Department. The annual rate of real gross domestic product (GDP)—the broadest measure of goods and services produced by the United States—was pegged at 2.2%, down from 3% in the fourth quarter of 2011.

The report contained support for both optimists and pessimists. The slowdown was mostly caused by disappointing data on business spending, including investment in nonresidential structures. Total fixed investment grew only 0.2%. On the brighter side, investment in residential structures rose to its highest level since mid-2010. Also, personal consumption accelerated from 1.5% in the previous quarter to 2% for the first quarter of the year, and exports increased more than imports, helping the international trade data to provide a more positive influence than in the previous quarter. Slower income growth combined with higher spending pushed the savings rate down from 4.5% to 3.9%, the lowest reading since 2007. (All figures are annualized and adjusted for inflation.)



This GDP report is in line with expectations," said Roger Aliaga-Díaz, Vanguard senior economist. "What's concerning is the composition of the aggregate demand data. We saw further weakening in business capital spending and further strengthening in consumer spending, which seems to be financed out of savings. We'll need the reverse trend to have a more sustainable growth rate for the recovery."

## Final Market Comment Report

**Funding Corporation is discontinuing the Market Comment report.** This report was launched in the pre-internet days when access to economic data and opinion was limited. Now, economic data is as close as your smart phone. For a quick summary of the week's important economic indicators, I continue to recommend the Vanguard Funds economic commentary, published on Fridays and available in the Personal Investors site, News Archive. <https://personal.vanguard.com/us/insights/article/economic-week-review-04272012>

If your economic data needs are more extensive please contact me and Funding Corp will make arrangements with a Selling Group Member to provide client access to economic commentary.

## FOMC Announcement: Fed Holds Steady, Sees Moderate Growth Ahead

Vanguard 4/27 - As expected, the Federal Reserve's policymaking committee announced this week that it was holding steady with its current monetary stance. The Fed said its key short-term interest rate (now between 0% and 0.25%) is still expected to remain "exceptionally low" until late 2014. The Fed's statement did note the recent inflationary impact of higher crude oil and gasoline prices, although it termed the effect a short-term one. The committee issued a revised longer-term forecast that was slightly more bullish than the one it issued in January. Committee members now foresee gross domestic product to rise 2.4% to 2.9% in 2012, compared with a forecast of 2.2% to 2.7% three months ago.

Econoday 4/25 – On other policy issues, Operation Twist continues-the Fed continues to keep downward pressure on longer-term interest rates. The balance sheet is being maintained at high levels with reinvestment of principal

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paid on agency debt and mortgage-backed securities and rollover of Treasuries. There is no mention of QE3 but options remain open.

"Voting against the action was Jeffrey M. Lacker, who does not anticipate that economic conditions are likely to warrant exceptionally low levels of the federal funds rate through late 2014."

Barclays 4/25 - Three language changes in the statement suggested a Fed on hold. First, the committee says it expects growth "to remain moderate over coming quarters and then to pick up gradually." The addition of the phrase that growth is expected to pick up is noteworthy and an upgrade from previous statements. Second, the committee signaled that it now sees "some signs of improvement" in the housing sector, although it still classifies the sector as "depressed." This is the first positive statement related to housing in an FOMC statement since late 2009. Finally, the statement says "inflation has picked up somewhat," although the committee still views the energy impulse as transitory. Taken together, 1) a firmer inflation backdrop, 2) a Fed that expects growth gradually to improve, and 3) a housing market that has more light and less tunnel does not sound to us like a Fed that is expecting to provide further stimulus. As always, Fed policy is data dependent; but for now, the Fed appears comfortable staying "on hold."

### Bernanke Press Conference Q&A

Econoday 4/25 – When asked whether the Fed is "closer" to QE3, Bernanke recapped Fed actions indicating aggressive policy, but he essentially dodged the question indicating that the Fed will continue to assess the economy, will assess costs and benefits, but additional easing is "still on the table."

On whether inflation has come down as expected, Bernanke repeated that Q1 movement in inflation is due to transitory sources and that he expects inflation to be at or below 2% by the end of 2012.

