

Market Comment *Economic Highlights for the week ended December 23, 2011*

Economic Week In Review: Nice Edges Naughty On Improved Growth And Housing Results

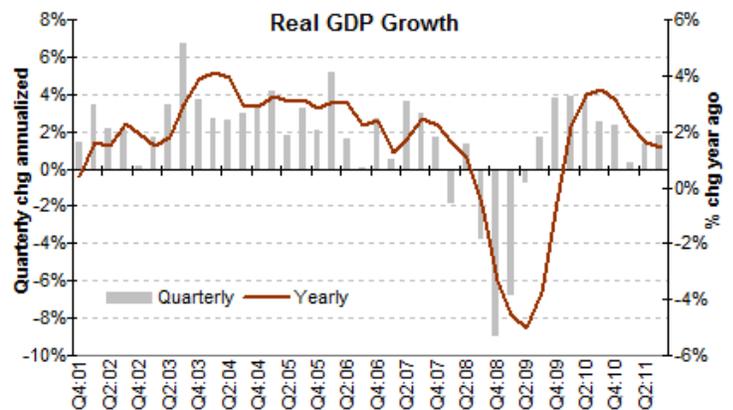
Vanguard 12/23 – As holiday shoppers grabbed last-minute gifts and Europe's leaders continued to search for solutions to their debt crisis, the latest economic reports offered more positive news than negative. Third-quarter GDP's lower-than-expected growth rate was still the best for the year, and leading economic indicators rose for the seventh straight month, while the battered housing market reported progress on a number of fronts. For the week ended December 23, the S&P 500 Index rose 3.7% to 1,265 (for a year-to-date total return—including price change plus dividends—of about 2.7%). The yield on the 10-year U.S. Treasury note rose 17 basis points to 2.03% (for a year-to-date drop of 127 basis points).

Third-Quarter GDP Is Revised Downward

Vanguard 12/23 – The nation's gross domestic product (GDP) surprised economists by growing at an annualized rate of 1.8% in the third quarter, which was lower than expected. Although this was the strongest quarterly gain for the year, it was below the previously reported estimate of 2.0% (and an earlier estimate of 2.5%). The lower growth rate was primarily because of a downward revision in consumer spending, especially for health care services, that was only partly offset by an upward revision to inventory accumulation. Final sales—a gauge of demand based on GDP minus the change in inventories—was a strong 3.2%, the second-largest increase in four years. Growth in third-quarter corporate profits, which was also revised downward, slowed but was 7.5% higher than a year earlier.

Econoday 12/22 – On a year-ago basis, GDP is up 1.5%, compared to 1.6% in the second quarter.

Economy-wide inflation revised up marginally to 2.6% from the second estimate of 2.5%.



Leading Economic Indicators – November

Vanguard 12/23 – The Conference Board's gauge of potential future economic activity rose 0.5% in November, higher than expected but slower than October's 0.9% gain. The index has increased for seven straight months. Seven index components rose, led by stock prices, money supply, and the yield curve, while manufacturing declined. Conference Board economist Ken Goldstein said that the index pointed toward continued growth that may gain momentum in the spring. Increases in building permits suggested "a chance that the long decline in housing is finally slowing." But, he added, the "somewhat positive outlook for the domestic economy is at odds with a global economy that appears to be losing steam."

Econoday 12/22 –The leading positive is the rate spread which reflects the Federal Reserve's zero interest rate policy. The second positive is building permits which appear to be building steam in what is very good news for the construction sector. Consumer expectations are a big positive in the month and judging from this morning's consumer sentiment report look to be a big positive for December. Another positive that's likely to extend through this month is the November improvement in jobless claims which gave the fifth strongest contribution to the month's 0.5% gain.

A decline in the factory workweek is the largest in the short list of negatives, and perhaps one that will reverse this month given early indications of strength in last week's Empire State and Philly Fed reports. A speeding up in vendor deliveries is the second largest negative.

Housing Starts: Multifamily Construction Boosts Housing Starts

Vanguard 12/23 – New residential construction increased 9.3% in November, more than expected. A 25.3% surge in multifamily starts, mostly apartment buildings, drove most of the gains. Apartments were in demand as many potential home buyers were unable or unwilling to make the commitment to purchase. Construction of single-family homes rose 2.3%. Issues for permits, which indicate new-home demand, climbed 5.7%, but completions dropped 5.6%. The Northeast and West fueled the boost in new construction. Only Midwest starts declined. Despite the overall increase, growth is still behind normal levels.

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Econoday 12/20 – Housing starts in November rebounded 9.3% after slipping 2.9% in October. The November annualized pace of 0.685 million came in higher than market expectations for 0.636 million units and is up 24.3% on a year-ago basis. The gain in November was led by a 25.3% jump in the multifamily component, following a 15.2% decrease in October. The single-family component improved 2.3% after a 3.6% rise the month before.

By region, the boost in starts was led by a 53.8% jump in the Northeast. Other regions showing increases were the West, up 22.6%, and the South, up 4.1%. The Midwest declined 18.2%.

