

Market Comment *Economic Highlights for the week ended November 18, 2011*

Economic Week in Review: Hopeful Signs Emerge

Vanguard 11/18 - After sputtering for months, the U.S. economy began to show some hopeful signs. Industrial output, retail sales, and a gauge of potential future economic activity all climbed substantially in October from September, while also significantly exceeding analysts' expectations. Consumer and producer prices declined. For the week ended November 18, the S&P 500 Index fell 3.8% to 1,215.65 (for a year-to-date total return of about -1.6%). The yield on the 10-year U.S. Treasury note fell 3 basis points to 2.01% (for a year-to-date drop of 129 basis points).

AFP 11/21 - Two price reports released last week by the Bureau of Labor Statistics had prices taking a step backwards in October. Also declining were first-time claims for unemployment insurance benefits, which fell to a seven-month low. Meanwhile, retail sales and manufacturing output picked up some momentum in October. Even housing data released last week could be interpreted as being positive. This all adds up to a picture of the U.S. economy appearing to have starved off a much feared recession...at least for now.

U.S. Retail Sales - October: Strong Start to Q4

Vanguard 11/18 - Retail sales climbed 0.5% in October, beating analysts' expectations. Sales for electronics and building supplies led the way as sales numbers rose for the 5th consecutive month.

On the downside, drops in sales for clothing, gasoline, and furniture served to restrain overall growth.

Barclays 11/15 - The upside surprise relative to our forecast was centered on the core (which strips out the volatile vehicles, gasoline and building materials components), which rose 0.6%, the strongest since March and well above our 0.2% forecast. In turn, this reflected fairly broad-based strength, with gains in electronics (3.7%), non-store sales (1.5%), sporting goods (1.3%) and food and beverages (1.1%). With consumer price inflation likely to have eased in October relative to Q3, the strength in nominal sales should translate into strong real consumer spending growth as well.

AFP 11/21 - Retail sales increased 7.2% over the past year, with at least some of the gain being funded by a recent decline in the savings rate.

Econoday 11/15 - Today's retail sales report shows a consumer much more willing to spend than sentiment surveys suggest.

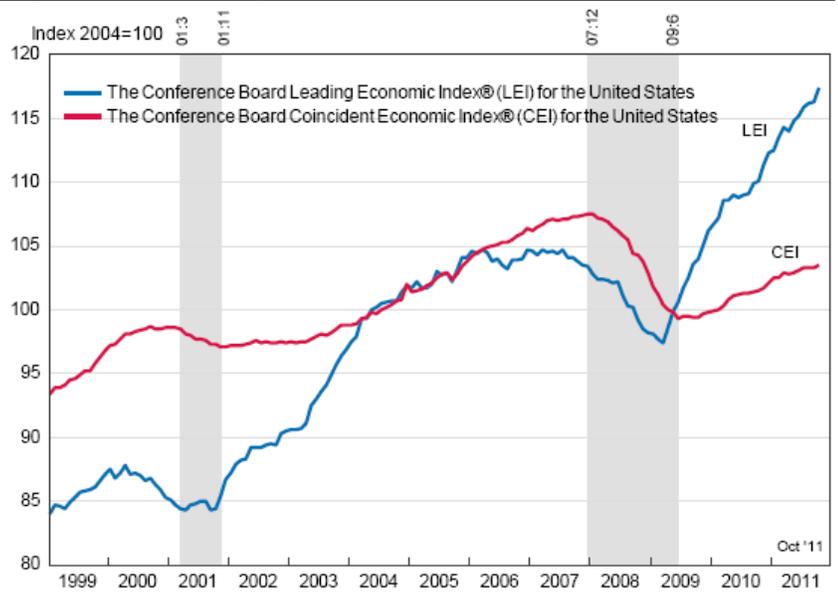
Leading Economic Indicators Rise - October

Vanguard 11/18 - The Conference Board's Leading Economic Index (LEI) increased 0.9% in October, bettering analysts' expectations. The gain was significantly better than September's 0.1% increase.

The Conference Board attributed the upturn to a surge in housing permits, and suggested that it represents a lowered chance of a "double dip" recession. Improving consumer sentiment, job growth, and market movement, as well as a solid interest rate spread, were also cited as contributing factors.

"The LEI is pointing to continued growth this winter, possibly even gaining a little momentum by spring. The lack of confidence has been the biggest obstacle in generating forward momentum, domestically or globally. As long as it lasts, there is a glimmer of hope," Conference Board economist Ken Goldstein said.