Regarding the "bias" of the FOMC, Bernanke sees current policy as "accommodative" and supported by a 9 to 1 vote at today's FOMC. But if the outlook strengthens, the committee will have to respond.

Bernanke noted that the U.S. is not in deflation as was the case for Japan 15 years ago. Since the U.S. is not in deflation, additional accommodation is not needed although monetary policy is extraordinarily accommodative.

Regarding fiscal policy, if Congress does not address fiscal contraction coming in January (tax increases and spending cuts), he noted it would increase risks to the economy.

Bernanke said the Fed is working to get rid of Too-big-to-fail and is making progress. This includes Basel III rules, stress tests, and a range of regulatory rules. He indicated that there must be the ability for a large institution to fail in an orderly manner and Dodd-Frank is helping to get there. He notes that government safety nets for banks have been cut back.

Barclays 4/25 - One notable comment was his view that **only 100k jobs per month are now needed to keep the unemployment rate stable**, significantly less than used to be the case. This is quite close to our own estimate (75-100k per month), driven by our view that retirements among the baby boomers are the largest factor pushing the labor force participation rate down. To the extent this represents a change in the Fed's view, it helps to explain why it is now looking for a faster drop in the unemployment rate.

### Consumer Confidence (April) Holds Nearly Steady

Vanguard 4/27 - For the second straight month, The Conference Board's Consumer Confidence Index declined slightly. April's reading of 69.2 was down 0.3 from a revised 69.5 in March. The overall index remained above its first-quarter average reading and much higher than its recent low of 40.9 in October. Improvement in the perception of present conditions was outweighed by increased pessimism about future conditions.

"As was the case last month, the slight dip [in the index] was prompted by a moderation in consumers' short-term outlook, while their assessment of current conditions continued to improve," said Lynn Franco, director of The Conference Board Consumer Research Center. "Overall, consumers are more upbeat about the state of the economy, but they remain cautiously optimistic."

### New Home Sales - March

Vanguard 4/27 - Fewer new homes were sold in March, but the slowdown followed a February reading that was revised sharply higher. Sales dropped to an annual pace of 328,000, a bit higher than analysts' expectations. February's number was revised upward to 353,000, the highest reading since April 2010. January's number was

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also revised higher, causing first quarter sales to rise about an annualized 16% from the fourth quarter of 2011. The inventory of new supply remained below 6 months, indicating a relatively tight market.

Econoday 4/24 – Supply of new homes on the market is manageable, at 5.3 months from February's 5.0. Price data are mixed and hard to read with the median down on the month but the average up sharply. Year-on-year rates are both solidly positive.

The regional sales breakdown for March, though showing big declines in the West and Midwest, does show a strong gain for the Northeast and, importantly, a solid gain for the South which is by the largest region.

Still, the month-to-month total change in March is a disappointment that doesn't point to building momentum for the new home sector. The housing sector is limping along with this report unlikely to build up much confidence for a spring surge.

### Case-Shiller Home Price Index (February)

Econoday 4/24 – Home prices showed mild improvement in February as the seasonally adjusted Case-Shiller composite 20 city index rose a monthly 0.2%, following a 0.1% dip the prior month (originally flat). The year-on-year rate (unadjusted) improved to minus 3.5 from a revised minus 3.9 in February.

As usual, the numbers vary sharply by city. On the plus side, Phoenix continued a string of pluses, rising 2.1% in the latest month. Miami and Minneapolis also are having a nice run upward. On the downside, Atlanta continued its slide, dipping 2.0% in February. Also with negative consecutive strings are Chicago, New York, and Cleveland.

### FHFA Home Price Index – February: First Y/Y Increase Since July 2007

Barclays 4/24 - The Federal Housing Finance Agency purchase-only house price index rose 0.3% m/m in February, above our forecast (0.2%) and consensus (0.1%) estimates. This came alongside a downward revision to the January reading (from 0.0% to -0.5%). By region, gains in the Mountain (1.9%), West S. Central (1.5%), East S. Central (1.0%), New England (0.8%), and South Atlantic (0.7%) more than offset declines in the remaining regions. The gain in February left the index up 0.45% y/y, the first positive reading in the y/y change since July '07.

