

Market Comment *Economic Highlights for the week ended October 28, 2011*

Economic Week in Review: A Turn for the Better?

Vanguard 10/28 - Signs of progress on Europe's sovereign debt crisis and solid, but unspectacular, GDP growth in the United States sounded hopeful notes in a week of otherwise mixed signals. The S&P 500 Index rose 3.8% to 1,285 (for a year-to-date total return of about 3.9%). The yield on the 10-year U.S. Treasury note increased 11 basis points to 2.34% (for a year-to-date decrease of 96 basis points).

Gross Domestic Product, 3rd Quarter 2011 (Advance Estimate)

Press Release 10/27 - Real gross domestic product -- the output of goods and services produced by labor and property located in the United States -- increased at an annual rate of 2.5% in the third quarter of 2011 (that is, from the second quarter to the third quarter) according to the "advance" estimate released by the Bureau of Economic Analysis. In the second quarter, real GDP increased 1.3%.

The Bureau emphasized that the third-quarter advance estimate released today is based on source data that are incomplete or subject to further revision by the source agency (see the box on page 3). The "second" estimate for the third quarter, based on more complete data, will be released on November 22, 2011.

The increase in real GDP in the third quarter primarily reflected positive contributions from personal consumption expenditures (PCE), non-residential fixed investment, exports, and federal government spending that were partly offset by negative contributions from private inventory investment and state and local government spending. Imports, which are a subtraction in the calculation of GDP, increased.

The acceleration in real GDP in the third quarter primarily reflected accelerations in PCE and in non-residential fixed investment and a smaller decrease in state and local government spending that were partly offset by a larger decrease in private inventory investment.

Vanguard 10/28 - GDP's solid, but not robust, growth seemed to have dispelled fears of another recession. Moreover, final sales—an indicator of the strength of domestic demand based on GDP minus inventories—rose at a 3.6% annualized rate, faster than in the previous two quarters. However, that pace was too slow to make a major dent in unemployment, analysts said.

Econoday 10/27 – Today's report is good news, showing that economic momentum has picked up a bit. The component mix is particularly encouraging as final sales have picked up. Strength was led by business fixed investment with personal consumption expenditures gaining momentum also. On a year-ago basis, GDP is up 1.6%, matching the pace in the second quarter.

Economy-wide inflation according to the GDP price index held steady at a 2.5% pace and equaled consensus forecasts for a 2.5% boost.

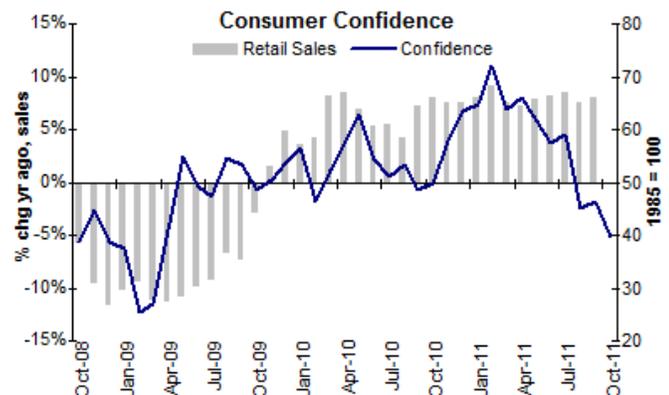
Consumer Confidence – October: Consumer Confidence Falls to Recession's Level

Vanguard 10/28 - Consumer confidence fell in October to the lowest level since March 2009, during the recent recession. The Conference Board's index of consumer confidence fell to 39.8, rather than remaining flat as expected, bringing the three-month slide to 20 points. Especially worrisome to consumers were their assessment of business conditions and their income expectations. There was, however, a slight decrease—a good sign—in the "jobs hard to get" category.

Econoday 10/25 – Today's report shows surprising weakness with the index reading of 39.8. The current conditions component was down a sharp seven points to 26.3 and the expectations component was reported down 6.4 points to 48.7.

And what is not a good sign for holiday spending, stand-out weakness also appears in income expectations where fewer, 10.3%, see their income rising and more, 19.2%, see their income decreasing. This inversion in income with pessimists on top is very rare for this series.

One good piece of news is a dip back, to 47.1%, in those who say jobs are currently hard to get in what is a mildly positive indication for the October jobs report. Inflation expectations are unchanged at 5.8%.



