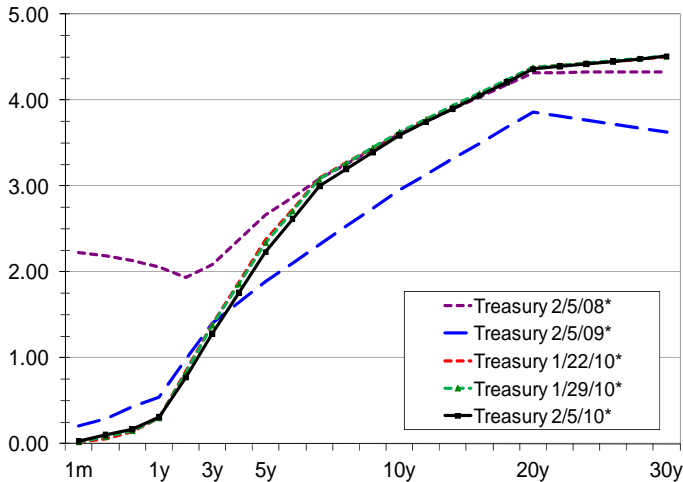
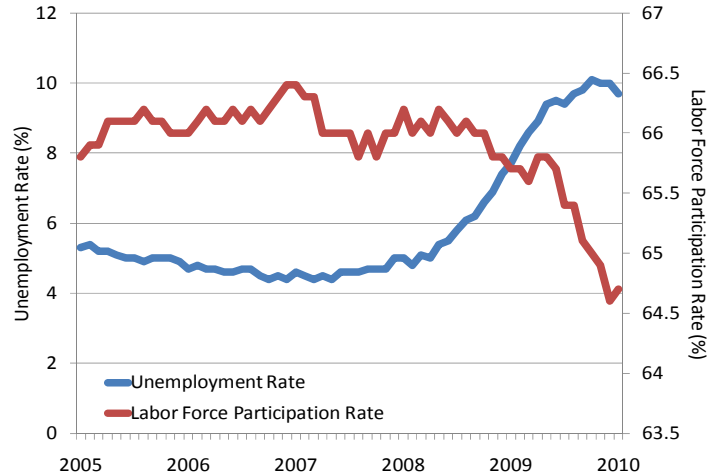




The Big Picture: Yield Curve & Unemployment



U.S. Treasury Yield Curve—Source: U.S. Department of the Treasury









Unemployment and Labor Force Participation Rate—Source: Bureau of Labor Statistics

Measure	Numerical Trend	Current Trend	Commentary
Employment January 2010 www.bls.gov/news.release/empsit.nr0.htm	<i>Payroll Gain</i> <i>Thousands</i> <i>Seasonally Adjusted</i> Jan 10: -20 Dec 09: -150 Jan 09: -779		Non-farm payrolls declined for the 24 th time over the past 25 months, but January's decline was relatively modest. The service sector added 40,000 jobs, boosted by an increase of 42,100 jobs in retail and 52,000 new temp jobs. While the goods producing sector lost 60,000 jobs, manufacturing payrolls grew by 11,000 (1 st net gain in 3 years). Data revisions added 620,000 to the total number of 2009 net job losses. Based on a separate household survey, the unemployment rate fell 3/10 ^{ths} of a percentage point to 9.7%. The same household survey showed the labor force growing by 111,000 workers (1 st increase since August).
Factory Orders (Revised) December 2009 www.census.gov/indicator/w/m3/	<i>Nondurable New Orders</i> <i>Percentage Change from Previous Month</i> <i>Seasonally Adjusted</i> Dec 09: +1.0% Nov 09: +2.2% Dec 08: -4.9%		The 1.5% increase in durable goods orders was revised upward from the initial estimate of +0.3% largely due to an upward revision in computers and electronic products orders. Orders of non-durables increased 1.8%. Shipments jumped 1.9%, including a 2.9% surge in durable goods shipments. Inventories contracted by 0.1% as the 0.2% decline in durable goods inventory counterbalanced the 1.4% increase in nondurables inventories.

