Market Comment *Economic Highlights for the week ended June 18, 2010*

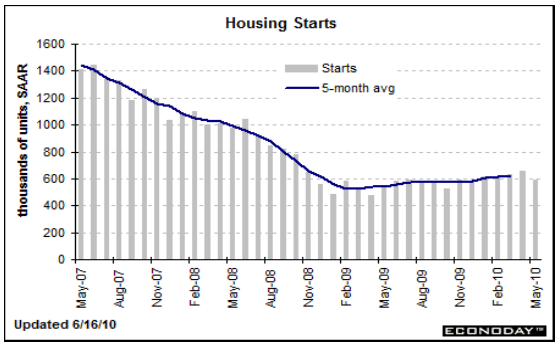
Economic Week in Review: A sluggish but persistent recovery

Vanguard 6/18 - The Conference Board's latest report on leading economic indicators suggests that the U.S. economy continues to expand, but at a subdued pace. Meanwhile, prices fell for both consumers and producers in May, signaling that inflation is likely a distant threat at this point. Housing starts also slipped last month after the government ceased offering tax credits to first-time home buyers. On a positive note, production in our nation's factories continues to surge.

US leading indicators rose 0.4% in May

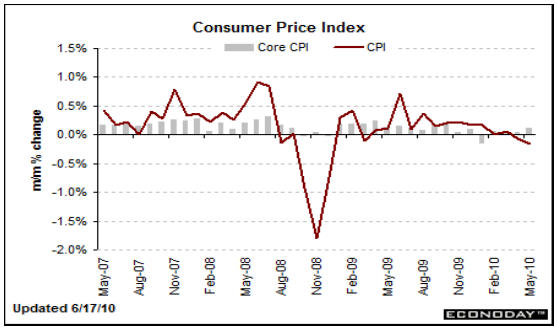
Barclays 6/17 - The index of US leading indicators rose 0.4% in May, a touch below our forecast (0.5%) but in line with that of the consensus. As expected, the wide interest rate spread and increases in the real money supply and workweek drove the improvement, with consumer expectations also contributing positively. Jobless claims and the pace of supplier deliveries were roughly flat, as were estimated consumer goods orders. Declines in stocks, building permits, and estimated nondefense capital goods orders provided some offset. The leading index was up 9.2% y/y in May, down from 10.4% in April but continuing to suggest that while the cyclical rebound may slow somewhat in coming months, it still has momentum.

Housing Starts



WSJ 6/16 - Homebuilders are playing it cautiously after the close of the special tax credits program. Housing starts in May fell back 10.0 %, following a 3.9 % boost in April. May's annualized pace of 0.593 million units came in well below the market projection for 0.650 million units and was up 7.8 % on a year-ago basis. The decline in the latest month was led by a 17.2 % decrease in single-family starts, following a 5.6 % gain in April. The multifamily component actually rebounded 33.0 % after a 5.1 % drop the prior month.

Consumer Price Index



WSJ 6/17 (Excerpts) - Over the last two months, consumer spending power has increased and not just because of income gains. A buck actually goes farther as prices have dropped on average, tugged down largely by lower gasoline prices. In May, overall CPI inflation declined 0.2 %, following a 0.1 % dip in April. The latest number matched the market forecast. Excluding food and energy, CPI inflation rose 0.1 %, following no change in both March and April. Analysts had projected a 0.2 % boost in the core rate.

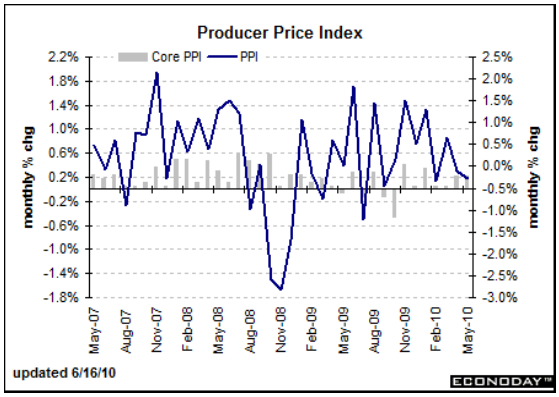
Checking out the components, energy component fell 2.9 %, following a 1.4 % dip in April. Gasoline decreased 5.2 % after a 2.4 % fall the prior month. Food price inflation came in at flat after posting a 0.2 % rise in April. Helping to keep the core rate soft was no change in the owners' equivalent rent subcomponent. This series has either been flat or negative for several months. Also, recreation was flat and medical care edged up only 0.1 % for the latest month. Year-on-year, overall CPI inflation slowed to 2.0 % (seasonally adjusted) from 2.2 % in April. The core rate in May was steady at 1.0 %. On an unadjusted year-ago basis, the headline number was up 2.0 % in May while the core was up 0.9 %.

