

Market Comment *Economic Highlights for the week ended August 26, 2011*

Economic Week in Review: Headwinds Blow As Fed Says No—For Now

Vanguard 8/26 – The march to extreme caution quickened its pace this week led by more disappointing news for the fragile economy. Key reports on housing, new orders, and national output (GDP) indicate that the economy, still buffeted by slow growth and persistent joblessness, remains far from reaching a sustained recovery. Amid this discouraging environment, Federal Reserve Chairman Ben Bernanke—in widely anticipated comments on Friday from Jackson Hole, Wyoming—said the central bank stands ready to help dig the economy out of the doldrums but didn't indicate what tools he would use to do so. For the week ended August 26, the S&P 500 Index rose 4.7% to 1,176.80 (for a year-to-date total return of about -5.2%). The yield on the 10-year U.S. Treasury note increased 12 basis points to 2.19% (for a year-to-date decline of 111 bps).

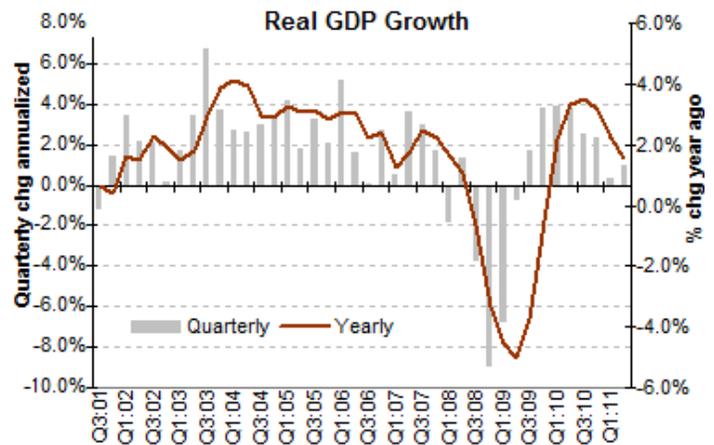
2nd-Quarter GDP Up Only 1%

Vanguard 8/26 – Real gross domestic product (GDP)—perhaps the country's most significant leading economic indicator—increased at a paltry 1.0% annualized rate for the second quarter, a revision from the previous low estimate of 1.3%. Although the latest figure exceeded the first quarter's rate of 0.4%, the latest GDP reading is yet another sign that the economy is continuing to stall amid reduced consumer spending, weak exports, and a smaller buildup of inventories. The core inflation rate, which excludes volatile food and energy prices, rose 2.1% from the first quarter.

Econoday 8/26 – The economy got a downgrade for the second quarter. The Commerce Department's second estimate for second quarter GDP growth was nudged down to a modest gain of 1.0% annualized, compared to first quarter growth of 0.4%. On a year-ago basis, GDP is up 1.5% in the second quarter, compared to 2.2% the previous quarter. Economy-wide inflation was revised up marginally to 2.4% annualized.

Barclays 8/26 - Finally, the first look at the corporate accounts painted a fairly upbeat picture for the business sector, with profits up 3.0% q/q. Profits have now risen for 10 consecutive quarters since the middle of the recession in 2008. While this has led to a

healthy rebound in business investment, for the recovery to become sustainable the relatively strong position of the corporate sector needs to be translated into consistent strong gains in employment, something that has clearly yet to materialize. All in all, while Q2 was unmistakably very soft, the foundations for a rebound in Q3 now look more encouraging.



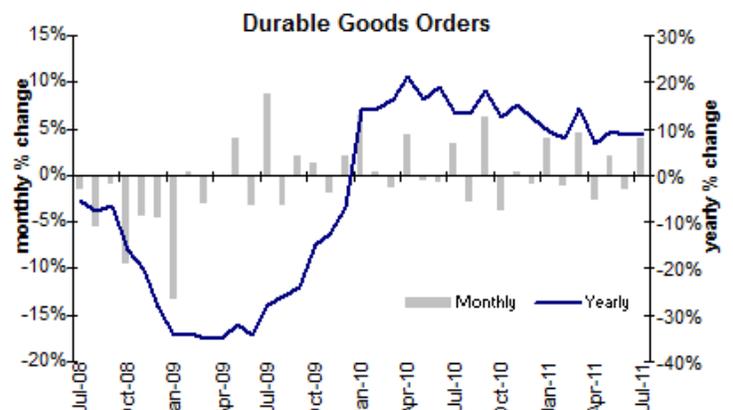
Durable Goods Orders – July: Rebound In US Durable Goods Orders, But Weak Core

Vanguard 8/26 – Orders for long-lasting factory goods jumped 4.0% in July, spurred primarily by increased demand for cars and commercial aircraft. Analysts said the 11.5% increase in car orders indicates an improvement in the supply chain, disrupted for much of the year by the earthquake and tsunami in Japan.

However, orders for non-defense capital goods excluding aircraft—widely considered a key gauge of capital spending—fell 1.5%. Analysts believe the drop reflected a continued shaky outlook for jobs and economic growth.