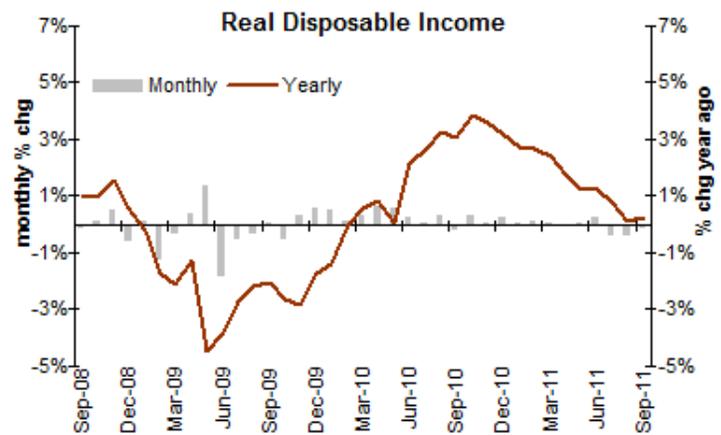
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Personal Income and Outlays – September: Consumers Spending More Even As They Earn Less

Vanguard 10/28 - Consumer spending was unexpectedly strong in September. Consumption rose 0.6% while personal income edged higher by only 0.1%. Personal savings in September declined to an annualized rate of 3.6%, the lowest reading since 2007 and the third straight monthly decline from June's 5.3% rate. Some details: spending growth (which has averaged 0.6% over the past three months) was led by purchases of durable goods, including a rebound in auto sales. Healthy growth in the wages and salaries component of personal income was offset by lower interest income and flat government benefits.

Econoday 10/28 –Turning to inflation numbers, the headline PCE price index increased 0.2% after gaining 0.3% in August. The core rate slowed to no change from up 0.2% in August.

Year-on-year, headline prices are up 2.9%, compared to 2.9% in September. The core is up 1.6% on a year-ago basis, down slightly from 1.7% in August.



Durable Goods Orders – September: Better Than You Might Think

Vanguard 10/28 - New orders for durable manufactured goods declined 0.8% in September—yet analysts viewed the report as reassuring. The reasons: When the (expected) steep decline in volatile aircraft orders is excluded, durable goods orders rose 1.7%. And orders for nondefense goods excluding aircraft—an indicator of business spending strength—rose 2.4%.

Econoday 10/26 – The only major industry category to decline in September was transportation which dropped 7.5% after rising 0.6% in August. Weakness was primarily in aircraft with defense down 33.9% and nondefense down 25.5%. Some of the weakness in transportation was in autos, which is baffling, given recently healthy sales. Motor vehicles dipped 2.7% after a 9.1% drop in August.

Outside of transportation, orders were healthy across the board. Increases were seen in primary metals, up 2.6%; fabricated metals, up 1.9%; machinery, up 1.8%; computers & electronics, up 1.0%; electrical equipment, up 1.9%; and "other," up 1.0%.

Overall, durables orders point to continued gains in manufacturing. Hard data are running stronger than surveys and anecdotes.

New Home Sales – September: New-Home Sales Show Surprising Strength

Econoday 10/26 – Sales of new homes are coming at the expense of price. New home sales jumped 5.7% in September to a 313,000 annual rate. The gain is centered in the two largest regions, the South and the West. The rise in sales drew down supply to 6.2 months at the current sales rate for the leanest level in a year-and-a-half and vs 6.6 months in August.

Price contraction is tangible in this report. The median price of \$204,400 is down 3.1% in the month for the third straight monthly decline. Year-on-year contraction of 10.4% is the steepest since the recession days of early 2009. The average price of \$243,900 is down 3.9%, which is also the third straight decline. Year-on-year contraction is 9.9% and is also the steepest since the recession.

The level of sales in this report is positive but other data on the housing sector, including last week's existing home sales report, point to a sector that continues to struggle at lows.

Case-Shiller Home Prices - August

Econoday 10/25 – Home prices, at best, may be stabilizing according to Case-Shiller data that show no change in the adjusted composite-20 index for August. The reading ends three prior months of 0.1% declines (July revised downward from no change). The unadjusted reading, at a very weak plus 0.2% vs. plus 0.9% and plus 1.1% in the two prior months, points to price contraction in August given that monthly readings in this report are

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three-month averages. Nevertheless, the unadjusted year-on-year pace of minus 3.8% is the best reading since February in what hints at a flattening in the slope of price contraction.

FHFA Home Prices - August

Econoday 10/25 – According to the FHFA, house prices slipped 0.1% in August after edging up 0.1% the prior month (originally up 0.8%). The August dip ended a string of four monthly gains in a row. The FHFA house price index covers mortgages financed by or bundled by federal housing agencies. On a year-on-year basis, the FHFA HPI is down 4.0%, compared to down 4.1% in July.

Pending Home Sales - September

Econoday 10/27 – Contract signings are very weak in the existing home sales market which points to further troubles for the housing and construction sectors. Pending sales fell 4.6% in September with declines split about evenly across regions. September's decline is unusually steep, following declines of 1.2% in August and 1.3% in July. The text of the report is downbeat saying a combination of weak consumer confidence together with tight credit conditions are holding back home buyers. Credit issues along with the inability of contract signers to sell their own homes have been leading to high cancellations and holding down closings, a special factor that points to additional trouble for the next existing home sales report.