Source: Bureau of Labor Statistics

Source: Census Bureau

<p>Vehicle Sales January 2010 www.motorintelligence.com/m_frameset.html</p> <p><i>Source: individual automakers via Autodata, Corp.</i></p>	<p><i>Millions Seasonally Adjusted Annualized Rate</i></p> <p>Jan 10: 10.78 Dec 09: 11.25 Jan 09: 9.62</p>		<p>Vehicle sales declined slightly in January, hurt particularly by the issues impacting certain Toyota automobiles. Net of Toyota (-11% year-to-year), sales increased (on a SAAR basis) during the month. Monthly sales for GM and Nissan grew while they slowed for Ford and Honda on a seasonally adjusted basis. Overall sales were 12.1% above that of January 2009, including a 21.6% jump for autos and a 3.1% increase for light trucks.</p>
<p>Personal Income December 2009 www.bea.gov/newsreleases/national/pi/pinewsrelease.htm</p> <p><i>Source: Bureau of Economic Analysis</i></p>	<p><i>Personal Income Percentage Change from Previous Month</i></p> <p>Dec 09: +0.4% Nov 09: +0.5% Dec 08: -0.3%</p>		<p>The increase in personal income was the result of retroactive social security benefit payments made due to “a recalculation of the earnings base” for recent retirees. Wage and salary income grew just 0.1%, versus a 0.4% increase in November. Consumption increased 0.2%, boosted by a 0.5% jump in spending on services (e.g., utilities). Spending on durable goods was flat while that for non-durable goods fell 0.6%. The savings rate grew 3/10^{ths} of a percentage point to 4.8%.</p>
<p>Construction Spending December 2009 www.census.gov/ftp/pub/construction/www/c30index.html</p> <p><i>Source: Census Bureau</i></p>	<p><i>Percentage Change from Previous Month Seasonally Adjusted Annualized Rate</i></p> <p>Dec 09: -1.2% Nov 09: -1.2% Dec 08: -3.4%</p>		<p>Construction spending slid to \$913.2 billion SAAR. Private construction also declined 1.2% during the month as residential construction fell 2.8% while non-residential construction grew 0.2%. Public construction contracted 1.2% to \$209.6 billion. Overall construction spending remained 9.9% below year-to-year levels. Private construction was 14.9% under that of December 2008 while public construction spending was 1.3% higher.</p>
<p>Productivity 4th Quarter 2009 www.bls.gov/news.release/prod2.toc.htm</p> <p><i>Source: Bureau of Labor Statistics</i></p>	<p><i>Non-farm Business Output per Hour Seasonally Adjusted Annualized Rate</i></p> <p>09 Q4: +6.2% 09 Q3: +7.2% 08 Q4: -0.8%</p>		<p>The rise in productivity was a result of a 7.2% spike in output that was supported by only an 1.0% increase in hours worked. Unit labor costs fell 4.4%. Manufacturing productivity grew 7.8%; with a 6.1% increase in output and 1.6% drop in hours worked. Unit labor costs plummeted 7.4%. Productivity during Q3 was revised down from 8.1% to 7.2%, with a downward revision in output and an upward revision in hours worked.</p>
<p>ISM-Manufacturing January 2010 www.ism.ws/ISMReport/index.cfm</p> <p><i>Source: Institute for Supply Management</i></p>	<p><i>Manufacturing Index Seasonally Adjusted</i></p> <p>Jan 10: 58.4 Dec 09: 54.9 Jan 09: 35.5</p>		<p>The manufacturing index improved in January largely due to a spike in production. This was the biggest increase since 2004 and the 6th consecutive month in which the index was above the 50-point expansionary threshold. The index for new orders rose to 65.9, its highest level since December 2004. The employment index increased from 3.1 points to 53.3.</p>
<p>ISM-Non Manufacturing January 2010 www.ism.ws/ISMReport/index.cfm</p> <p><i>Source: Institute for Supply Management</i></p>	<p><i>Non-Manufacturing Index Seasonally Adjusted</i></p> <p>Jan 10: 50.5 Dec 09: 49.8 Jan 09: 42.9</p>		<p>Unlike the manufacturing sector above, the service sector remains rather sluggish as the composite index struggles to stay above 50.0. The index for new orders grew 2.7 percentage points to 54.7 while the index for employment index increased 1.6 points to a still contracting reading of 44.6. The 4 of 19 tracked industries that reported growth were utilities, information, wholesale trade and “other industries.” 11 other industries contracted.</p>

