

Weekly Economic Commentary



November 29, 2010

December Data Deluge

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Highlights

- A deluge of key economic events awaits market participants returning from the long Thanksgiving weekend.
- The November jobs report is likely to highlight an improving job market.
- The consumer is in focus as the holiday shopping season kicks off.

Economic Calendar

Tuesday, November 30	Challenger Layoff Announcements <i>November</i>
Chicago Purchasing Managers Index <i>November</i>	Beige Book
Consumer Confidence <i>November</i>	Thursday, December 2 Initial Claims <i>wk 11/27</i>
Wednesday, December 1	Friday, December 3
Unit Labor Costs <i>Q3</i>	Private Sector Payrolls <i>November</i>
Productivity <i>Q3</i>	Unemployment Rate <i>November</i>
ISM Manufacturing <i>November</i>	Nonfarm Payrolls <i>November</i>
Construction Spending <i>October</i>	Factory Orders <i>October</i>
Domestic Light Vehicle Sales <i>November</i>	ISM Service Sector <i>November</i>
ADP Employment <i>November</i>	

This week (November 29-December 3) is full of key economic reports in the United States, as financial market participants return from the Thanksgiving weekend. The reports will cover the status of the labor market, manufacturing, the consumer, and will help to set the tone for financial markets as the remainder of 2010 unfolds. In addition to the data deluge in the United States, financial market participants are likely to continue to fret about the ongoing sovereign debt issue in Europe, the flare-up of tensions on the Korean peninsula, and China's actions to cool economic growth and lending. Six global central banks meet to set monetary policy this week: India, Indonesia, Thailand, Hungary, Bulgaria and the European Central Bank (ECB). None of the six banks are expected to raise rates, although both India and Thailand have already begun raising rates in this cycle. A key report on the manufacturing sector in China, the November PMI, is due out early this week, and may reignite talk of more policy shifts in China aimed at slowing growth and, more importantly, cooling inflation.

One of the key questions financial market participants will be asking themselves as they interpret this week's data is whether or not the U.S. economy has definitively emerged from the summer soft spot that commenced in late spring 2010 and began to firm as the weather began to turn cooler. In general, most of the economic data released in the United States since early to mid-September supports the notion that the summer soft spot has ended and that the economy is reaccelerating. The pace of that reacceleration will be at the center of the debate this week.

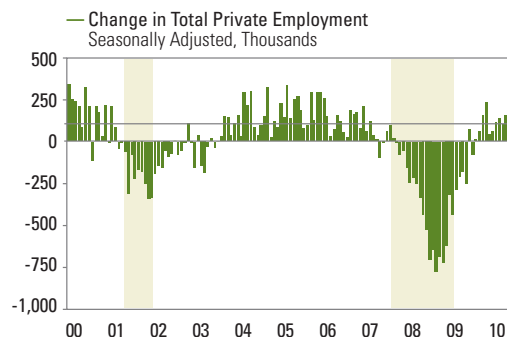
The release of the Federal Reserve's (Fed) Beige Book, a qualitative assessment of economic conditions in each of the 12 Federal Reserve districts will provide the broadest (and most timely) look at economic and business conditions in the U.S. economy in November. We will be looking for color on bank lending, business demand for bank loans, hiring, an early read on holiday shopping, and any change in tone following the results of the mid-term Congressional elections. This will be the first Beige Book since the onset of the Fed's second round of quantitative easing (QE2), and we will also be combing through the report looking for early signs of the impact QE2 is having on the economy. The Beige Book is due on Wednesday, December 1.

The November Jobs Report Likely to Highlight an Improving Labor Market

Employment will be a major theme of the week's data and, as any good holiday gift should, it comes in several varieties this week. The employment component of the November Chicago Area Purchasing Managers Index



1 The Private Sector Economy Has Not Generated 100,000+ Jobs in Five Consecutive Months Since Early 2006



Source: Bureau of Labor Statistics /Haver Analytics 11/29/10
(Shaded areas in chart indicate recessions)

(Tuesday, November 30), the November Institute for Supply Management (ISM) report on manufacturing (Wednesday, December 1), and the Dallas Fed Index (Monday, November 29) will be the first employment related reports of the week. The results of these two surveys will be compared against the employment data already available for November—weekly initial claims, the employment readings from the Philly Fed, Richmond Fed, Kansas City Fed and Empire State manufacturing indices—all of which suggest some acceleration in hiring in the private sector between October and November.

