

ECONOMIC & MARKET UPDATE: MARCH 28, 2011 "A CENTRAL BANK CAGE MATCH"

Economic Data - Previous Week

Date	Series	Actual	Survey	Prior	
3/21	Existing Home Sales	4.88M	5.12M	5.40M	Existing home sales fall 10%, supply at 8.6 mos
3/23	New Homes Sales	250K	290K	301K	Sales fall to record low, prices lowest since 2003
3/24	Durable Goods Orders	-0.9%	1.1%	3.6%	New orders surprisingly weak, led by transportation
3/25	GDP - Q4 Final	3.1%	3.0%	2.8%	Inventories, non-res fixed invsmt boost final figure
3/25	UMich Confidence	67.5	68.0	68.2	Minimal change after last month's sharp drop

Economic Data - Upcoming Week

Date	Series	Actual	Consensus	Previous	
3/28	Personal Spending	--	0.5%	0.2%	Retail sales data point to increase in expenditures
3/29	S&P/CS 20 City Idx	--	-0.45%	-0.41%	Continued slow decline in home prices anticipated
3/29	Consumer Confidence	--	65.0	70.4	Decline expected due to rising gas and food costs
3/31	Factory Orders	--	0.5%	3.1%	Fall in durables to weigh on overall factory orders
4/1	Nonfarm Payrolls	--	190K	192K	Private job growth to be offset by public job losses
4/1	Unemployment Rate	--	8.9%	8.9%	Consensus looks for no change in headline rate
4/1	ISM Mfg Index	--	61.0	61.4	Little room for expansion from peak levels

Source: Bloomberg

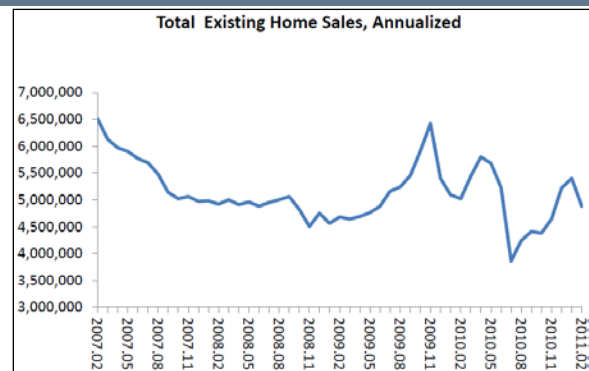
HOUSING SLIDES INTO THE SPRING BUYING SEASON

Equity markets donned the rally cap last week as the S&P 500 index finished higher by 2.7% and the Dow Jones Industrial Average experienced a 3.1% gain.

Stability in the price of crude oil and improvement in Japan lent a helping hand to the markets, as did the announcement that AT&T would buy T-Mobile.

On the domestic front, investors turned a blind eye to the slew of negative economic data. Housing, in particular, experienced the brunt of the disappointment.

Existing home sales offered the first piece of bad news after falling 9.6% to 4.88mln on a seasonally-adjusted annual rate in February.



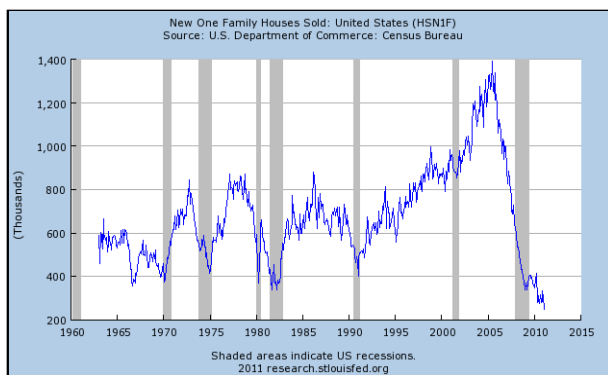
Source: National Association of Realtors

Behind February's decline was what the NAR referred to as "unnecessarily tight credit conditions" and "contract cancellations from some appraisals not supporting prices negotiated between buyers and sellers." Those two issues sent sales prices lower, with the national median existing-home price falling to \$156k in the month. Homes priced below \$100k are one of the few groups to experience a measurable pickup in sales over

|| EVERMAY

the past 12 months, indicative of the role that distressed buyers are presently playing in the market. The NAR said that distressed sales accounted for nearly 40.0% of all existing home sales in February.

A plethora of distressed existing homes on the market is wreaking havoc with new home sales, as well. New single-family homes reached a seasonally-adjusted annual rate of 250k in February, the lowest point in the history of that index.



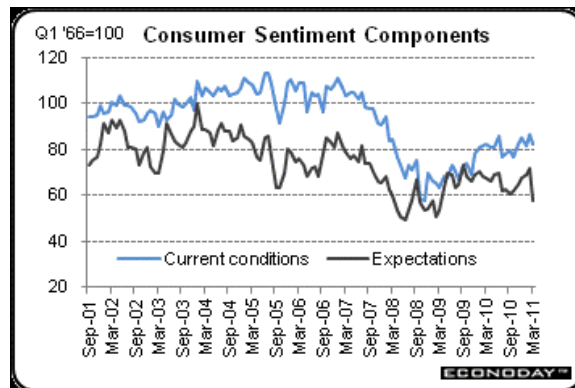
Source: Federal Reserve Bank of St. Louis

February is not a traditionally strong month for home sales in the US, so both releases need to be considered with a grain of salt, but the direction of the home sales trend into the summer months will be very important for the economy.