Barclays 6/17 (Excerpts) - Within non-core items, energy prices fell 3.0% and food prices were flat, the former slightly stronger than our forecast, the latter slightly weaker. The drop in energy prices was driven by a 5.0% decline in gasoline prices, reflecting a small decline on the month and a large negative seasonal factor, as we had factored in.

Within the core, most components posted small increases. Apparel prices rose 0.2%, following four straight months of declines; vehicle prices were also up 0.2%, public transport 1.5% and shelter 0.1%. The latter reflected 0.0% readings on the rent and owner's equivalent rent (OER) components and a 2.5% jump in lodging away from home. On an unrounded basis, OER posted the firmest reading (+0.03%) since August 2009. Cut another way, both core goods and core services rose 0.1%. On a y/y basis, the CPI fell to 2.0% from 2.2%, and the core was unchanged at 0.9%.

Producer Price Index

WSJ 6/16 - Gasoline prices pulled down the PPI but not as much as expected due to sharp gains in some narrow components of the core. Overall PPI inflation weakened even further to a 0.3 % drop in May after dipping 0.1 % in April. May's decline was less negative than analysts' projection for a 0.5 % decrease. At the core level, the PPI gained 0.2 %, matching the rate in April. The consensus had called for a 0.1 % uptick. The core was boosted largely by jumps in prices for tobacco products and for light trucks.



The decline in the headline PPI was led by a 1.5 % drop in energy costs, following a 0.8 % dip in April. Gasoline fell 7.0 % in May after slipping 2.7 % the prior month. Also adding to weakness in the headline number was a 0.6 % decrease in food prices after a 0.2 % decline in April.

At the core level, the mild acceleration in May was led by a 2.2 % spike in tobacco prices and a 0.8 % boost in light truck prices. For the overall PPI, the year-on-year rate eased to 5.1 % from 5.4 % in April (seasonally adjusted). The core rate rose to 1.3 % from 1.0 % the month before. On a not seasonally adjusted basis for May, the year-ago increase for the headline PPI was up 5.3 % while the core was up 1.3 %. Despite some firming in the core, inflation at the producer level remains subdued.

Barclays 6/16 - Weakness in the headline measure reflected a 1.5% drop in energy prices and a 0.6% decline in food prices. The former was driven by a 7.0% drop in gasoline and the latter by a sharp 18.0% decline in vegetable prices (which have been very volatile in recent months). Outside of vegetable prices, most food components rose, which suggests that pipeline food price pressures continue to build. We expect this to feed through to the CPI in the coming months. Within the core PPI, price increases were fairly broad based, although the upside surprise, relative to our forecast, largely reflected strength in light motor trucks (0.8%) and tobacco products (2.2%). Looking further back on the production line, core intermediate goods prices rose 0.3%, but core crude goods fell 1.6%, reversing a small amount of the very strong gains in recent months. All in all, recent PPI data continue to suggest that pipeline price pressures are gradually building across most sectors. While this is unlikely to feed through to CPI inflation one-for-one in the near term, it does limit the chances of sustained disinflation at the consumer level, in our view.

Broad based gain in US manufacturing output

Barclays 6/16 - Industrial production rose 1.2% in May, above our (0.7%) and the consensus (0.9%) forecast. A small upward revision to March offset a small downward revision to April. The core manufacturing component rose 0.9%. Strength was broad based. Output of durable goods rose 1.7%, with strong gains in autos (5.5%), machinery (2.0%) and computer and electronics (1.4%). Nondurable output was flat on the month, depressed by a 2.2% drop in the petroleum component. Categorized by market group, there were 1%-plus gains in consumer goods, business equipment and business materials. All in all, today's report suggests continued momentum in the manufacturing recovery - growth in Q2 is tracking 8.9% q/q (saar), compared with 6.3% in Q1, supporting our view that GDP growth will accelerate in Q2 relative to Q1.