Economic Commentary edited by Kevin Roth

The U.S. economy lost another 20,000 jobs on a net basis in January as growing business activity slowed but did not reverse the contraction in payrolls that has occurred in 24 of the past 25 months. But January was the second month in the past three in which the labor market showed solid signs that it has likely hit a bottom. While the number of net job losses in December was revised upwardly (to 150,000), so was November's net job gain (+64,000). And, while payrolls in the goods-producing sector of the economy contracted for the 35 consecutive month, manufacturing payrolls grew for the first time since January 2007 (+11,000).

Even more hopeful was the addition of 52,000 temporary help service workers, who employers tend to increase their use of prior to permanently expanding payrolls. The BLS noted that the number of temp workers has risen by nearly a quarter of million since its low point last September. Overall service sector payrolls grew by 40,000 workers, where in addition to the jump in the use of temporary workers, retail payrolls increased by 42,000 while education/health services added 16,000 workers. Government payrolls declined by 8,000 workers, as a decline in state and local government workers outweighed a gain of 33,000 workers at the federal level (including 9,000 temporary positions to support the 2010 Census).

Whereas the data presented above comes from a survey of establishments, the headline result from the accompany household survey had the unemployment rate falling 3/10^{ths} of a percentage point to 9.7 percent as the number of unemployed workers fell by 430,000 (the third consecutive monthly decline). Also, the number "involuntary part-time workers"—part-time workers who had seen their hours cut back or were unable to find full-time work—fell from 9.17 to 8.32 million in January, its lowest reading in a year. Even the broadest measure of labor underutilization released by the BLS declined. The total number of unemployed workers, plus the sum all persons marginally attached to the labor force and those who are involuntary part-time workers, as a percentage of the civilian labor force plus all persons marginally attached to the labor force fell from 17.3 percent to 16.5 percent.

Factory orders increased for the ninth time over the past 11 months in December as orders for durable and

non-durable goods both increased. Experiencing the biggest increase in orders was machinery, up 6.6 percent for the third rise over the past four months. Orders were 3.3 percent above levels of December 2008. Shipments of manufactured goods increased for the sixth time in seven months (+1.9 percent) and were 2.9 percent above year ago levels.

The improvement in the manufacturing sector was further supported by a closely watched survey on the sector. The Institute for Supply Management reported last week that the manufacturing sector expanded for the sixth consecutive month in January, at least according to the key metric of its Manufacturing Report on Business. The Purchasing Managers' Index increased 3.5 points to 58.4, its highest reading since August 2004. Any reading above 50.0 suggests expansion and, in noting the six month streak above the threshold, the press release stated that January's reading "provides significant assurance that the manufacturing sector is in recovery."

Thirteen of 18 tracked manufacturing industries reported growth in the January survey with the best performers being apparel, leather products, textile mills, and machinery. Only one industry—furniture—reported a decline in business activity. Among key components of the PMI: production jumped 6.5 points to 66.2, new orders grew 1.1 points to 65.9 and employment increased 3.1 points to 53.3. The ISM report on non-manufacturing suggests that the service sector has not been growing at same robust pace as has manufacturing. The headline index increased to just over the 50.0 threshold to 50.5.

Financial institutions did not further tighten lending standards during the fourth quarter of 2009, but few banks actually loosened such standards during the same period. This was the key finding of the most recent Senior Loan Officer Opinion Survey on Bank Lending Practices from the Federal Reserve released last week. Fifty-two of 55 banks that participated in the survey indicated that their credit standards for approving applications for commercial & industrial loans or credit lines had "remained basically unchanged" while three banks noted that credit standards had actually loosened during the final three months of the year. In past surveys, the bias was significantly towards significant

tightening. Of lines of credit offered, terms were unchanged from the third quarter in terms of: credit line size, maturity, costs, spreads over banks' cost of funds, risk premiums, loan covenants and collateralization requirements.