Employment Cost Index – 3 Qtr 2011: Growth in Employee Compensation Slows

Vanguard 10/28 - The wages, salaries, and benefits paid to civilian employees grew 0.3% in the third quarter, half the expected pace and less than half the increase of the prior quarter. Wages and salaries (about 70% of compensation) increased 0.3% in September while benefits (30%) were virtually unchanged. Analysts said that the results reflected the continued soft labor market, which was particularly difficult for state and local government employees, who have been facing payroll cuts. On a year-ago basis, compensation grew by 2.0%, which also represented a slowdown compared with the 12-month results for prior quarters.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week of Oct 22

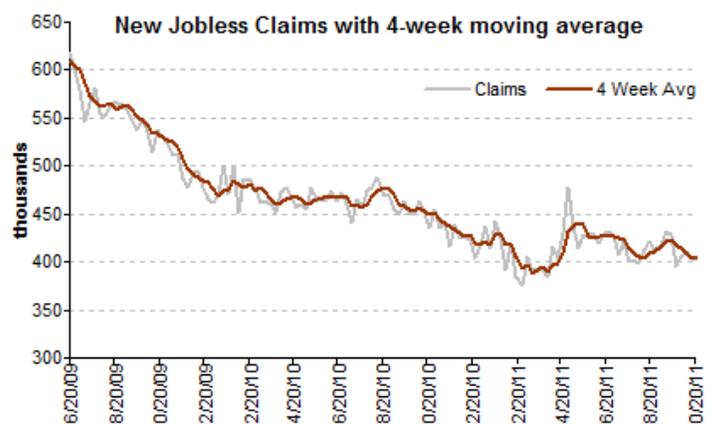
Press Release 10/27 (excerpts) - In the week ending October 22, the advance figure for seasonally adjusted **initial claims** was 402,000, a decrease of 2,000 from the previous week's revised figure of 404,000. The 4-week moving average was 405,500, an increase of 1,750 from the previous week's revised average of 403,750.

The advance seasonally adjusted **insured unemployment rate** was 2.9% for the week ending October 15, a decrease of 0.1percentage point from the prior week's revised rate of 3.0%.

WEEK ENDING	Oct 22	Oct 15	Change	Oct 8	Prior Year
Initial Claims (SA)	402,000	404,000	-2,000	409,000	435,000
4-Wk Moving Average (SA)	405,500	403,750	+1,750	409,250	449,750

The advance number for seasonally adjusted **insured unemployment** during the week ending October 15 was 3,645,000, a decrease of 96,000 from the preceding week's revised level of 3,741,000. The 4-week moving average was 3,701,000, a decrease of 26,750 from the preceding week's revised average of 3,727,750.

Econoday 10/27 – Initial jobless claims are holding steady in a narrow range just above 400,000. Continuing claims in data for the October 15 fell 96,000 to 3.645 million with the four-week average of 3.701 million nearly 50,000 lower on the month-ago comparison. Improvement for continuing claims is an uncertain mix between hiring and benefit expiration. The unemployment rate for insured workers dipped one tenth to 2.9%. There are no special factors in today's data.



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Consumer Sentiment - October

Econoday 10/28 – The Reuters/University of Michigan's consumer sentiment index fell 1.9 points at the mid-month October reading to 57.5, extending recently sharp weakness going back to the August shock month when equities plunged. Weakness was centered once again in the leading component of expectations which at 47.0, was down 2.4 points from September's final reading. The assessment of current conditions also declined, down 1.1 points to a 73.8 level that continues to show less severe weakness than expectations.

The Economic Week Ahead: Oct 31– Nov 4, 2010

Vanguard 10/28 - The Federal Open Market Committee holds a regular meeting on Wednesday, with economic-growth strategies likely high on the agenda. Other upcoming reports include construction spending and the manufacturing index produced by the Institute for Supply Management (ISM) on Monday; productivity, factory orders, and ISM's non-manufacturing index on Thursday; and the unemployment rate and nonfarm payrolls on Friday.

This Week's U.S. Economic Calendar

Source: MarketWatch

	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
MONDAY, OCT. 31	9:45 am	Chicago PMI	Oct.	58.0%	60.4%
TUESDAY, NOV. 1	10 am	ISM Manufacturing Index	Oct.	52.2%	51.6%
	10 am	Construction Spending	Sept.	-0.1%	1.4%
WEDNESDAY, NOV. 2	8:15 am	ADP Employment	Oct.	--	91,000
	12:30 pm	FOMC Announcement		--	--
	2:15 pm	Bernanke Press Conference		--	--
THURSDAY, NOV. 3	8:30 am	Initial Jobless Claims	10-29	N/A	402,000
	8:30 am	(Labor) Productivity	3Q	4.0%	-0.7%
	8:30 am	Unit Labor Costs	3Q	-1.0%	3.3%
	10 am	ISM Services Index	Oct.	53.6%	53.0%
	10 am	Factory Orders	Sept.	-1.0%	2.1%
FRIDAY, NOV. 4	8:30 am	Nonfarm Payrolls	Oct.	95,000	103,000
	8:30 am	Unemployment Rate	Oct.	9.1%	9.1%
	8:30 am	Average Hourly Earnings	Oct.	0.2%	0.2%