Market Comment *Economic Highlights for the week ended December 9, 2011*

Economic Week in Review: Service-Sector Activity Downshifts Again

Vanguard 12/9 - Growth in service-sector activity slowed for the third month in a row as other economic reports issued mixed signals. News from Europe continued to weigh on the markets, even as some European Union nations announced a plan to address the debt burden plaguing the EU economies. For the week ended December 9, the S&P 500 Index rose 0.9% to 1,255.2 (for a year-to-date total return of about 1.8%). The yield on the 10-year U.S. Treasury note increased 2 basis points to 2.07% (for a year-to-date drop of 123 basis points).

ISM Services - November: Details stronger than the headline

Vanguard 12/9 - The Institute for Supply Management (ISM) Non-Manufacturing Index dropped nearly a point in November to 52.0, well below the 53.5 forecast and the third straight monthly decline. The report, culled from surveys of service-sector companies, followed an October index that was the lowest since January 2010.

Econoday 12/5 – A drop in employment pulled down the ISM's non-manufacturing composite which fell nearly one point in November to 52.0, still above 50 to indicate monthly growth in business activity but at a slightly slower rate than October. Employment fell 4.4 points to a sub-50 level of 48.9 to indicate a decline in the size of the ISM sample's workforce. The drop in employment follows a soft new orders reading in October with new orders in November rising only slightly to 53.0, but still an improvement that will help limit future losses in employment.

Other readings include a strong rise in business activity, which is akin to a production index, to 56.2. But backlog orders are soft at 48.0 which will limit future gains for business activity. This report offers mixed signals for the bulk of the US economy.

US Trade Deficit Narrows on Real Export Growth, Boosts Q4 GDP Tracking To 3.5%

Vanguard 12/9 - The U.S. trade deficit narrowed for the fourth consecutive month in October, even as exports fell for the first time in four months. The deficit fell to $43.5 billion, as strong exports of capital goods and petroleum products helped offset the slight decline in overall exports. Imports dropped 1% for the month. The trade numbers were expected and could be seen as a good sign for U.S. economic growth.

Barclays 12/9 - Looking at geographic regions, exports to the euro area increased 5.4% on a non-seasonally adjusted (NSA) basis. However, after we adjust for seasonality, they fell 0.2%, marking the second straight month of declines in the seasonally adjusted data and suggesting the strains in the euro area are surfacing in a modest slowing of exports to that region. Exports to China jumped 16.4% (NSA), though after adjusting for seasonality, they were down 2.3%.

Consumer Credit - October: Consumer credit rises, driven again by non-revolving credit

Vanguard 12/9 - U.S. consumer credit rose to $7.6 billion in October, driven largely by an increase in non-revolving credit, which includes big-ticket items such as car and student loans. Revolving credit, which includes credit cards, expanded more than $360 million. This marks the ninth monthly increase in outstanding credit this year, as consumers seem more willing to assume debt as they move into the holiday season despite high unemployment and a meager (1.8%) average wage increase.

Econoday 12/7 –The increase is once again centered in non-revolving credit, which reflects strength in vehicle sales. But a steady increase is now appearing for non-revolving credit, up $0.4 billion for a second consecutive month and offering evidence that consumers are once again, at least to a limited extent, using their credit cards. September’s consumer credit was revised to $6.9 billion.

Barclays 12/7 - The rise, however, reflected direct lending from the federal government, primarily for student loans. For example, non-revolving debt held by the federal government stands $97.8bn above its level a year ago. In contrast, every other major holder of non-revolving consumer debt have seen either very modest increases or outright declines. Revolving credit continues to trend sideways, as it increased a slight $0.3bn in October, leaving it $9.2bn below its level a year ago. In general, these trends indicate that the only steady source of credit growth over the past year has been student loans and otherwise, consumers and lending institutions have remained cautious in terms of both borrowing and extending credit.

Factory Orders - October: Upward Revisions and Strong Inventory Build

Vanguard 12/9 - U.S. factory orders fell in October for the second straight month, as manufacturers continued their struggle to gain traction in the sluggish economy. Orders fell 0.4% to $450 billion, slightly more than forecast and triggered largely by a nearly 1% drop in orders for nondefense capital goods. Analysts believe the sharp economic pause earlier this year continues to restrain manufacturers.

Econoday 12/5 – The decline on the durables side is skewed by a monthly downswing in aircraft orders while the decline on the non-durables side reflects price changes for energy products.

A possible alarm in today's report is a big build in inventories of 0.9%. High inventories, together with soft orders, will limit demand for inventory replenishment.

Today's report is for October and last week's big jump for new orders in the ISM manufacturing report for November offers a strong anecdotal indication that new momentum, despite troubles in Europe and slowing in China, may be building in the factory sector. Next data on the factory sector will be goods exports in Friday's international trade report.