Consumers are apparently none too happy about the prospect of higher gasoline costs and falling home prices. The Reuters/University of Michigan Consumer Sentiment index fell from 77.5 in February to 67.5 in March.

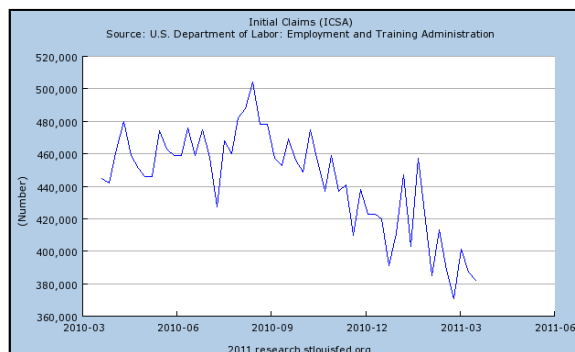
The source of consternation for consumers is not the current state of affairs but rather what may lurk around the corner. The expectations component of the index fell to 57.9 from 71.6 in February. Since the height of the recession

in 2008, the expectations index has been unable to muster any form of sustainable recovery and it seems that the events of 2008 left a lasting impact on consumers' psyche.



Source: Econoday

There was some positive news for consumers last week, in the form of initial claims for unemployment benefits. After breaking through the 400k barrier earlier in the year, weekly initial claims continue to drift lower. In the week ending March 19th, 382k claims were filed, the second lowest reading since the summer of 2008. Continuing claims for unemployment benefits are also pushing to new post-recession lows, reaching the same point as in the fall of 2008.



Source: Federal Reserve Bank of St. Louis

|| EVERMAY

LET THE CENTRAL BANK GAMES BEGIN

Prior to the global financial crisis, many central banks were a misunderstood relic of the economic system. Since the crisis began, however, central banks became an integral part of the day-to-day functioning of the financial markets, and more broadly the economy. As we move past the financial crisis, central banks are in the unsavory role of unwinding support mechanisms while avoiding the throes of a new crisis.

By most measures, the recession is over. That is true in many respects, but the effects of the financial crisis are still being seen in numerous pockets around the globe, be it housing, labor markets or the European debt crisis. In order to combat the lingering hangover from our multi-decade credit binge, central banks, specifically the Bank of England (BoE), the European Central Bank (ECB) and the US Federal Reserve, actively sought to resuscitate the economy from its doldrums and to their credit, those efforts appear to have worked.

Emerging markets, on the other hand, were largely unscathed during the crisis. Yes, there was a notable slowdown in growth, but the time to recovery was relatively short, and emerging market nations are already back on stable ground, with one caveat – inflation.

So, now what?

Central banks in the developed world are not yet ready to signal the all clear and begin tiptoeing away from the markets. There are indications that the exit is moving closer, but thus far, there are no definitive changes in policy. Following its early March policy meeting, for instance, ECB President Jean-Claude Trichet said that “an increase in interest rates at the next meeting (April 7th) is possible.”

According to the markets, though, at least one rate hike in the EU is a foregone conclusion, but US hikes are not likely to happen any time soon. In fact, there is less than an 8% chance that overnight interest rates will change by early August and a 26.0% chance of a rate hike by December. Those percentages are actually trending lower since the start of the year as traders grapple with a sluggish recovery and the realization that the Fed is in no hurry to change its stance.

The BoE is in a tighter bind than the US at the moment. Inflation in England currently stands at 4.4% over the past year, more than double the target 2.0% rate. At the March 9th and 10th monetary policy meeting, three committee members out of nine voted against holding rates at 0.5%. One committee member went as far as indicating that a 50 basis point rate increase was warranted.

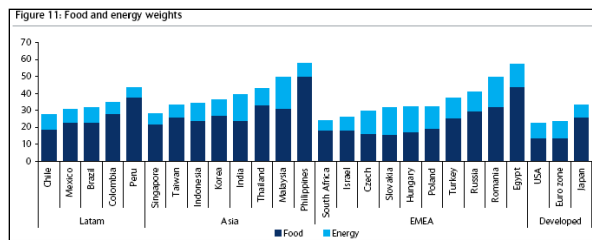
Loose monetary policy in the developed world is making the situation in emerging markets more complicated by the day. Of the 21 countries in the MSCI Emerging Market index, the overwhelming majority are in the process of tightening monetary policy.

China, for example, is attempting to cool its economy by soaking up excess liquidity from its banking system. For the third time this year, the People’s Bank of China increased the bank reserve requirement ratio by 50 basis points to 20.0%. For every dollar deposited in Chinese banks, 20.0% is now required to be set aside at China’s central bank.

