

Weekly Economic Commentary



April 12, 2010

Information Overload

Last week was relatively quiet on the economic front. The best news of the week was the unexpected surge in pending home sales in February, along with a better-than-expected reading on both chain store sales and the service sector Institute for Supply Management (ISM) index for March. The unexpected rise in first-time filings for jobless claims in early April was a disappointment, but was likely influenced by the Easter holiday. The minutes of the March 16 Federal Open Market Committee (FOMC), as well as two speeches from the Chairman of the Federal Reserve (Fed) Ben Bernanke, were viewed by the market as "dovish" (meaning the Fed is in no hurry to raise interest rates), and markets lowered the odds of rate hikes later in 2010.

As noted above, the best report of the week was the surprisingly strong pending home sales report for February, which revealed that pending home sales rose 8.2% in February versus January. The consensus was looking for no change in the number of pending home sales between January and February. The robust gain in pending home sales—which usually become existing home sales within 60 days—gave the market faint hope that the second incarnation of the first-time homebuyer tax credit was finally gaining traction, after having no discernable impact on the housing market since it was extended and expanded in November 2009.

On balance, last week's data kept the economy on track to post a 4.0% gain (as measured by Real Gross Domestic Product (GDP)) in the first quarter of 2010. The first quarter 2010 GDP data is due out at the end of April.

Our View on the Key Reports and Events of the Coming Week:

This week is chock full of economic data, public appearances from key Fed officials, the Fed's Beige Book—a qualitative assessment of economic activity in each of the 12 regional Federal Reserve districts—along with several global central bank meetings.

The U.S. data due out this week includes data on virtually every sector of the economy, as market participants firm up their estimates for first quarter 2010 GDP growth. The first quarter GDP data is due out on April 30. The consensus estimate is currently 3.0%, while our forecast is for 4.0% GDP growth in Q1. In addition to getting a better read on Q1 growth, the market will be looking ahead to see if the data for March and April sets the stage for continued above-trend GDP growth over the remaining quarters of 2010.

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ECONOMIC CALENDAR

Monday, Apr 12

Treasury Statement
Mar

Tuesday, Apr 13

Import Price Index
Mar

Trade Balance
Feb

Wednesday, Apr 14

CPI
Mar

Beige Book
Mar

Retail Sales
Mar

Business Inventories
Feb

Thursday, Apr 15

NY Fed Empire State Mfg
Apr

Initial Claims
wk 04/10

Capacity Utilization
Mar

Industrial Production
Mar

Philly Fed Index
Apr

NAHB Housing Survey
Apr

Friday, Apr 16

Housing Starts
Mar

U of Mich Consumer
Sentiment
Apr

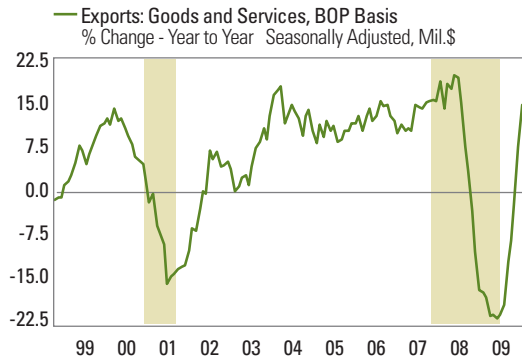
Highlights

A quiet week for U.S. economic data kept the U.S. economy on pace for growth at close to 4.0% in the first quarter 2010.

This week, the full slate of U.S. economic data has to compete with the start of earnings season, a full calendar of Chinese economic data, as well as two speeches from Fed Chairman Bernanke and the Fed's Beige Book.



1 The Booming Export Sector has Lifted Business Capital Spending and Manufacturing



Source: Census Bureau, Haver 04/12/10
Shaded areas represent recessions.

An early April survey (by Bloomberg) of 74 economists put the odds of a “double dip” recession at 15%, the same as in the March 2010 survey. By contrast, last fall, economists put the odds of a “double dip” at 25%. We were never in the double dip camp, and we would put the odds of another recession beginning in 2010 at around 5 % only.