Econoday 8/24 - A monthly surge in new orders for motor vehicles & parts, the best in eight years, headlines a strong durable goods report for July. Excluding transportation, new orders rose a solid 0.7%.

Barclays 8/24 - The upside surprise was wholly centered in the volatile components, with gains in vehicles (11.5%) and non-defense aircraft (43.4%).



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Core capital goods orders came in weaker, falling 1.5%, with declines in computers and electronics, machinery and fabricated metals.

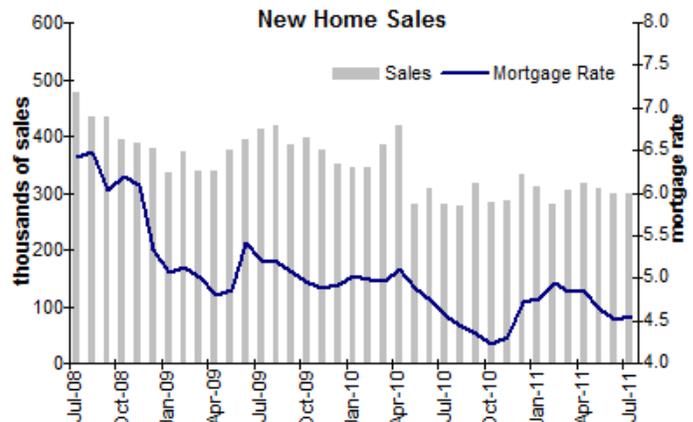
New-Home Sales Down Again – July; Inventories Remain At Record Lows

Vanguard 8/26 – Sales of new homes dropped to a 5-month low, yet another sign that ample inventory and record-low interest rates haven't been enough to jump-start the housing business. New-home sales fell 0.7% to an annualized 298,000 in July, as jittery shoppers are either reluctant to buy new homes or opting for foreclosed properties at bargain rates. June's numbers also were revised downward almost 4%.

Barclays 8/23 –The inventory of new homes for sale also fell, to 165,000, the lowest level in the history of the series dating back to January 1963, and months' supply remained unchanged at 6.6 months. Therefore, even as the level of inventory continues to register historical lows, the tepid pace of sales is keeping inventory elevated in terms of months' supply. We see homebuilders as continuing in wait-and-see mode until inventory levels shrink further.

Econoday 8/23 - The average price for a new home was little changed at \$272,300.

The outlook for the new home market and for home builders remains very difficult. Low interest rates may be a big plus but are being more than offset by heavy supply of low priced existing homes, by appraisal uncertainties, and by continuing tightness in the credit market.



FHFA Home Price Index: US FHFA Home Prices Surprise, Rise 0.9% M/M in June

Barclays 8/24 - The FHFA Purchase-Only House Price Index rose 0.9% m/m in June, following the 0.9% increase in May. The increase leaves the y/y decline at 4.2%, versus 6.2% a month earlier. The index had recorded ten straight monthly declines through March of this year, but has now risen in each of the past three months, suggesting that the recent weakness in home prices continues to abate. Looking at the geographic breakdown, seven of the nine regions posted gains.

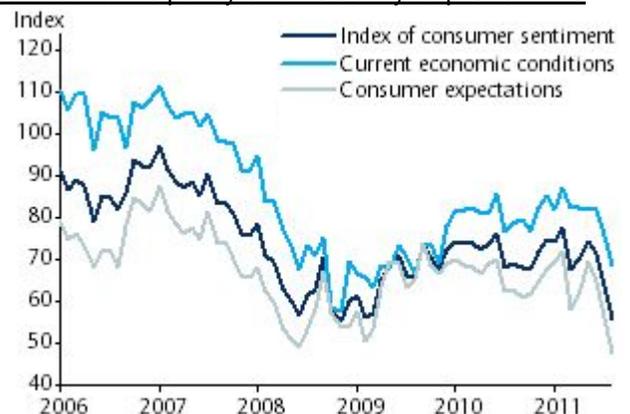


Consumer Sentiment – August: Consumer sentiment remains at depressed levels

Barclays 8/26 - Consumer expectations and their assessment of current conditions were both notably down relative to July. Expectations were revised slightly higher to 47.4, whereas current conditions were revised lower to 68.7. The University of Michigan cited concern over government economic policy and its ability to prevent the economy from entering another recession as a key factor weighing on sentiment. Overall, two-thirds of respondents indicated they viewed the economy as having recently deteriorated and about 74% reported the expected "bad times" ahead, apparently driven by concerns over the labor market. Consequently, consumer buying plans for large-ticket items have been scaled back and are in line with recessionary lows.

Overall, the report continues to raise concerns about the outlook for the consumer, but as we have previously discussed, what consumers say and how they behave do not always align.

Econoday 8/26 – Just up from completely depressed is a fair way to describe consumer sentiment which bounced up from the bottom but only slightly in the last half of the



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month. The full-month sentiment index is 55.7. A look back shows a 55 reading in November 2008 just after the Lehman-led bank meltdown.