The Conference Board Leading Economic Index® (LEI) for the U.S. Increases in October



Latest LEI Trough March 2009, Latest CEI Trough June 2009
Shaded areas represent recessions as determined by the National Bureau of Economic Research. Source: The Conference Board

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AFP 10/21 – Nine of the 10 components that make up the leading index grew during the month, with the biggest positive contributors being building permits, the interest rate spread, manufacturing hours worked and stock prices.

Producer Price Index (PPI) – October: Producer Prices Fall

AFP 11/21 - Producer prices for finished goods fell on a monthly basis for only the 2nd time in 16 months. Prices of finished energy goods dropped 1.4% (gasoline prices declined 2.4%) while prices of finished foods grew 0.1%. Net of energy and food ("core" PPI), prices of finished goods were unchanged for the month. Earlier in the production cycle, prices of intermediate goods dropped 1.1% (prices of core intermediate goods slipped 0.6%). Prices of crude goods declined 2.5% while those of core crude goods fell 4.3%. Over the past 12 months, prices of finished producer prices have grown 5.9% (the smallest 12-month comparable since March), while those of core finished goods were up 2.8%.

Econoday 11/15 – Weaker energy costs turned producer price inflation negative—at least temporarily in October. Producer prices fell 0.3% in October after jumping 0.8% in September. The October number came in lower than the consensus forecast for a 0.2% dip.

By major components, energy fell 1.4% after rebounding 2.3% in September. Gasoline dropped 2.4%, following an increase of 4.2%. Food costs decelerated to a 0.1% rise, following a 0.6% boost in September. At the core level, the PPI was unchanged in October, following a 0.2% rise the month before. Analysts expected an increase of 0.1%. Declines in prices for prices of passenger cars and light trucks played a key role in keeping the core flat.

For the overall PPI, the year-ago rate in October was 6.1%, compared to September's 7.0% (seasonally adjusted). The core rate in October firmed to 2.8% from 2.5% in September. On a not seasonally adjusted basis for October, the year-ago headline PPI was up 5.9%, compared to 6.9% the prior month. Meanwhile the core was up 2.8% on an NSA year-ago basis, compared to 2.5% in September.

Barclays 11/15 - The downside surprise, relative to our forecast, reflected a sharper decline in energy prices (-1.4%) and smaller increase in food prices (0.1%) than we had penciled in.

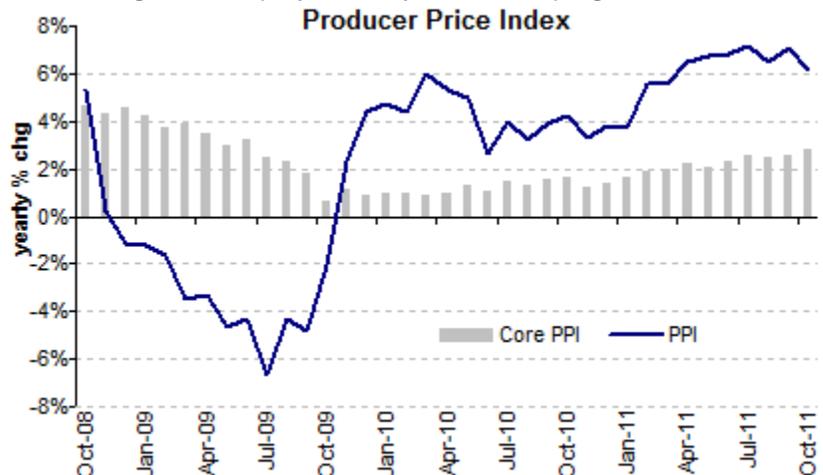
Outside of energy, food and vehicles, there were small gains in most components, such as furniture (0.6%), appliances (0.3%) and electronics (0.4%), partly offset by a decline in male apparel (-1.3%).

Consumer Price Index - October: Small downside surprise on US CPI

Vanguard 11/18 - Consumer prices fell 0.1% for the month of October, also the second decline in 2011. The decrease was largely attributed to falling energy costs. Excluding energy and food, "core" consumer prices rose 0.1% for the month.

