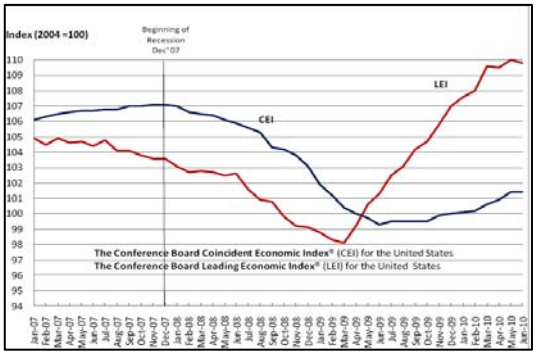
Market Comment *Economic Highlights for the week ended July 23, 2010*

Economic Week in Review: At the moment, we have movement

Vanguard 7/23 – The speed might resemble that of rush hour traffic, but the economy is still moving. If a breakdown occurs, Federal Reserve Chairman Ben Bernanke said the Fed would take further measures. The news was mostly negative this week, but the long-term recovery still appears to be on course. Both existing-home sales and housing starts were down, mostly because of April's expiration of the federal homebuyer tax credit. The Conference Board's index of leading indicators also fell. For the week, the S&P 500 Index rose 3.5% to 1,103 (for a year-to-date total return—including price change plus dividends—of about –0.1%).

US leading indicators slipped 0.2% in June



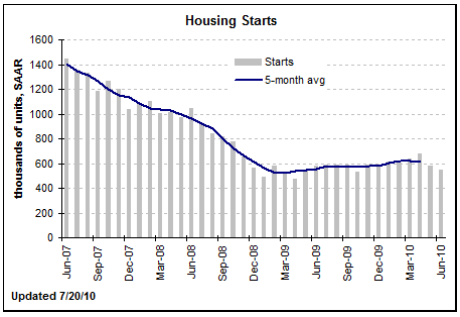
Barclays 7/22 - The index of leading indicators decreased 0.2% in June after a 0.5% gain in May, in line with our forecast but above that of the consensus (-0.3%). The biggest drags were decreases in the average workweek and pace of supplier deliveries, with continued stock market weakness and a slight increase in initial jobless claims also weighing on the index. The wide interest rate spread and an increase in the real money supply provided some offset, and the increase in building permits also contributed positively. Estimated consumer goods orders and nondefense capital goods orders were roughly unchanged and in line with our expectations, as were consumer expectations. The slowing in the leading index over the past few months suggests that the economy has downshifted from the rapid pace of expansion that characterized the early recovery. Nevertheless, the overall trend remains upward, indicating more modest growth, but giving no indication of a double-dip.

Federal Reserve Commentary: Bernanke signals no additional stimulus

Barclays 7/21 – (Excerpts) Federal Reserve Chairman Ben Bernanke's testimony to Congress was largely as we had expected and in line with the minutes of the June FOMC meeting. In particular, he highlighted that he still expected a moderate recovery and did not signal that additional stimulus from the Fed should be expected. As in the minutes, his testimony stated that the recovery is "proceeding at a moderate pace," but the softening data means the "economic outlook remains **unusually uncertain**." The chairman highlighted recent gains in private payrolls as encouraging and the strong growth in business spending on equipment and software as reflecting the need to rebuild inventories after the downturn. However, his testimony also stated that financial conditions had become less supportive of growth, based in part on reduced risk-taking activities amid sovereign debt fears in Europe. This, combined with generally tight conditions in the US banking system, was a factor in the slower growth outlook. Consequently, given the slower growth outlook and less supportive financial conditions, Chairman Bernanke said that the "progress in reducing the unemployment rate is now expected to be somewhat slower than previously projected."

Although he noted that the economic outlook remained uncertain and that the Fed remained "prepared to take further policy actions as needed to foster a return to full utilization of our nation's productive potential in a context of price stability," Chairman Bernanke's written testimony gave no new information on any additional stimulus policies that the Fed might use should the outlook worsen significantly. In fact, the testimony focused largely on the familiar set of exit strategies for withdrawing the extraordinarily accommodative policy at a measured pace and at the appropriate time. We take this to mean that, although the outlook has become more uncertain, the Fed has not changed its policy stance in favor of further accommodation.

Housing Starts



Econoday 7/20 - Housing is still suffering from the end of expired tax incentives as starts fell sharply in June. But the good news is that housing permits rebounded, perhaps indicating a bottom for starts. Homebuilders again slowed the pace of ground breaking as housing starts in June declined 5.0 % after a 14.9 % plunge in May. The June annualized pace of 0.549 million units fell well short of analysts' expectations for 0.580 million units and is down 5.8 % on a year-ago basis. The latest fall was primarily due to a 21.5 % plummet in multifamily starts, following a 4.3 % gain in May. The single-family component only slipped 0.7 % after an 18.8 % decrease the prior month.

By region, the decline in starts was led by an 11.3 % drop in the Northeast Census region. Decreases also were seen in other regions with the Midwest down 6.9 %; West, down 5.9 %; and the South, down 2.4 %.The near term outlook is less gloomy as permits rebounded 2.1 % in June, following a 5.9 % drop in May. Permits in June came in at an annualized rate of 0.586 million units and are down 2.3 % on a year-ago basis. Clearly, the starts and permit levels are weak. But June's starts numbers are not as bad as at face value as the multifamily component is very volatile and led the drop. And the comeback in permits suggests that the post-tax credits decline is leveling off.

