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ECONOMIC & MARKET UPDATE: APRIL 4, 2011 "EMPLOYMENT MANUFACTURES ANOTHER MONTH OF POSITIVE GROWTH"

Economic Data - Previous Week

Date	Series	Actual	Survey	Prior	
3/28	Personal Spending	0.7%	0.5%	0.3%	Spending up, led by auto sales and higher gas prices
3/29	S&P/CS 20 City Idx	-0.22%	-0.45%	-0.39%	13 of 20 cities showing accelerating price declines
3/29	Consumer Confidence	63.4	65.0	72.0	Poor inflation expectations weigh on optimism
3/31	Factory Orders	-0.1%	0.5%	3.3%	Slight moderation in orders after strong January
4/1	Nonfarm Payrolls	216K	190K	194K	Broad private job growth offset by govt job losses
4/1	Unemployment Rate	8.8%	8.9%	8.9%	Rate edges down, labor participation unchanged
4/1	ISM Mfg Index	61.2	61.0	61.4	Slight moderation from 7 year high

Economic Data - Upcoming Week

Date	Series	Actual	Consensus	Previous	
4/5	ISM Non-Mfg Idx	--	59.5	59.7	Moderation expected from 5 year high in services
4/7	Consumer Credit	--	\$4.8B	\$5.0B	Auto sales to boost non-revolving credit outstanding
4/8	Wholesale Inventories	--	1.0%	1.0%	Little change anticipated in inventory growth

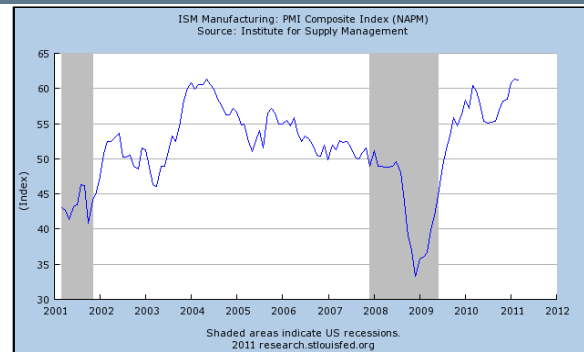
Source: Bloomberg

MANUFACTURING TRIES ITS HAND AT REVIVING THE ECONOMY

Equity markets surged into quarter end, with the S&P 500 index rising 1.4% and the Dow Jones Industrial Average increasing 1.3%. For the first time since February the S&P 500 increased in two consecutive weeks.

After hitting a trough on Tuesday morning, several positive employment reports encouraged the equity markets to move higher.

As expected, manufacturing activity experienced a modest deceleration, as the ISM Purchasing Managers Index (PMI) fell from 61.4% in February to 61.2% in March. Readings above 50% are representative of expansion in the manufacturing sector. Although the index fell slightly, it is still the third highest reading since 1990.

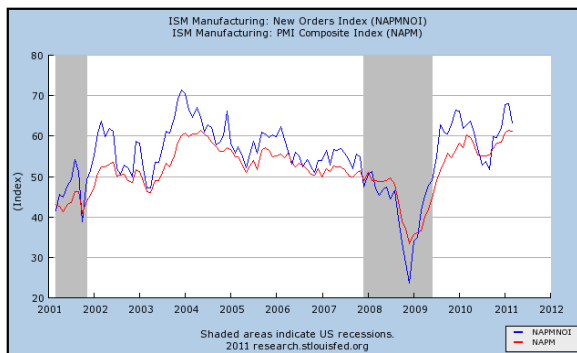


Source: Federal Reserve Bank of St. Louis

Based on a severe drop in the new orders index, a component of the headline PMI, future manufacturing activity is unlikely to stay at this elevated plateau. After reaching 68.0% in February, the new orders index fell to 63.3% in March. That is a robust level, but history suggests that further slowdown is to be expected.

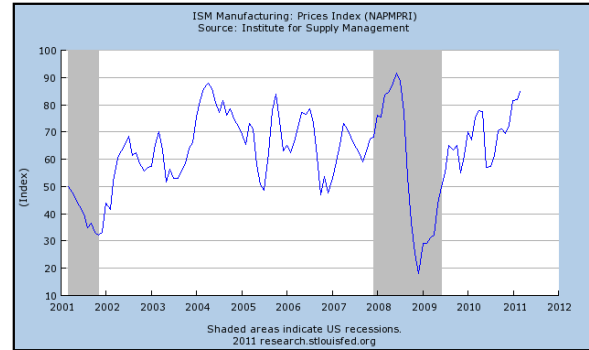
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In December 2009, the new orders index reached a peak of 66.4% before declining nearly 15 points through September 2010. Three months after new orders reached that peak, the PMI reached its own recent high. The ensuing fall lasted four months until the new orders index snapped back. Similar relationships are seen throughout the life of the PMI, notably in periods such as early 2004 and 2006.



