

Weekly Economic Commentary

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ECONOMIC CALENDAR

Tuesday, Jun 1 Construction Spending <i>Apr</i>	Thursday, Jun 3 ADP Employment Report <i>May</i>
ISM Manufacturing <i>May</i>	Productivity <i>Q1</i>
Wednesday, Jun 2 Domestic Light Vehicle Sales <i>May</i>	Initial Claims <i>wk 05/29</i>
Challenger Job Cut Announcements <i>May</i>	ISM Service Sector <i>May</i>
Pending Home Sales <i>Apr</i>	Factory Orders <i>Apr</i>
	Chain Store Sales <i>May</i>
	Friday, Jun 4 Nonfarm Payrolls <i>May</i>
	Unemployment Rate <i>May</i>

Highlights

- Markets largely ignored last week's economic data in the United States even as it continued to show that a successful transition to sustainable growth was underway.
- The May employment report is the marquee report in a very busy week of data, but will markets look past the data again this week?

Does the Economic Data Matter?

Last week's batch of economic data for April and May in the U.S. came in better than expected, including:

- New and existing home sales,
- Home prices,
- Consumer confidence,
- Shipments and orders for durable goods,
- First time filings for unemployment insurance, and
- Inflation.

Taken together, the data suggest that the U.S. economy continued to make a successful transition from recovery to sustainable growth as the first quarter of 2010 ended and the second quarter began. Financial markets, however, are forward looking and largely ignored last week's data, focusing instead on the potential damage the European debt contagion may have on global growth later in 2010.

The U.S. economy's transition from recovery to sustainable growth has been called into question by the flare-up of the European debt problem and its potential impact on global economic growth. On the one hand, the U.S. banking system is relatively insulated from Europe's debt woes. However, the U.S. export sector, and in turn, business capital spending, may be vulnerable to both a pull back in global growth that could result from a post Lehman-like freeze of global liquidity and trade, and a return to recession in the Eurozone as a result of cuts in government spending and higher borrowing costs.

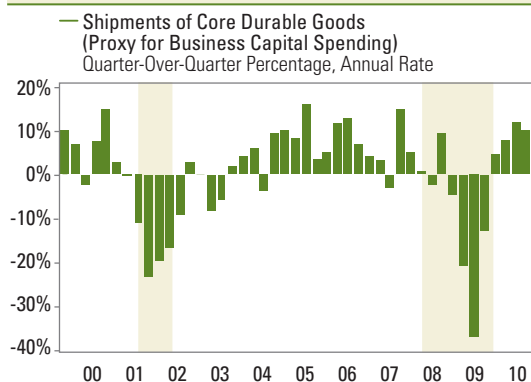
For now, we are sticking to our forecast for 3–4% real Gross Domestic Product (GDP) growth in the United States in 2010. The consensus outlook for U.S. GDP growth, at 3.2%, has moved much closer to our view in recent months. We continue to expect stronger GDP growth in the United States in the first half (3–5%) of 2010, and then a slowdown in the second half (2–3%). However, a prolonged period of elevated global liquidity concerns and an outright return to recession in Europe, among other factors, would cause us to revisit our thesis on the U.S. economy over the rest of 2010.

A few of the economic reports released last week deserve a closer look, including the report on durable goods orders and shipments for April and a report on global growth from the Organization of Economic Cooperation and Development (OECD), a global think tank representing 31 developed nations.

The April data on durable goods (manufactured goods expected to last at least three years) suggests that the business spending and export-led recovery



1 Business Capital Spending Got off To Solid Start in Q2



Source: Census Bureau, Haver Analytics 06/01/10
Shaded areas represent recessions.

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continued in the first month of the second quarter of 2010. Core durable goods orders, a good leading indicator of future business spending, were running 11% ahead of their first quarter average in April, and are on track to post their fifth consecutive quarter-over-quarter gain, a healthy sign of an economy transitioning from recovery to sustainable growth. Core durable goods shipments—a good real-time indicator of current capital spending—were running 10% ahead of their Q1 average in April, suggesting another solid contribution to real GDP growth from business capital spending in Q2. Although inventory restocking had been a major factor in contributing to the gain in business spending since mid-2009, exports have also been a big driver. The recent turmoil in Europe has the potential to slow global growth and, in turn, U.S. exports. We will continue to monitor the leading indicators of business spending and exports closely.