Barclays 7/20 – (Excerpts) In contrast to starts, the increase in headline permits was driven by an increase in multi-family permits, which rose 19.6%, to 165,000 from 138,000 in May. Single-family permits were down 3.4%, to 421,000 from 436,000, and have registered three consecutive monthly declines. Overall, the report suggests that the housing market is trying to find a bottom after the expiration of the homebuyer tax credit. We continue to expect total housing starts to rebound in the second half of the year, albeit at a gradual pace.

Existing Home Sales

Econoday 7/22 - Existing home sales fell in June but not as much as expected, down 5.1 % to a 5.37 million annual rate. Prices are a big positive in the report, up 5.2 % for the median price to $183,700. Yet supply is a big negative, up to 8.9 months from 8.3 months. Heavy supply will hold back price improvement. The National Association of Realtors, which compiles the report, sees inventories rising to 10 months in the next report. The association stresses that the housing market will turn on the unemployment rate.

Barclays 7/22 – (Excerpts) Despite the decline in June, the level of existing home sales is still likely to reflect a boost from the first-time homebuyer tax credit. Since this measure of home sales tracks closed contracts, we expect the tax credit to continue to distort the headline reading until September of this year, when the deadline for closed contracts passes. Regionally, the Northeast saw a sharp jump in home sales of 7.9%, although this was offset by declines in the Midwest (-7.5%), South (-6.5%), and West (-9.3%). The resilience of home prices amid the post-tax credit decline in activity is an encouraging sign.

Housing Market Index

Econoday 7/19 - Home builders are reporting the weakest conditions since April last year. The housing market index fell to 14 in July, down two points from June, which is revised one point lower, and down eight points from its recovery high of 22 in May. The traffic component, down three points to 10, is the weakest since March last year. The end of second-round stimulus has created a mid-year wasteland for the housing sector. Homebuilders continue to report tight credit conditions and competition from foreclosures and distressed sales.

Barclays 7/19 - Today's report was discouraging and represents a further dip in homebuilder sentiment after the expiration of the homebuyer tax credit in April. However, the two-point drop in the headline index in July was smaller than the six-point drop in June, suggesting the decline in sentiment may be nearing an end. Smoothing through the volatility from the stimulus measures, homebuilder sentiment has continued to move sideways for much of the last year.

Stabilization in US house prices

Barclays 7/22 - The FHFA house price index, which tracks repeat sales, rose 0.5% in May, close to our forecast (0.4%) but well above the consensus (-0.3%). April's gain was revised up a tenth, to 0.9%. The y/y% rate improved to -1.2% from -1.4%. This measure of house prices has now risen for three consecutive months and stands consistent with our view that national home prices have stabilized and are moving broadly sideways in y/y terms. We expect this to continue for some time, with an improving economic backdrop likely to limit sharp price declines, but the significant foreclosure pipeline likely to limit broad-based price gains.

Jobless Claims

Press Release 7/22 - In the week ending July 17, the advance figure for seasonally adjusted initial claims was 464,000, an increase of 37,000 from the previous week's revised figure of 427,000. The 4-week moving average was 456,000, an increase of 1,250 from the previous week's revised average of 454,750.

Econoday 7/22 – (Excerpts) Continuing claims fell 223,000 in data for the July 10 week. The four-week average for this reading shows only marginal improvement from a month ago: at 4.567 million vs 4.573 million in the June 19 week. The

unemployment rate for insured workers fell two tenths in the week to 3.5 %. Weekly initial claims data will be distorted through the month of July, beginning with the opening holiday and in following weeks on calendar shifts for retooling in the manufacturing sector. Nevertheless, today's report isn't very good.

Barclays 7/22 – (Excerpts) We think the increase is partly attributable to the cancellation of its usual two-week summer shutdown by GM, which resulted in lower-than-expected jobless claims last week and likely pushed the number higher this week. The Labor department also said that the volatility of the past two weeks can be explained by the July 4 holiday, leading to a lower number of claims filed last week and a bounce back in filings this week.

Unemployment Insurance Weekly Claims Report

WEEK ENDING	July 17	July 10	Change	July 3	Prior Year
Initial Claims	**464,000**	**427,000**	**+37,000**	**458,000**	564,000
4-Wk Moving Average	456,000	454,750	+1,250	467,000	569,250

Economic Week Ahead

Vanguard 7/23 – Economists will have an assortment of data to decipher next week. Friday brings reports on gross domestic product (GDP) and the employment cost index. The news begins Monday with new-home sales and continues Tuesday with consumer confidence. The Federal Reserve's Beige Book release on economic conditions across the United States is scheduled for Wednesday along with data on durable goods.

Week of July 26 - July 30

Date	ET	Release	For	Consensus	Prior
Jul 26	10:00	New Home Sales	Jun	338K	300K
Jul 27	09:00	Case-Shiller 20-city Index	May	NA	3.81%
Jul 27	10:00	Consumer Confidence	Jul	51.5	52.9
Jul 28	08:30	Durable Orders	Jun	1.25%	-0.6%
Jul 28	08:30	Durable Orders ex Transportation	Jun	NA	1.6%
Jul 29	08:30	Initial Claims	07/24	NA	464K
Jul 29	08:30	Continuing Claims	07/17	NA	4487K
Jul 30	08:30	GDP-Adv.	Q2	NA	2.7%

FFCB Weekly Debt Issuance Activity

Week Ended Date	Discount Notes $million	New Bonds $millions	Issue Count	Called Bonds Par $millions	Issue Count
25-Jun	8,840	3,530	35	2,001	26
2-Jul	9,945	831	12	862	10
9-Jul	6,030	1,812	13	220	4
16-Jul	8,297	3,766	21	1,694	17
23-Jul	10,145	2,690	20	1,414	9