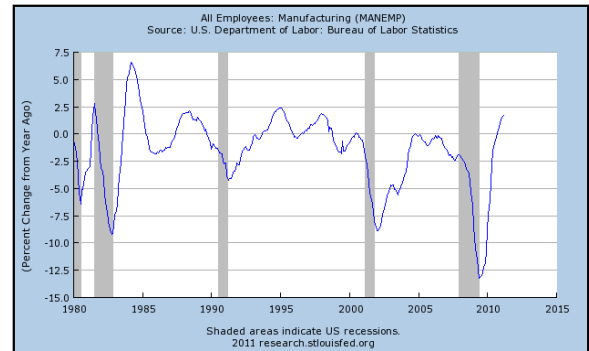
Source: Federal Reserve Bank of St. Louis

Another touchy area for manufacturers is the recent spike in raw material costs. The ISM Prices Paid index hit a staggering 85.0% in March, the highest reading since July 2008. A mere 2% of respondents reported paying lower prices for goods while more than 70% indicated paying higher prices. With little ability to pass costs along to consumers, manufacturers are facing the difficult task of balancing input costs with tepid consumer demand.



Source: Federal Reserve Bank of St. Louis

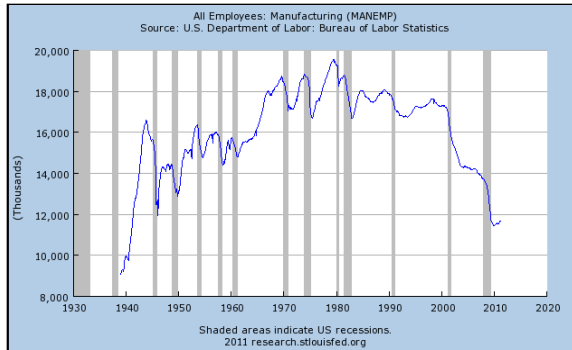
Manufacturing became a focal point for President Obama last August when he signed the Manufacturing Enhancement Act of 2010. The bill was designed to stimulate manufacturing activity and ultimately create jobs in that sector. To some degree the legislation succeeded. During the past 12 months, employment in the manufacturing sector rose 1.7%, the fastest rate of increase since 1998. It is also the first time since mid 2000 that manufacturing is experiencing year-over-year employment growth.



Source: Federal Reserve Bank of St. Louis

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The domestic manufacturing sector draws significant attention in the media, but technological advances and corresponding globalization has reduced the significance of manufacturing within the overall US economy. In the 1970s, more than 19.5mln people in the US worked in manufacturing. By the late 1990s, that figure fell to 17.5mln, and now there are fewer than 12mln. That contraction occurred despite a rapidly growing population, underscoring the United States' transition from a manufacturing to service-oriented economy.



Source: Federal Reserve Bank of St. Louis

JOBS LESS THAN PLENTIFUL, BUT THE TREND IS OUR FRIEND

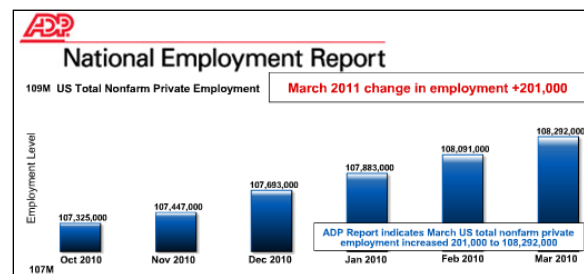
A collective sigh of relief was heard on Friday morning after it was confirmed the labor market grew at a stronger-than-expected rate in March. Traders and economists alike were buying into the recovery story and, ultimately, their confidence seems justified.

Before Friday's nonfarm payroll release from the Bureau of Labor Statistics (BLS), markets were greeted with two mostly positive reports on the health of the US labor market.

First was the ADP National Employment Report. There is generally a strong relationship between ADP's report of private sector payroll growth and similar measures from the BLS, so traders were hopeful when

The good news is that manufacturing is expanding; the bad news is that this pace appears unsustainable. Based on ISM research, the current PMI reading is consistent with a "6.5% increase in real gross domestic product". Few economists believe this rate will be achieved, but it does indicate that the manufacturing sector is doing its best to aid in the recovery process.

ADP reported growth of 201k private sector jobs in March.



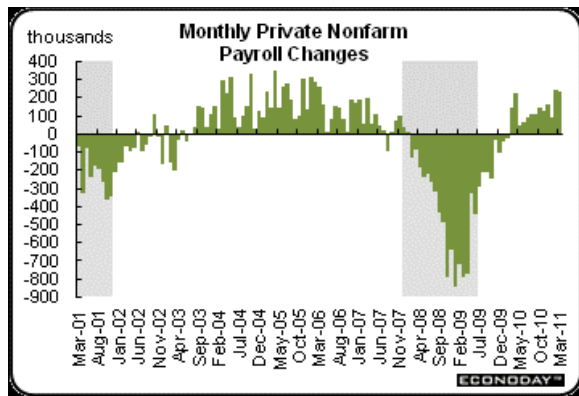
Source: ADP

On Thursday morning initial claims for unemployment benefits were reported to be 388k for the week ending March 26th, below the psychologically important 400k barrier.