As mentioned above, there is data due out this week on virtually all the key sectors of the economy, ranging from the strongest part of the economy (exports and manufacturing) to the weakest, the housing sector.

The February merchandise trade data is due out this week, and it is likely to reveal another booming month for U.S exports. The export sector has helped to lead the economy out of recession in the last two recoveries (1991 and 2001), and this time is no different. The boom in exports has allowed the manufacturing sector to prosper. Data from the Philadelphia Fed and the New York Fed on the manufacturers in those areas will likely confirm that booming exports (along with inventory restocking) continued into April.

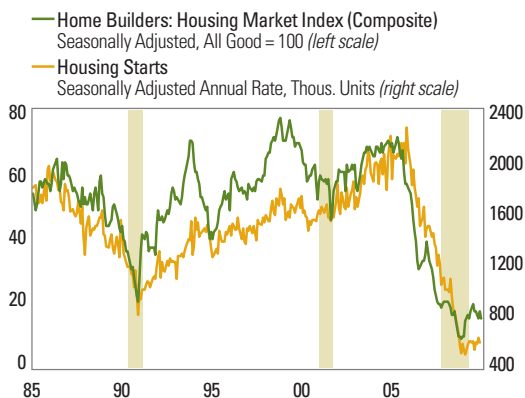
Over on the other side of the coin is the housing market, which has been one of the weak spots in the recovery. This week, markets will digest the April reading on the National Association of Homebuilders sentiment index, along with the housing starts data for March. While the surprising surge in pending home sales in February (reported last week) was welcome news, market participants remain skeptical that the housing market can be a meaningful participant in the recovery. In addition, with the end of the first-time homebuyer tax credit looming—buyers must have a signed agreement of sale by April 30 to qualify—time is running out on government support for housing.

The market will digest a full plate of Chinese economic data for March this week. That data, which is likely to show a booming Chinese economy, may prompt Chinese authorities to take additional steps to reign in bank lending and raise interest rates. Over the weekend, and overnight Sunday into Monday, China did release some of the data mentioned above. Data on new loan growth, money supply growth and China’s trade balance revealed that while China’s economy slowed (amid mandated policy tightening in China that began in January), it probably did not slow enough to prevent Chinese authorities from tightening policy again soon. That tightening could come as soon as this week.

As markets continue to puzzle over the Fed’s next move, Federal Reserve Chairman Ben Bernanke will deliver a speech on Tuesday, April 13 and testify before Congress on April 14. The market is looking for clues as to whether or not the Fed will retain the “extended period” language in its next (April 28) policy statement. Bernanke did not mention “extended period” in either of the two speeches he delivered last week, which could suggest that the FOMC may be moving away from a time-based (i.e. rates low for an extended period) promise, to a more data-dependent (i.e. is inflation or economic growth tracking to the Fed’s forecast) promise on rates.

Finally, the Fed will release its Beige Book this week. The Beige Book is typically released two weeks ahead of the ensuing FOMC meeting, and can often provide insight into how the FOMC participants view the economy.

2 The Housing Market Has Yet to Respond to the Extension and Expansion of the First Time Homebuyers Tax Credit



Source: NAHB, Census Bureau, Haver 04/12/10
Shaded areas represent recessions.



Recent Beige Books have been quite mild in their assessment of the economy, the labor market, and importantly, the inflation situation. Another benign Beige Book may signal that the Fed will be on hold for even longer than the market now expects. The market now expects the Fed's first rate hike to occur at the November FOMC meeting, and we concur.

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Investing in international and emerging markets may entail additional risks such as currency fluctuation and political instability. Investing in small-cap stocks includes specific risks such as greater volatility and potentially less liquidity.

Stock investing involves risk including loss of principal. Past performance is not a guarantee of future results.

ISM Manufacturing Index: An index based on surveys of more than 300 manufacturing firms by the Institute of Supply Management. The ISM Manufacturing Index monitors employment, production inventories, new orders and supplier deliveries. A composite diffusion index is created that monitors conditions in national manufacturing based on the data from these surveys.

Manufacturing Sector: Agglomeration of industries engaged in chemical, mechanical, or physical transformation of materials, substances, or components into consumer or industrial goods.

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