A report last week from the OECD lent support to the idea that the turmoil in European debt markets will not torpedo global growth in 2010 or 2011. The OECD, in the June version of its bi-annual forecast, said that GDP across the 31 OECD countries is projected to rise by 2.7% this year and by 2.8% in 2011. These are upward revisions from the November 2009 forecasts of OECD-wide GDP growth of 1.9% in 2010 and 2.5% in 2011. Notably, the OECD now expects Europe to grow at just 1.2% in 2010 and by 1.8% in 2011. Those forecasts are little changed from the December 2009 OECD Outlook publication, suggesting that the OECD sees very little impact on European economies as a result of the still-unfolding European fiscal problems. As an aside, the OECD expects growth in non-OECD nations (Emerging Markets) to be 4.0% this year and 3.9% in 2011.

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

Despite a calendar that is chock full of crucial data for April and May on manufacturing, vehicle sales, chain store sales, and construction, markets may once again look past the near-term data on the U.S. economy, and focus on what, if any, long-term damage is being inflicted on global growth as a result of the slowdown in Europe. The aforementioned reports due out early this week will largely be a sideshow to the reports due out late in the week on the health of the labor market in May.

The market is expecting another robust gain in private sector employment in May (the 6th in the past 7 months), but the question is will the markets dismiss the data as old news.

On the policy front this week, while there are a number of Federal Reserve officials slated to make public appearances, Fed chairman Ben Bernanke is not one of them. Treasury Secretary Tim Geithner is scheduled to attend a meeting of the G-20 in South Korea. There are several global central bank meetings this week. As this report was being published, the Bank of Canada, as expected, raised its overnight lending rate by 0.25 basis points to 0.50, the first G-7 nation to raise rates in this cycle. The Reserve Bank of Australia (RBA) also met on Tuesday, June 1, and, as expected kept its policy rate unchanged. The RBA has been tightening policy in steady increments since September 2009. There are also several less influential central bank meetings this week (Indonesia,



Top 10 Months for Nonfarm Job Growth

Month	Month-over-Month Increase in Employment
September 1983	1,088,000
March 1946	962,000
August 1952	797,000
January 1946	754,000
April 1946	713,000
May 1941	657,000
August 1950	637,000
April 1978	636,000
August 1956	632,000
March 1950	502,000

Source: Bureau of Labor Statistics; Haver 6/01/10

Thailand, the Philippines, and Romania). The next event for the Federal Reserve is the release of the Beige Book—a qualitative assessment of economic conditions in the 12 Federal Reserve districts—that is prepared for each meeting of the Federal Open Market Committee (FOMC). The Beige Book is due out on Wednesday June 9. The next FOMC meeting is slated for June 28.

Looking ahead to the May jobs report (due out Friday, June 4), the odds that we get a blowout jobs report in May are still pretty high. The U.S. government plans to hire around 600,000 temporary workers to conduct the 2010 Census. At the end of April, only 208,000 Census workers were on the government payroll. This suggests that Census-related payrolls will increase by close to 400,000 in May versus April. At the same time, the consensus is looking for a 175,000 gain in private sector employment in May, (after the 231,000 gain in private sector jobs in April). Thus, the headline reading on overall job creation in May could approach 600,000. Of course, the market will only focus on the private sector figure, as the Census workers will begin to be a drag on the overall payroll job count in June.

Even though the large majority of the jobs created in May will be temporary Census jobs, that kind of number will be hard to ignore for the Fed, the markets, and in particular, for the general public. It also may have political implications as we head into primary season, and closer to the midterm elections in November.

For perspective, the table below is the top 10 months ever for nonfarm job growth, many of these gains were one-offs, related to war, strikes, etc.

- The big gains in 1941 and 1946 were impacted by gyrations related to strikes and the wind up (and then wind down) of WWII production.
- The big gain in August 1952 was also a snapback from strikes, as was the big gain in August 1956.
- The 636,000 gain in jobs in April 1978 was in part due to the end of a five-month strike by coal miners.
- The 1 million gain in jobs in September 1983 was a rebound from the AT&T strike in August 1983.

Thus the potential gain in overall employment in May 2010 vs. April 2010 could be one of the largest (non-strike, non-wartime) job gains ever, not taking into account the size of the labor force, which is of course much larger today than it was in the 1950s or even the late 1970s.



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The Organization of Economic Cooperation and Development (OECD) brings together the governments of countries committed to democracy and the market economy from around the world to support sustainable economic growth, Boost employment, raise living standards, maintain financial stability, assist other countries' economic development, and contribute to growth in world trade.

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