There are signs that the level of activity in single-family home sales is picking up, but the real action clearly has shifted to the multifamily sector as high unemployment and still tight credit are constraining home sales.

Existing-Home Sales – November: Previously Reported Sales Revised Down Significantly

Vanguard 12/23 – Sales of existing homes rose 4.0% in November to an annual rate of 4.42 million, the highest mark in ten months. Sales were strongest in the Northeast, slowest in the South, and overall were 12.2% higher than a year earlier. The inventory of unsold homes declined sharply—from 7.7 to 7 months' supply at the current pace—primarily because there were fewer homes available for sale. The National Association of Realtors' report noted an elevated level of canceled contracts, suggesting that "overly restrictive mortgage underwriting" was a factor. In addition, historical data was significantly revised: Sales and inventory from 2007 through 2010 were 14.3% lower than originally reported.

Press Release 12/21 (excerpts) – According to Freddie Mac, the national average commitment rate for a 30-year, conventional, fixed-rate mortgage fell to a record low 3.99% in November from 4.07% in October; the rate was 4.30% in November 2010; records date back to 1971.

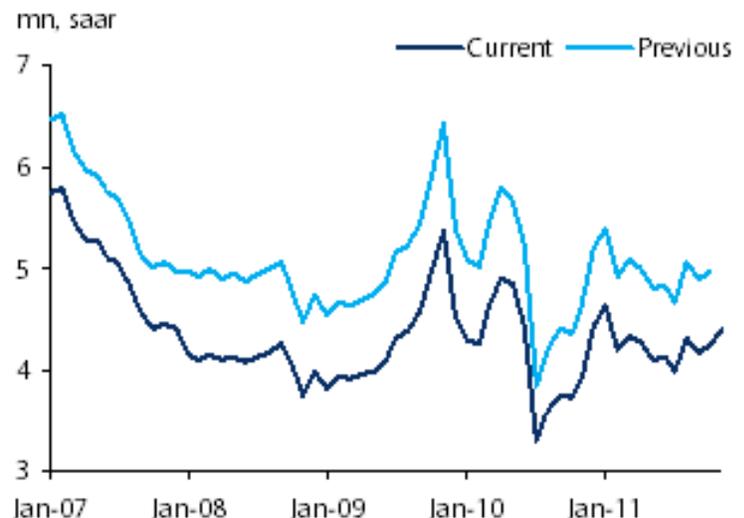
Total housing inventory at the end of November fell 5.8% to 2.58 million existing homes available for sale, which represents a 7.0-month supply at the current sales pace, down from a 7.7-month supply in October. "Since setting a record of 4.04 million in July 2007, inventories have trended down and supplies are moving close to price stabilization levels," Yun said.

The national median existing-home price for all housing types was \$164,200 in November, down 3.5% from a year ago. Distressed homes – foreclosures and short sales typically sold at deep discounts – accounted for 29% of sales in November (19% were foreclosures and 10% were short sales), compared with 28% in October and 33% in November 2010.

NAR President Moe Veissi said housing affordability conditions have set a new record high. "With record low mortgage interest rates and bargain home prices, NAR's housing affordability index shows that a median-income family can easily afford a median-priced home," he said.

Also released today are benchmark revisions to historic existing-home sales. The 2010 benchmark shows there were 4,190,000 existing-home sales last year, a 14.6% revision from the previously projected 4,908,000 sales. For the total period of 2007 through 2010, sales and inventory were downwardly revised by 14.3%. The revisions are expected to have a minor impact on future revisions to Gross Domestic Product.

A divergence developed over time between sales reported by MLSs and sales determined by a U.S. Census benchmark; the variance began in 2007. Reasons include growth in MLS coverage areas from which sales data is collected, and geographic population shifts. "It appears that about half of the revisions result solely from a decline in for-sale-by-owners (FSBOs), with more sellers turning to Realtors® to market their homes when the market softened. The FSBO market was overwhelmed during the housing downturn, and since most FSBOs are not reported in MLSs, national estimates of existing-home sales began to diverge based on previous assumptions," Yun said.



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New-Home Sales – November: Pace Is Highest Since April

Vanguard 12/23 – Sales of new single-family homes climbed 1.6% in November to an annual rate of 315,000, as October sales were revised upward to 310,000. The pace is the highest since April and slightly better than analysts had projected. Growth in the South and Midwest drove the gains as sales rose 9.8% compared with a year ago. The supply of new homes fell from 6.2 in October to 6 months. However, the median sales price dropped to \$214,100 from \$222,600.

Home Builders Index – December: US Home Builder Sentiment Gradually Improving

Econoday 12/19 – The good economic news keeps rolling in and increasingly includes indications of positive momentum in the housing sector. The home builders index rose two points in December to 21 for its best reading since May last year when government efforts were stimulating buying (November revised to 19). And for the first time since mid 2009, the index has posted three consecutive gains.