Further, a small net fraction of banks increased rather than decreased their willingness to make consumer installment loans during the end of 2009 (11.5 percent versus 1.9 percent). This was the first time in nearly three years in which banks were more willing than not to make consumer installment loans. For 86.5 percent of banks, their willingness to make consumer installment loans was unchanged while 91.7 percent of banks had maintained credit standards for approving credit card applications. Similarly, 79.2 percent of banks maintained credit standards on residential mortgages made to "prime" customers while 70.6

percent of banks did the same for their "non-traditional" mortgage customers.

(<http://www.federalreserve.gov/boarddocs/SnLoanSurvey/201002/table1.htm>)

Construction spending fell 1.2 percent in December, following an identical decline in November, as spending in both the public and private sector fell by matching percentages (-1.2 percent). Spending on residential construction slumped 2.8 percent during the month—the sharpest decline since May—hurt by the passing of the original deadline for the first-time homebuyer tax credit and severe weather conditions towards the latter half of the month. Spending on the non-residential sector increased for the first time since March (+0.2 percent). Year-to-year, construction spending was off 9.9 percent, including a sharp 14.9 percent fall off in the private sector.

***The Week in Corporate Finance* edited by Brian Kalish**

Back in 2002, when the University of Maryland was making its run at the NCAA men's basketball championship, the term "Fear the Turtle" became popular. It was a reference to the less-than-frightening school mascot, the Terrapin. This week, a significantly more frightening chant heard around the world, which was "Fear the PIGS". With the "PIGS" being a reference to the countries of Portugal, Ireland and Italy, Greece and Spain.

We witnessed a great bit of uncertainty in the global markets as participants around the world were greatly concerned about the potential of a credit event in one or more of these European Community members. We watched as absolute credit spreads and credit default spreads continued to widen and as debt and equity deals were delayed and postponed.

There are two concerns at work here. The first one is a flat-out credit event, and the second one is a bit more subtle: that being a general slowdown of the European economy and a weakening of the Euro.

While the focus has certainly been on Europe, given the interdependencies of worlds' economies, the effects of this risk uncertainty are being felt around the world, from Tokyo to Toronto, from Boston to Buenos Aires.

We saw a classic flight-to-quality trade take place on a macro scale. There was a move away from risk to safety. The world's stock markets sold off, commodity prices dropped, and money moved away from all but the safety fixed-income securities. US Treasury securities were the beneficiaries of this desire for safe and simple securities, especially on the shorter end of the maturity curve.

Here in the USA, we continue to receive mixed signals on the state of the economy and what may lay ahead for US businesses.

The jobs report continues to indicate a weak economy at best. We suffered our 16th bank failure this week. The continuing concern is that we may witness 100-200 more failures this year.

On the other hand, given the improvements in the economy and the functionality of the financial markets, the Fed has wound down four of its emergency liquidity programs this week. Probably the best known of the programs is the Commercial Paper Funding Facility (CPFF). At its peak, the CPFF had approximately \$350 billion in assets.

We seem to be alternating between an extreme of emotions, either elation or despair. The cause of this volatility is simple, uncertainty. As we bump along out of the worst financial crisis in seventy years, there is a severe lack of clarity as to what lays next for us.

We will continue to sweep the horizon in order to gain insight as to where we are heading and how we can best maximize the opportunities and minimize the risk.

What to watch over the next week:

Monday, February 8, 2010

- *No new reports*

Tuesday, February 9, 2010

- Job Openings and Labor Turnover (www.bls.gov/jlt/)
- Wholesale Trade (www.census.gov/wholesale)

Wednesday, February 10, 2010

- International Trade (www.census.gov/foreign-trade/www/press.html)
- Treasury Budget (www.fms.treas.gov/mts/)

Thursday, February 11, 2010

- Retail Sales (www.census.gov/marts/www/marts.html)
- Business Inventories (www.census.gov/mtis/www/current.html)
- Metro Prices (www.realtor.org/research/research/metroprice)

Friday, February 12, 2010

- Univ Mich Consumer Sentiment (customers.reuters.com/community/university/default.aspx)



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