Econoday 11/16 – By major components, energy declined 2.0%, following a jump of 2.0% in September. Gasoline dropped 3.1% after spurring 2.9% higher in September. Food price inflation softened to a 0.1% rise after jumping 0.4%. Within the core, upward pressure was seen in medical care and apparel with declines in new vehicles and used cars partially offsetting.

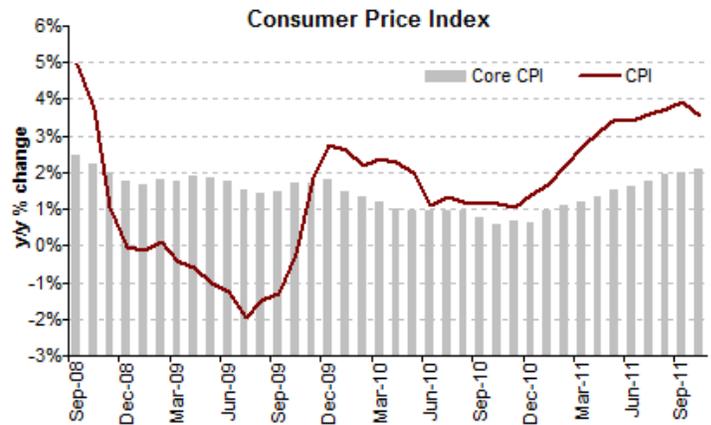
Year-on-year, overall CPI inflation slowed to 3.6% from 3.9% in September (seasonally adjusted). The core rate nudged up to 2.1% from 2.0% the month before on a year-ago basis. On an *unadjusted year-ago basis*, the headline number was up 3.5% in October, compared to 3.9% in September. The core was up 2.1%, compared to 2.0% the month before.



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Today's numbers are consistent with the Fed's hope for an easing in inflation. However, the headline number will be under upward pressure in November from the rebound in crude oil prices.

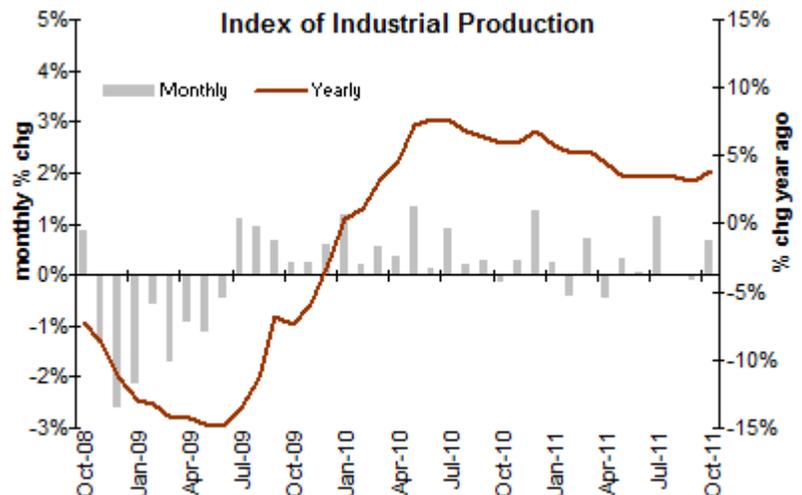
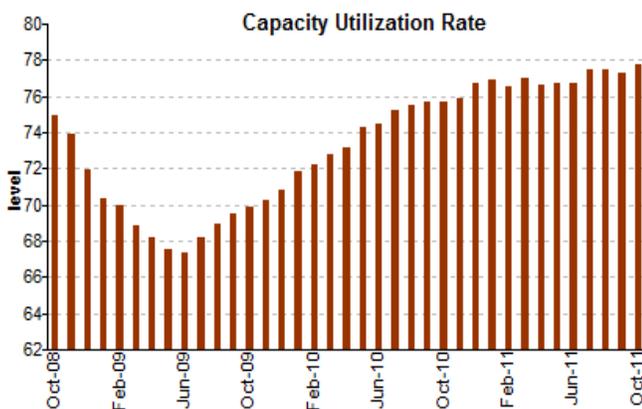
Barclays 11/16 - All in all, we don't read much into the small downside surprise in October. The underlying trend continues to be one of gradually increasing core inflation, in our judgment, particularly within the heavily weighted and persistent components of core services prices, consistent with our view that the degree of economic slack is not large. From a different angle, the decline in overall consumer prices in October, alongside the strength of nominal retail sales, is a positive for real consumption and the broader growth outlook in Q4.