By midweek, the focus will shift to the ADP employment report and the Challenger layoff report for November. Both reports are due out on Wednesday, December 1. The ADP employment report tracks hiring trends in the private sector based on data from the nation's largest payroll processing firm. Over the past six months, the ADP jobs report has underestimated actual private payrolls by between 50,000 and 100,000 per month. The market is looking for a 65,000 gain in ADP employment in November, which is consistent with a private sector payroll gain of around 140,000 in November. The Challenger layoff data has been a useful indicator in recent months as market participants debated whether or not the summer soft spot would turn into a double-dip recession. Layoff announcements from U.S. corporations are at their lowest level in more than 10 years, suggesting that while companies may not be hiring as quickly as we would like them to be, they are not laying off very many workers either. The signal emanating from the Challenger layoff data is that a double-dip recession is not in the cards.

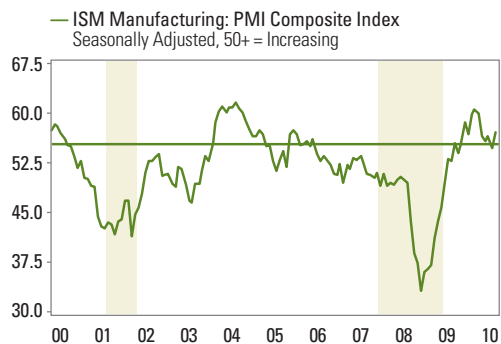
Finally, the key employment-related report of the week is due out on Friday, December 3. For the first time since early 2010, there will not be much distortion in the jobs report from the hiring of temporary government workers to conduct the 2010 Census. Thus, for the first time since the first few months of 2010, the market's focus will be on total nonfarm payroll employment, and not just private sector employment. While it is helpful that the November jobs data is likely to be free of the Census-related distortions that have plagued the data since early 2010, the market may shift its focus from the private sector (where more than 1.1 million jobs have been created in the past 12 months) to the government sector, and especially the state and local government sector.

Typically, a reliable engine of jobs growth in good times and in bad, the state and local government sector has shed jobs in nine of the first ten months of 2010, and in 20 of the 26 months since September 2008. State and local governments have shed more than 400,000 jobs since September 2008, as the woes of the national economy and housing market hit state and local government budgets. Since most states are required by law to balance their budgets, (and labor costs account for a huge chunk of public sector costs) job cuts and funding cuts to cities, towns and municipalities are always part of the equation for legislators looking to cut costs. We continue to expect more pain on the state and local job front in the year ahead.

Over on the private sector side, the consensus is looking for a 155,000 gain in employment in November, following the surprisingly large 159,000 gain in October. If achieved (and absent any revision to prior months), the back-to-back gains in jobs in October and November would be the most



2 The ISM Index Has Not Been Consistently Above 55 Since Early 2004



Source: Institute for Supply Management/Haver Analytics 11/29/10
(Shaded areas in chart indicate recessions)

robust since March and April 2010 (prior to the onset of the summer growth slowdown and double-dip fears). A gain in private sector employment close to the consensus would also mark the first time since late 2005/early 2006 that the private sector economy has generated more than 100,000 jobs in five consecutive months.

The Manufacturing and Consumer Sectors Also In Focus This Week

The manufacturing sector will also be in focus this week, highlighted by the release of the Chicago Area Purchasing Managers Index for November on November 30, and the broader, national ISM report on manufacturing on December 1. Based on the regional ISMs and regional Fed manufacturing surveys already released for November, there is a strong likelihood that the overall ISM for November will remain above 56.0 (where a reading above 50 indicates that the manufacturing sector is expanding) for the second consecutive month, after dipping to 54.4 in September. If the ISM does indeed stay above 56.0 in November, it would mark the longest stretch of time since early 2004 that the ISM has consistently been at or above 55.0. We would interpret this as yet another sign that the recovery in U.S. economy that began in June 2009 is beginning to gain some traction.