The leading component, expectations, rose to 47.4. To find readings lower than this we have to go back to the Iranian hostage and oil crisis of the early 80s. The assessment of current conditions actually weakened further, to a final 68.7. These levels were seen in late 2008 and early 2009.

This report doesn't point to any burst in confidence following resolution of the debt-ceiling drama at the beginning of the month. Weak job growth and now volatility in the financial markets are keeping spirits down.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – Week of Aug 20

Press Release 8/25 (excerpts) – In the week ending August 20, the advance figure for seasonally adjusted initial claims was 417,000, an increase of 5,000 from the previous week. The 4-week moving average was 407,500, an increase of 4,000.

The advance seasonally adjusted insured unemployment rate was 2.9% for the week ending August 13, a 0.1 percentage point decrease from the prior week.

The advance number for seasonally adjusted insured unemployment during the week ending August 13 was 3,641,000, a decrease of 80,000. The 4-week moving average was 3,701,000, a decrease of 19,500.

WEEK ENDING	Aug 20	Aug 13	Change	Aug 6	Prior Year
Initial Claims (SA)	417,000	412,000	+5,000	399,000	469,000
4-Wk Moving Average (SA)	407,500	403,500	+4,000	406,000	477,250

Barclays 8/25 - The Labor Department reported that the labor dispute between Communication Workers of America and Verizon Communications was a special factor pushing claims higher in recent weeks, leading to the filing of 12,500 initial claims in the week ending August 13 and 8,500 claims in the week ending August 20. In other words, the labor dispute at Verizon Communications appears to account for most of the recent rise in initial jobless claims.

Econoday 8/25 - The four-week average ended its seven-week run of declines, rising 4,000 to a 407,500 level that shows a 7,000 improvement from the month-ago comparison.

Chairman Bernanke At Jackson Hole: No New Policies Now, A Fuller Discussion In September

Barclays 8/26 - The chairman refrained from making any concrete policy announcements in his speech this morning in Jackson Hole, Wyoming. He said that the expectation of the FOMC is for a moderate recovery that gradually strengthens over time. However, in light of recent developments, the FOMC had marked down its outlook for the likely pace of growth "over coming quarters," which was behind the decision at the August FOMC meeting to provide more specific forward guidance about its expected path for the federal funds rate. Looking ahead, the Chairman simply said that "the Federal Reserve has a range of tools that could be used to provide additional monetary stimulus" and the FOMC will "continue to consider those and other pertinent issues...at our meeting in September." The chairman declined to provide a list of potential policy options, but did say that the meeting in September would be scheduled for two days (the 20th and 21st) instead of a one-day meeting as previously scheduled, "to allow a fuller discussion." We see the committee as carefully examining incoming data during the intermeeting period as it assesses the relative merits of further policy actions.

Beyond the immediate and potential stance of monetary policy, the chairman said that the committee expects that inflation will "settle, over coming quarters, at levels" consistent with the Fed's dual mandate. The chairman remained optimistic on the long-term growth prospects in the US, saying that the growth fundamentals of the US economy did not appear to be permanently altered by the severe financial crisis experienced in recent years. He did note, however, that financial stress continues to be a significant drag on the recovery "here and abroad" as "sharp bouts of volatility and risk aversion" are likely to reflect heightened uncertainty and fragile business and consumer confidence.

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The Economic Week Ahead: Aug 29 – Sept 2, 2010

Vanguard 8/26 – It'll be a busy week of facts and figures to digest, beginning with personal income on Monday, followed by Tuesday's report on consumer confidence as well as anxiously awaited minutes from the Federal Open Market Committee. Factory orders are due out Wednesday, and a busy Thursday brings reports on productivity and costs, construction spending, and the ISM manufacturing index. The week will wrap up Friday with a report on the employment situation.

This Week's U.S. Economic Calendar

Source: MarketWatch

	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
MONDAY, AUG. 29	8:30 am	Personal income	July	0.3%	0.1%
	8:30 am	Consumer spending	July	0.5%	-0.2%
	8:30 am	Core PCE price index	July	0.2%	0.1%
TUESDAY, AUG. 30	9 am	Case-Shiller home prices	June	--	1.0%
	10 am	Consumer confidence	Aug.	53.0	59.5
	2 pm	FOMC minutes	8/9	--	--
WEDNESDAY, AUG. 31	8:15 am	ADP employment	Aug.	--	114,000
	10 am	Chicago PMI	Aug.	57.0%	58.8%
	10 am	Factory orders	July	0.8%	-0.8%
THURSDAY, SEPT. 1	8:30 am	Jobless claims	8/27	N/A	N/A
	8:30 am	Productivity	2Q	-0.5%	-0.3%
	8:30 am	Unit labor costs	2Q	2.7%	2.2%
	10 am	ISM	Aug.	49.5%	50.9%
	10 am	Construction spending	July	0.2%	0.2%
FRIDAY, SEPT. 2	8:30 am	Nonfarm payrolls	Aug.	110,000	117,000
	8:30 am	Unemployment rate	Aug.	9.1%	9.1%
	8:30 am	Average hourly earnings	Aug.	0.1%	0.4%