AFP 12/12 - While factory orders declined in Oct. to $450.0 billion, they remained 10.8% above year ago levels.

Wholesale Trade - October

AFP 12/12 - This was the fastest increase in wholesale inventories since July. Inventories were valued at $470.2 billion, an increase of 10.6% from a year earlier. Inventories of durable goods increased 0.8% while those of non-durable goods expanded by 2.8%. Sales were up 0.9% on a monthly basis, including an 1.7% jump in sales of non-durable goods sales. The inventories-to-sales ratio was 1.16, down 2-basis points from a year earlier.

Consumer Sentiment

Econoday 12/9 – Consumer spirits are definitely picking up but from deeply depressed levels. The mid-month consumer sentiment index rose a strong 3.6 points to 67.7 led by a strong 5.7 point jump to 61.1 in the leading component of expectations. The gain in expectations suggests that consumers see improvement for their job prospects and for their income prospects, keys for acceleration in consumer spending.

The consumer's assessment of current conditions is also showing improvement but to a lesser degree with the component up only three tenths to a still soft level of 77.9. Inflation expectations are benign despite $100 oil which has, however, yet to inflate prices at the gas pump. One-year inflation expectations are down one tenth to 3.1% with five-year expectations unchanged at 2.7%.

Stronger improvement in the jobs market together with an easing in the volatility of the financial markets would go a long way to further improve the consumer's mood.

Flow-of-Funds Accounts of the United States

AFP 12/12 - The Federal Reserve reported that U.S. companies continued to build out their cash holdings during the third quarter. According to the *Flow of Funds Accounts of the United States*, non-financial companies had liquid assets totaling $2.115 trillion at the end of September. This was up from the $2.074 trillion estimated for the second quarter and the $1.941 trillion reported for the third quarter of 2010.

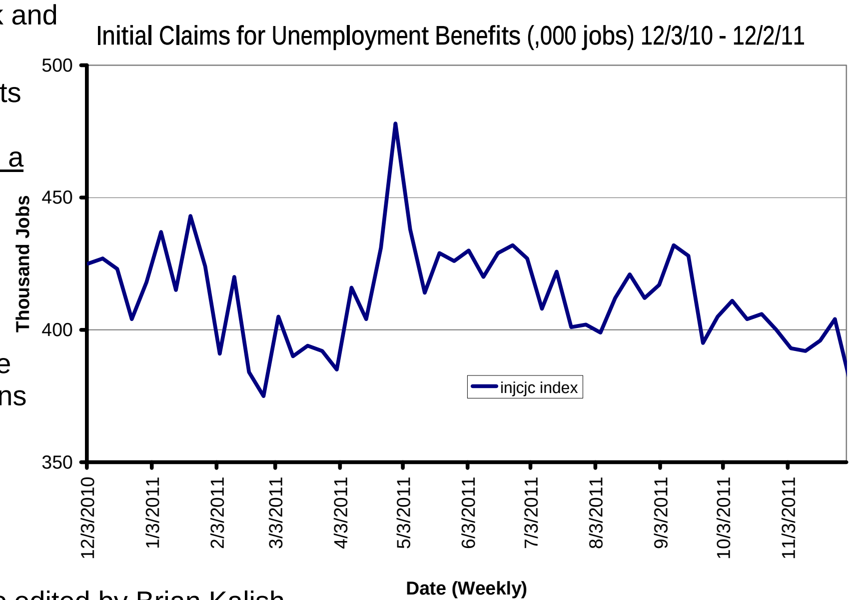
The same report also found that households continued to deleverage during the third quarter. Households had $13.208 trillion in outstanding debt at the end of September, down from the $13.247 trillion at the end of the second quarter and $13.349 trillion from a year earlier. Outstanding corporate debt meanwhile has been increasing. The Fed estimates outstanding corporate debt at the end of September was $11.499 trillion, up from $11.400 trillion at the end of the second quarter and $11.090 trillion at the end of third quarter of 2010.

Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week of Dec 3

Press Release 12/8 (excerpts) - In the week ending December 3, the advance figure for seasonally adjusted initial claims was 381,000, a decrease of 23,000 from the previous week's revised figure of 404,000. The 4-week moving average was 393,250, a decrease of 3,000 from the previous week's revised average of 396,250.

WEEK ENDING	Dec 3	Nov 26	Change	Nov 19	Prior Year
Initial Claims (SA)	381,000	404,000	-23,000	396,000	425,000
4-Wk Moving Average (SA)	393,250	396,250	-3,000	395,250	430,250

Econoday 12/8 – Initial jobless claims fell a sizable 23,000 in the December 3 week to 381,000, their lowest level since February (prior week revised 2,000 higher to 404,000). There are no unusual factors in the data though the unadjusted week-to-week increase for the post-Thanksgiving week is the largest of the year, a factor that seasonal adjustments smooth and one that clouds the results a bit. A clearer positive is the four-week average of 393,250, down 3,000 in the week and at its lowest level since April.