Industrial Production & Capacity Utilization - October: Solid Rise in U.S. Manufacturing Output

Econoday 11/16 – In a convincing sign of economic strength, industrial production surged 0.7% in October reflecting a very strong 0.5% rise in manufacturing output and a 2.3% rebound in mining output. The rebound in mining follows a sharply downward revised 0.5% decline in September, a revision from an initial reading of plus 0.8% which is largely responsible for a downward revision to total September industrial production from plus 0.2% to minus 0.1%.

But the downward revision to September is a footnote compared to October's strength in the key manufacturing component where gains were led by a 3.1% surge in autos as the rebound from prior Japan-supply dislocations appears to be hitting a peak. Excluding autos, manufacturing still posted a second-straight and respectable 0.3% gain. Overall output of consumer goods shows a very strong 0.5% gain in the month with business equipment output extending its long run of strength, up 1.0% in the month.



Other readings in today's report include a five tenths surge in total capacity utilization to 77.8% which is the highest reading of the recovery (prior month revised to 77.3%). Output at utilities had little bearing on October's results, slipping 0.1% in the month.

Despite all the troubles in the domestic job sector and questions over European demand for US goods, the manufacturing sector is once again the focal piece of economic strength.

Barclays 11/16 - All in all, a solid report, suggesting that manufacturing output has picked up from a soft patch over the summer and that auto production continues to rebound. Any supply constraints resulting from flooding in Thailand have not, as yet, had a material effect.

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Business Inventories Flat

Vanguard 11/18 - Business inventories were flat in September, representing a reversal from the 0.8% average monthly increase over the first 8 months in 2011. The growth stall broke the string of 20 consecutive months of increases dating back to January 2010.

Econoday 11/15 – Businesses are carefully managing their inventories, keeping them lean as sales move incrementally forward.

Housing Starts – October

Econoday 11/17 – New residential construction essentially held steady in October but homebuilders may be increasingly optimistic as housing permits jumped. Housing starts in October nudged back only 0.3%, after rebounding a sharp 7.7% the prior month. The October annualized pace of 628,000 units beat analysts' estimate for 605,000 units and is up 16.5% on a year-ago basis. The dip in October was led by an 8.3% decline in the multifamily component, following a 35.0% spike in September. The single-family component rebounded 3.9% after a 2.6% decrease the month before.

By region, the decrease in starts was due to a 16.5% drop in the West. Other regions gained with the Northeast up 17.2%; the Midwest up 9.7%; and the South up 1.6%.

In an improvement for future construction housing permits jumped 10.9% after declining 5.8% in September. But the optimism is mainly for multifamily construction. Permits in October are up 17.7% on a year-ago basis. For the latest month, multifamily permits gained 24.4% while single-family permits rose 5.1%. On a year-ago basis, multifamily permits are up 48.0% while single-family permits are up 6.6%.

Homebuilders clearly are more optimistic about the multifamily sector than single-family. Apparently, excess supply is still somewhat an issue for the single-family sector, along with continued soft demand.

Empire State Index - November: Empire State Manufacturing Index Bounces Back

Barclays 11/15 - In the U.S., the Empire State Manufacturing index posted its first positive reading in five months, rising to 0.6 in November from -8.5 in October. The real news, however, was the surge in general business conditions expected in six months, which moved to 39 from 6.7 in the prior month. Expectations for capital expenditures also improved notably, moving higher to 25.6 (previous: 7.9). Overall, the report suggests that current manufacturing conditions are improving and will likely be supported by inventory rebuilding in the months ahead. Perhaps more encouraging, however, is the broad-based improvement in expectations of future conditions.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week of Nov 12

Press Release 11/17 (excerpts) - In the week ending November 12, the advance figure for seasonally adjusted initial claims was 388,000, a decrease of 5,000 from the previous week's revised figure of 393,000. The 4-week moving average was 396,750, a decrease of 4,000 from the previous week's revised average of 400,750.

WEEK ENDING	Nov 12	Nov 5	Change	Oct 29	Prior Year
Initial Claims (SA)	388,000	392,000	-5,000	400,000	441,000
4-Wk Moving Average (SA)	396,750	400,750	-4,000	405,250	441,500

Econoday 11/17 – Jobless claims continued a recent, mild downtrend with a 5,000 decline in the November 12 week to 388,000. Initial claims have decreased three weeks in a row and in four of the last five.