### Durable-Goods Orders Decline (March)

Vanguard 4/27 - New orders for durable goods fell 4.2% in March, below expectations. The most noticeable number was a nearly 50% slowdown in non-defense aircraft orders. Excluding transportation, orders fell 1.1%. On the plus side, shipments rose 1%. Machinery shipments, up four of the last five months, had the largest increase at 6.5%, reflecting the highest dollar level for this category since the series was first issued in 1992. Inventories continued to grow, most recently at 0.4%. Growing inventories could create a drag on the economy if demand weakens, because manufacturers would likely slow production until they have depleted their stockpiles.

Econoday 4/25 – Durables orders came in unexpectedly soft in March. Transportation was expected to pull down overall orders but core orders also were negative. The positive was in shipments.

### Labor Costs Continue To Rise Modestly (1Q 2012)

Vanguard 4/27 - The Employment Cost Index, a broad measure of employers' labor costs including wages and benefits, ticked up 0.4% in the first quarter. The wages and benefits components of the index each rose 0.5%. Annual growth of total compensation continues to hold steady at nearly 2%.

### Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – Week of April 21

Press Release 4/26 (excerpts) - In the week ending April 21, the advance figure for seasonally adjusted initial claims was 388,000, a decrease of 1,000 from the previous week's revised figure of 389,000. The 4-week moving average was 381,750, an increase of 6,250 from the previous week's revised average of 375,500.

WEEK ENDING	April 21	April 14	Change	April 7	Prior Year
Initial Claims (SA)	388,000	389,000	-1,000	388,000	426,000
4-Wk Moving Average (SA)	381,750	375,500	+6,250	369,250	414,000

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Barclays 4/26 - The recent trend of upward revisions continued: today's report marked the twelfth consecutive week that the level of claims has been revised higher and the eighteenth in the past twenty.

## University of Michigan Consumer Sentiment Index (April)

Econoday 4/27 – Consumer sentiment is inching back near the very highest level of the recovery. The Reuters/University of Michigan index rose slightly to 76.4 in April with strength, given comparison with a slightly lower mid-month reading, loaded in the last couple of weeks. The recovery peak for this index, hit early last year, is just a little higher than the current level. The index also hit a similar peak in early 2010. But the final story for the prior two peaks was disappointment as the index quickly lost steam and slid back -- and especially so last year.

## The Economic Week Ahead: April 30 – May 4, 2012

Vanguard 4/27 - Analysts will be busy next week, as each day will bring fresh readings on the state of the economy. Personal income data are due to come out Monday. Construction spending and an update on manufacturing are on tap for Tuesday. Factory orders will be updated on Wednesday. Thursday will bring reports on productivity and nonmanufacturing industries. To cap off the week, the closely watched employment report will be released on Friday.

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

*Source: MarketWatch*

RELEASE DATE	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
<b>MONDAY, APRIL 30</b>	8:30 am	<b>Personal Income</b>	March	0.2%	0.2%
	8:30 am	<b>Consumer Spending</b>	March	0.3%	0.8%
	8:30 am	Core PCE Price Index	March	0.2%	0.1%
	9:45 am	Chicago PMI	April	62.0%	62.2%
<b>TUESDAY, MAY 1</b>	10 am	ISM Manufacturing Index	April	53.2%	53.4%
	10 am	Construction Spending	March	0.4%	-1.1%
	TBA	Motor Vehicle Sales	April	14.4 mln	14.4 mln
<b>WEDNESDAY, MAY 2</b>	8:15 am	ADP Employment	April	--	209,000
	10 am	Factory Orders	March	-0.5%	1.3%
<b>THURSDAY, MAY 3</b>	8:30 am	Weekly Jobless Claims	4-28	N/A	388,000
	8:30 am	Productivity	1Q	-0.5%	0.9%
	8:30 am	Unit Labor Costs	1Q	3.0%	2.8%
	10 am	ISM Non-Manufacturing	April	55.5%	56.0%
<b>FRIDAY, MAY 4</b>	8:30 am	<b>Nonfarm Payrolls</b>	April	193,000	120,000
	8:30 am	Unemployment Rate	April	8.2%	8.2%
	8:30 am	Average Hourly Earnings	April	--	0.2%

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