Today's report is very welcome but the results will have to be confirmed by improvement in subsequent weeks. The holidays are always a tough time to get a clear read on weekly claims data.

Barclays 12/8 - The broader picture is now suggesting that jobless claims are beginning to head lower after a period of moving broadly sideways, consistent with the recent improvement in labor market conditions and in line with our view that payroll growth should continue to accelerate in the coming months.

Eurozone Comment

AFP 12/12 - *The Week in Corporate Finance* edited by Brian Kalish

So what did happen in Europe this week? On Monday, S&P got the week started by putting most of the Euro-zone not already on negative watch, on negative watch. The market pretty much just shrugged its collective shoulders at this hardly earth-shattering news. The focus of the week was on the Euro Summit taking place in Brussels on Thursday and Friday. As we waited for news of a new rescue plan to come out of Belgium, the ECB in Frankfurt (as expected) announced they were lowering their benchmark rate by 25bps from 1.25% to 1.00%. This was the second consecutive meeting where the rate was lowered by 25bps and now after the two earlier tightenings in the year, the benchmark rate is back to its all-time low.

With the announcement that the ECB would not be accelerating its purchasing of European government bonds, the weaker European sovereigns sold-off. On Friday, we received news that Europe would be tightening its budget rules and accelerating the start of its rescue fund, so the markets felt a bit calmer, and money moved away from safety into riskier assets.

During the week the Italian 10-year bond yield spiked to 6.69%, before closing the week at 6.36%; the Spanish 10-year bond yield got as high as 5.99%, before falling to 5.75%; the Belgian 10-year bond yield reached as high as 4.75%, before dropping to 4.55%; and the German 2-year note actually fell to a new all-time low yield of 27bps, before creeping up to 32bps.

The Greek 1-year note closed at a new all-time high yield of 352.88%, their 2-year note hit a new all-time high yield of 150.57% before easing off a bit to 147.99%, and the Greek 10-year bond settled for the week at an all-time new high yield of 35.06%. The market continues to vote with its wallet that there is a high probability that Greece will default and there will be a significant loss of principal for investors.

We continue to witness ongoing year-end pressures in the money-markets. The 3-month LIBOR rate reached 54.18bps, the highest level since July 2009; the LIBOR-OIS spread widened to 44.8bps, the greatest it's been since May 2009; and the TED spread reached 54bps, the widest it has been since June 2009.

The Economic Week Ahead: Dec 12– Dec 16, 2010

Vanguard 12/9 - Next week's reports begin Tuesday with data on retail sales and business inventories, along with the Federal Open Market Committee's scheduled meeting. Reports continue on Thursday with the Producer Price Index and industrial production, followed by the Consumer Price Index on Friday.

AFP 12/12 - The Federal Open Market Committee will have their final scheduled meeting for 2011 this week. While the focus of the meeting is likely to be on expanding/improving the communication of the committee's policy goals, it appears at least one voting member will push the committee to launch a third round of quantitative easing. Federal Reserve Bank President Charles Evans stated in a speech last Monday that "[t]here is simply too much at stake for us to be excessively complacent while the economy is in such dire shape. It is imperative to undertake action now."

This Week's U.S. Economic Calendar *Source: MarketWatch*

	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
MONDAY, DEC. 12	2 pm	Federal Budget	November	--	-$150 billion
TUESDAY, DEC. 13	8:30 am	Retail Sales	November	0.3%	0.5%
	8:30 am	Retail Sales Ex-Autos	November	0.1%	0.6%
	10 am	Inventories	October	0.5%	0.0%
		FOMC Meeting	December		
WEDNESDAY, DEC. 14	8:30 am	Import Prices	November	1.5%	-0.6%
THURSDAY, DEC. 15	8:30 am	Jobless Claims	12-10	N/A	N/A
	8:30 am	Producer Price Index	November	0.1%	-0.3%
	8:30 am	Core PPI	November	0.2%	0.0%
	9:15 am	Industrial Production	November	0.2%	0.7%
	9:15 am	Capacity Utilization	November	77.9%	77.8%
FRIDAY, DEC. 16	8:30 am	Consumer Price Index	November	0.0%	-0.1%
	8:30 am	Core CPI	November	0.2%	0.1%

FFCB Weekly Debt Issuance Activity

Week Ended Date	Discount Notes $million	New Bonds $millions	Issue Count	Called Bonds Par $millions	Issue Count
11-Nov	$ 3,165	$ 2,693	28	$ 2,080	14
18-Nov	4,170	1,736	27	625	2
25-Nov	4,800	1,804	22	385	4
2-Dec	2,280	2,824	22	1,051	7
9-Dec	4,290	3,936	28	1,875	13