FFCB Weekly Debt Issuance Activity

Week Ended Date	Discount Notes \$million	New Bonds \$millions	Issue Count	Called Bonds Par \$millions	Issue Count
21-Oct	\$ 8,445	\$ 1,841	20	\$ 1,093	8
28-Oct	5,190	2,993	27	1,140	8
4-Nov	2,565	2,115	18	1,572	10
11-Nov	3,165	2,693	28	2,080	14
18-Nov	4,170	1,736	27	625	2

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The Economic Week Ahead: Nov 21 – Nov 25, 2011

Vanguard 11/18 - A shortened holiday week will feature a report on existing-home sales on Monday, while Tuesday the Department of Commerce will release its GDP report. Reports on durable goods and personal income, as well as minutes from the recent Federal Open Market Committee meeting, will be released on Wednesday.

This Week's U.S. Economic Calendar

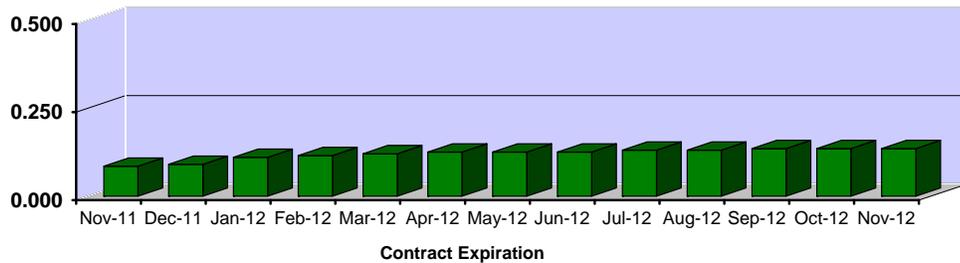
Source: MarketWatch

RELEASE DATE	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
MONDAY, NOV. 21	10 am	Existing Home Sales	October	4.80 million	4.91 million
TUESDAY, NOV. 22	8:30 am	Gross Domestic Product	3Q	2.3%	2.5%
WED., NOV. 23	8:30 am	Jobless Claims	11-19	N/A	N/A
	8:30 am	Personal Income	October	0.1%	0.2%
	8:30 am	Consumer Spending	October	0.2%	0.6%
	8:30 am	Core PCE Price Index	October	0.1%	0.0%
	8:30 am	Durable Goods Orders	October	-2.0%	-0.6%
	9:55 am	Consumer Sentiment	November	N/A	64.2
THURSDAY, NOV. 24	Thanksgiving	None Scheduled			
FRIDAY, NOV. 25		None scheduled			

Futures-Implied Fed Funds Rate

Avg. Fed Funds Rate %

Monday, Nov. 21, 2011 (10:23am EST)



Rate %	Nov-11	Dec-11	Jan-12	Feb-12	Mar-12	Apr-12	May-12	Jun-12	Jul-12	Aug-12
Rate %	0.085	0.090	0.110	0.115	0.120	0.125	0.125	0.125	0.130	0.130

FOMC MEETINGS: 11/2 12/13 1/25 3/13 4/25 6/20 7/31

VIX INDEX VIX ↓ 35.08 +3.08 Op 34.59 Hi 35.29 Lo 33.62 1/29

Range 01/07/05 - 11/18/11 Period Weekly GPO - Bar Chart Currency USD

DELAY 11:16

Last 32.00
High on 10/24/08 89.53
Average 21.90
Low on 12/15/06 9.39



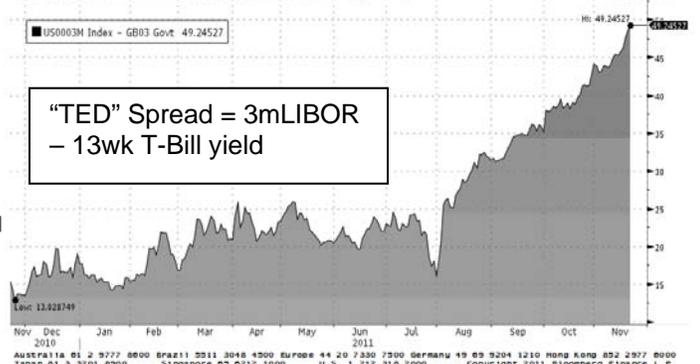
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Sell GB03 Govt Buy US0003M Index Edit

Govt TED3

Yield Spread



"TED" Spread = 3mLIBOR
- 13wk T-Bill yield