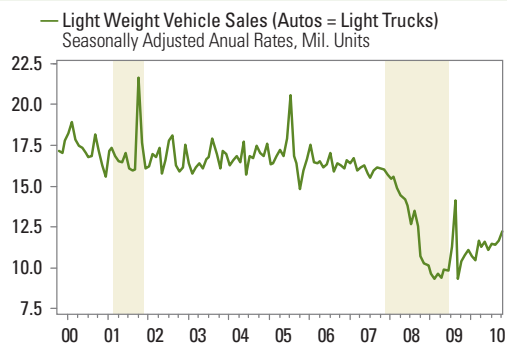
Already in focus as the 2010 holiday shopping season kicks into higher gear over the Thanksgiving weekend, the health of the U.S. consumer will again be tested as the November vehicle sales (Wednesday, December 1) and November chain store sales (Thursday, December 2) are released.

As we have been outlining in these pages throughout 2010, expectations for the consumer heading into 2010 were low. A year ago, the questions around the consumer were not about how much the consumer could spend in 2010, but how much debt they could pay down or how much money they could save. As it turns out (and as we have been pointing out all year) the consumer has been able to do all three of these things—spend a little, pay down debt, increase saving—as 2010 progressed.

Many market observers also missed the idea that “consumers” were not a single entity. The high-end consumer has seen somewhat of a resurgence, while the low- and middle-end consumers have struggled a bit more.

This week’s reports on vehicle sales and chain store sales in November are likely to continue the themes we have seen throughout 2010. Aided by a better labor market, low interest rates, and an improved financing backdrop, vehicle sales are likely to come in above the 12.0 million annualized sales pace in November for the second consecutive month. Although vehicle sales surged to a 14.2 million annualized sales pace in August 2009, as the government-sponsored “cash for clunkers” program boosted sales, vehicle sales have not been consistently above 12 million units since before the collapse of Lehman Brothers in September 2008. Vehicle sales spent most of the mid-2000s in the 16 to 17 million range, peaking at 21 million in July 2007. A return to sales consistently above the 12.5 million range would be yet another sign that the consumer is beginning to find its footing after more than two years of unsteadiness.

3 At Around A 12 Million Annualized Pace, Vehicle Sales Remain 25% Below Their Mid-2000s Pace



Source: Bureau of Economic Analysis/Haver Analytics 11/29/10
(Shaded areas in chart indicate recessions)



IMPORTANT DISCLOSURES

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Purchasing Managers Index (PMI) is an indicator of the economic health of the manufacturing sector. The PMI index is based on five major indicators: new orders, inventory levels, production, supplier deliveries, and the employment environment.

Quantitative Easing is a government monetary policy occasionally used to increase the money supply by buying government securities or other securities from the market. Quantitative easing increases the money supply by flooding financial institutions with capital in an effort to promote increased lending and liquidity.

The ISM index is 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.

The Federal Reserve is the central bank of the United States. Its unique structure includes a federal government agency, the Board of Governors, in Washington, D.C., and 12 regional Reserve Banks (Atlanta, Boston, Chicago, Cleveland, Dallas, Kansas city, Minneapolis, New York, Philadelphia, Richmond, San Francisco, and St. Louis).

The NY Empire State Index is a seasonally-adjusted index that tracks the results of the Empire State Manufacturing Survey. The survey is distributed to roughly 175 manufacturing executives and asks questions intended to gauge both the current sentiment of the executives and their six-month outlook on the sector.

Challenger, Gray & Christmas is the oldest executive outplacement firm in the United States. The firm conducts regular surveys and issues reports on the state of the economy, employment, job-seeking, layoffs, and executive compensation.

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