Durable Goods Orders – November: Aircraft Lift Durable Goods Orders

Vanguard 12/23 – New orders for durable manufactured goods jumped 3.8% in November, more than forecast and the fourth rise in five months. Orders from Boeing fueled a 73.3% gain in non-defense aircraft and parts; excluding transportation, new orders increased just 0.3%. Shipments declined 0.4%, unfilled orders climbed 1.3%, and inventories rose 0.6%. Core capital goods, a measurement of business investment spending, declined 1.2%. Gains in metal and machinery were offset by declines in computer-related equipment.

Barclays 12/23 - The upside surprise fully reflected gains in the volatile non-defense aircraft (73.3%) and defense (3.7%) components. Core capital goods orders declined 1.2%, well below our forecast (0.7%), although this was partly offset by an upward revision to October, to -0.9% from -1.8%.

Personal Income and Consumer Spending – November

Vanguard 12/23 – Personal income and consumer spending both grew 0.1% in November, less than expected. Higher rental, dividend, and interest income led the rise in income, as wages dropped after two months of gains. Inflation, as measured by consumer prices, fell slightly for the second straight month, although it was 2.5% higher than a year ago. Core inflation, which excludes food and energy costs, increased 0.1% in November and was up 1.7% from last year. The 3.5% personal savings rate was down slightly from October.

Barclays 12/23 - All in all, a broadly neutral report in terms of tracking real consumption in Q4, but the weakness of household income sets an uneasy backdrop for consumption prospects in 2012, highlighting the importance of the extension of the payroll tax cut.

Consumer Sentiment - December

Econoday 12/22 – Consumer sentiment continues to extend its improvement, to 69.9 in December from 64.1 in November and from 67.7 at mid month. The reading implies a very strong 72.1 over the last two weeks which points to momentum for January. The bulk of the gain is centered in expectations, at 63.6 in December for a more than eight point monthly gain that points further to momentum in the New Year. The assessment of current conditions, likely held down by bad news out of Europe, rose only two points in the month to 79.6.

One likely positive for sentiment is improvement in the jobs market as well as the stock market which has been on the recovery. Another positive may be gasoline prices which, despite \$100 oil, are on the decline. One-year inflation expectations eased one tenth in the month to 3.1% with five-year expectations unchanged at 2.7%. The Dow is moving to morning highs following this report. The December consumer confidence report from the Conference Board, which in November surged, will be posted on Tuesday.

Barclays 12/22 - Overall, the report is generally positive and points to an on-going improvement in sentiment following the August confidence shock that was brought about by the contentious debt-ceiling debate and S&P downgrade of US sovereign debt. A current risk is how the debate regarding the payroll tax cut will unfold and affect sentiment in the months ahead. We would emphasize, however, that we often see a disconnect between what consumers say and how they act - so while a failure to extend the payroll tax cut would likely weigh on sentiment, the larger risk to the outlook in this case would rest with the real reduction in disposable personal income, rather than a potential drop in sentiment.

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Unemployment Insurance Weekly Claims Report (Initial Jobless Claims) – week of Dec 17

Press Release 12/22 (excerpts) - In the week ending December 17, the advance figure for seasonally adjusted initial claims was 364,000, a decrease of 4,000 from the previous week's revised figure of 368,000. The 4-week moving average was 380,250, a decrease of 8,000 from the previous week's revised average of 388,250.

WEEK ENDING	Dec 17	Dec 10	Change	Dec 3	Prior Year
Initial Claims (SA)	364,000	368,000	-4,000	385,000	423,000
4-Wk Moving Average (SA)	380,250	388,250	-8,000	394,250	428,500

Econoday 12/22 – Layoffs are on a steady decline in what is good news for the jobs market and for the December employment report. Both Initial claims and the four-week average fell for a third week in a row..

The holidays, with its shortened weeks and extreme effects, are always a tough time to gauge weekly jobless claims data, but the trend is clearly lower in what should be good news for the markets and which should continue to build expectations for a strong gain in December payrolls.

The Economic Week Ahead: Dec 26– Dec 30, 2010

Vanguard 12/23 – The last week of the year will be quiet for economic reports, with only The Conference Board's consumer confidence survey set for release on Tuesday.

This Week's U.S. Economic Calendar

Source: MarketWatch

	TIME (ET)	REPORT	PERIOD	FORECAST	PREVIOUS
MONDAY, DEC. 26		None Scheduled			
TUESDAY, DEC. 27	9 am	Case-Shiller Home Prices	October	--	
	10 am	Consumer Confidence	December	60.0	56.0
WEDNESDAY, DEC. 28		None Scheduled			
THURSDAY, DEC. 29	8:30 am	Initial Jobless Claims	12-24	N/a	N/A
	9:45 am	Chicago PMI	December	62.0%	62.6%
FRIDAY, DEC. 30		None Scheduled			

FFCB Weekly Debt Issuance Activity

Week Ended Date	Discount Notes \$million	New Bonds \$millions	Issue Count	Called Bonds Par \$millions	Issue Count
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
16-Dec	5,455	4,209	26	1,634	16
23-Dec	4,200	1,504	17	884	6