The difficulty in managing monetary policy for emerging market central banks is that food and energy costs represent a far greater outlay in those economies.

|| EVERMAY

In countries such as the Philippines, food and energy is a more than 50.0% weight in its inflation index. For the largest emerging market economies, Brazil and Korea, in particular, food and energy is roughly 30% of inflation. By comparison, food and energy accounts for less than a 20.0% weight in the US consumer price index.



Source: *Barclay's Capital*

As pressure builds around the globe, it is important to remember the Federal Reserve's mandate: "maximum employment, stable prices and moderate long-term interest rates." With domestic labor markets stagnating and

consumer prices largely stable, there is no reason to suspect a suddenly aggressive policy mantra will be in the Fed's future. This will inevitably spill over into the emerging markets and create the possibility of new asset bubbles. Central bankers in those emerging market economies are well aware of what is occurring.

The global economy is more closely interwoven than at any time in history. Managing rampant inflation and excess liquidity becomes increasingly difficult for emerging market central banks when their developed equivalents are hesitant to turn off the spigots. Without a clear policy directive from developed nations, emerging market countries will likely be caught in a tumultuous cycle of inflation and asset bubbles.

THE WEEK AHEAD

Two key reports will be released in the US this week – nonfarm payrolls and the ISM Manufacturing index for March. Initial claims for unemployment benefits fell in each of the past three weeks, setting the stage for an improved labor report. Manufacturing is unlikely to experience a major slowdown considering that the new orders index remains well within expansionary territory but there is a modest deceleration expected given the heightened level at which that index currently stands.

Several Treasury auctions are scheduled for this week, including \$35bln of 2-yr notes (Monday), \$35bln of 5-yr notes (Tuesday) and \$29bln of 7-yr notes (Wednesday).

The only corporate earnings report of note this week is Family Dollar on Wednesday.

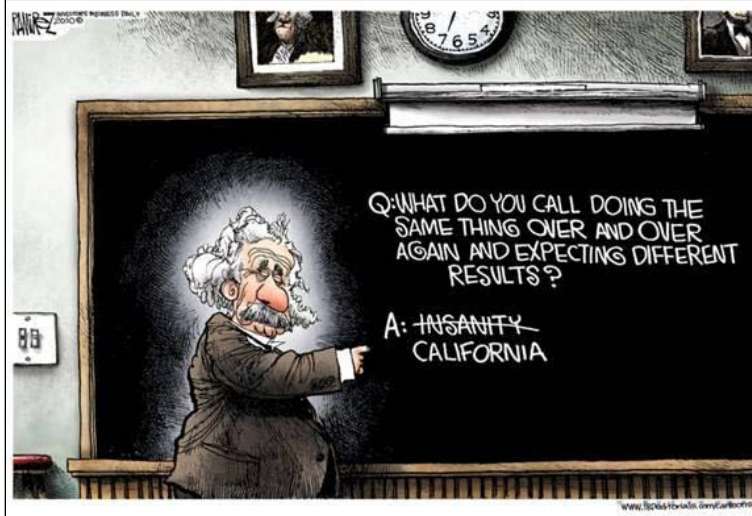
Taiwan's central bank meets on Thursday with economists anticipating a 12.5bps rate

hike. Global manufacturing indices will be released on Friday and modest slowing is expected.

Portugal, a country where the cost of debt financing has skyrocketed in recent weeks, will be acutely in the crosshairs in the upcoming week. Portugal is resisting calls to accept a bailout from the European Union, but its attempts to avoid a dreaded bailout look less and less likely following a ratings downgrade by Standard & Poor's. Portuguese Prime Minister Jose Socrates came under fire after his proposed austerity package was voted down last week. Portugal faces a cumulative \$12.8bln worth of bond redemptions in mid-April and June. Bond maturities in April are not expected to present a problem, but those in June could prove far trickier. Analysts believe Portugal will require a bailout on the order of €70bln should Portugal elect to go down that route.

|| EVERMAY

LIGHTER SIDE



Source: *Global Macro Monitor*

Disclosure Information

Some part of the information contained herein was prepared for Evermay Wealth Management, LLC by employees of Fortigent, LLC. This information is not meant as a guide to investing, or as a source of specific investment recommendations, and Evermay Wealth Management, LLC and Fortigent make no implied or express recommendations concerning the manner in which any client's accounts should or would be handled, as appropriate investment decisions depend upon the client's investment objectives. The information is general in nature and is not intended to be, and should not be construed as, legal or tax advice. In addition, the information is subject to change and, although based upon information that Evermay Wealth Management, LLC and Fortigent consider reliable, is not guaranteed as to accuracy or completeness. Evermay Wealth Management, LLC and Fortigent make no warranties with regard to the information or results obtained by its use and disclaims any liability arising out of your use of, or reliance on, the information.

This report is for illustrative purposes only. Past performance is not indicative of future results. The information contained in this report has been gathered from sources we believe to be reliable, but we do not guarantee the accuracy or completeness of such information, and we assume no liability for damages resulting from or arising out of the use of such information. The performance numbers displayed herein may have been adversely or favorably impacted by events and economic conditions that will not prevail in the future. The indices discussed are unmanaged and do not incur management fees, transaction costs or other expenses associated with investable products. It is not possible to directly invest in an index.

Not FDIC Insured No Bank Guarantee May Lose Value