Empire State manufacturing index improves in June

Barclays 6/15 - The Empire State manufacturing index increased to 19.57 in June from 19.11 in May, a bit below our (21.0) and consensus (20.0) forecasts. The details also generally signaled improvement, with the new orders index rising to 17.53 from 14.30 and shipments jumping to 19.67 from 11.29. The employment index was a bit of a weak spot, falling to 12.35 from 22.37, but this follows two readings above 20, so the underlying trend of this component remains positive. The workweek index rose to 8.64 from 0.00, and the index of supplier delivery times, a leading indicator, jumped to a six-year high of 9.88 from -6.58. The index of unfilled orders improved to -1.23 from -7.89, while the inventories index slipped to -1.23 from 1.32. On the inflation front, the prices paid index dropped to 27.16 from 44.74, and prices received edged lower to 4.94 from 5.26. Despite a slightly softer headline print than was expected, this was a generally positive report, consistent with continued strength in the manufacturing sector.

US import prices decline as energy prices fall

Barclays 6/15 - Import prices for May declined 0.6% after a 1.1% rise in April (revised from 0.9%). This was above our (-1.0%) and consensus (-1.2%) forecasts. Excluding petroleum, import prices rose 0.5%, above our forecast of a 0.2% increase. The softness in the headline reading was driven by a 5.0% drop in petroleum prices and a 2.2% decrease in prices for industrial supplies; the latter was also dragged down by declining energy prices, as industrial supplies excluding fuels actually rose 1.9% in May. The rise in ex-petroleum prices was also driven by a 1.4% in foods and beverage prices and a 0.2% increase in capital goods prices. Today's report suggests that import prices will be putting some upward pressure on the core components for the PPI and CPI indices in coming months.

US jobless claims softer than expected

Barclays 6/17 - Initial jobless claims rose to 472k in the week of June 12 from an upwardly revised 460k in the week prior (last: 456k). This was above our (445k) and consensus (450k) expectations. Today's report leaves the four-week moving average unchanged at 464k. Continuing claims increased 88k, to 4.571mn, partly reversing the 234k decline in the previous week, but still below the recent trend. The insured unemployment rate ticked higher to 3.6%, above last week's reading of 3.5% but similar to levels seen in the past three months. Despite the pickup in private hiring and a drop in the unemployment rate in the May employment report, the past few weeks of data in claims have been disappointing. We look to the June employment report to bring more clarity regarding the pace of recovery in the labor market.

Press Release 6/18 - In the week ending June 12, the advance figure for seasonally adjusted **initial claims** was 472,000, an increase of 12,000 from the previous week's revised figure of 460,000. The 4-week moving average was 463,500, a decrease of 500 from the previous week's revised average of 464,000.

WEEK ENDING	June 12	June 5	Change	May 29	Prior Year
Initial Claims (SA)	472,000	460,000	+12,000	459,000	604,000
4-Wk Moving Average (SA)	463,500	464,000	-500	460,500	607,000

The Economic Week Ahead: June 21-25

Vanguard 6/18 - A revised first-quarter report on gross domestic product (GDP)—a leading indicator on the overall health of the nation's economy—will be released next Friday. Other news will include the latest on existing-home sales (Tuesday), new-home sales and FOMC monetary policy (both on Wednesday), and durable goods (Thursday).

Date	ET	Release	For	Consensus	Prior
Jun 22	10:00	Existing Home Sales	May	6.10M	5.77M
Jun 22	10:00	FHFA Housing Price Index	Apr	NA	0.3%
Jun 23	10:00	New Home Sales	May	480K	504K
Jun 23	14:15	FOMC Rate Decision	Jun 23	0.25%	0.25%
Jun 24	08:30	Durable Orders	May	-1.4%	2.8%
Jun 24	08:30	Initial Claims	06/19	NA	472K
Jun 24	08:30	Continuing Claims	06/19	NA	4571K
Jun 25	08:30	GDP - Third Estimate	Q1	3.0	3.0