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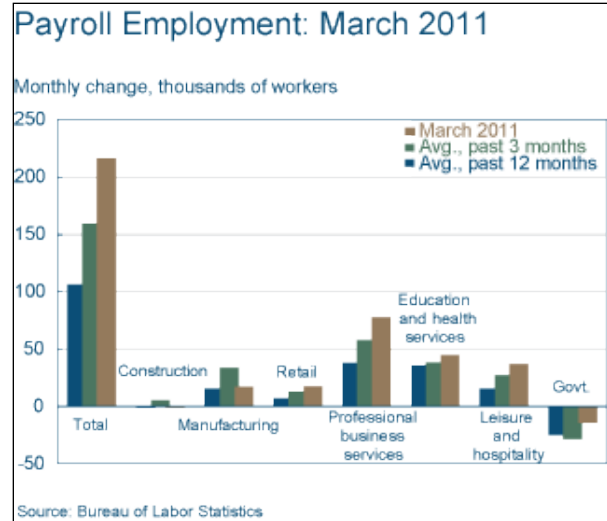
The post-recession economy has struggled to keep initial claims consistently below this 400k level. Continued improvement in jobless claims should boost consumer confidence and lend further credence to the notion that the economy is actually in a sustainable recovery.

On Friday, the BLS reported that nonfarm payrolls grew by 216k in March, while official unemployment dipped to 8.8%. Private payrolls registered growth of 230k during the month.



Source: Econoday

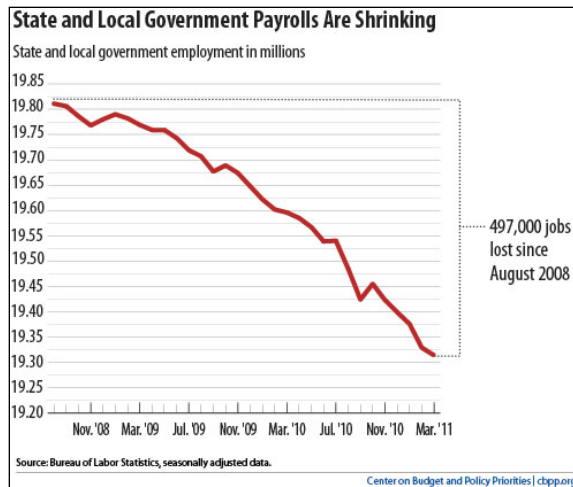
Employment gains were broad-based across multiple sectors, particularly in areas such as the service sector, temporary help, health care, hospitality, manufacturing, and education.



Source: Federal Reserve Bank of Cleveland

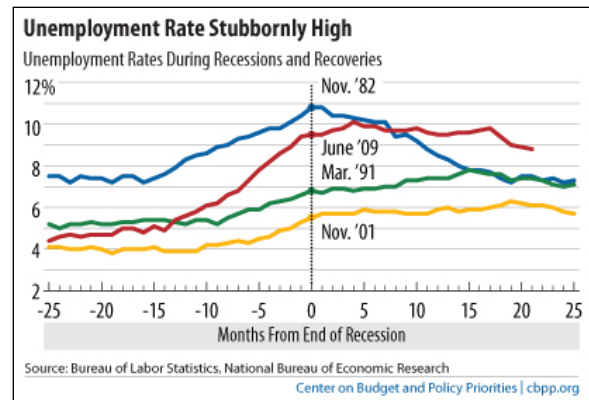
In contrast to this improvement is contracting employment in state and local governments. Another 15k jobs were lost in this sector in March, with the entirety of cuts occurring at the local level. On a cumulative basis, nearly 500k jobs have now disappeared from state and local government payrolls since August 2008. The ongoing fiscal challenges of many state and local budgets are likely exacerbating this trend.

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Source: Center on Budget and Policy Priorities

While the overall unemployment rate fell from 9.4% in November 2010 to 8.8% this past March, it is still tracking at a sluggish pace compared to previous recoveries. Following the 1982 recession, the unemployment rate fell by more than 2% within 12 months. This time around, we are almost two years into the recovery and the unemployment rate has improved by less than 1%. A similar phenomenon was seen in 2002 after the tech bubble burst, but the unemployment rate then was barely above 6%, far lower than where it stands today.



Source: Center for Budget Policy and Priorities

On the whole, the labor report for March was positive, but labor markets are struggling to climb out of an enormous hole. It will take years of moderate-to-strong economic growth before we return to unemployment rates in the 5% range – a rate the US considers “full employment.” With the economy growing at a modest rate, employment will likely continue to move along at its current positive, but underwhelming, pace.

THE WEEK AHEAD

It is a somewhat quiet week for economic releases, but the ISM Non-Manufacturing index is released on Tuesday. That same afternoon the FOMC will release the minutes of its March 15th meeting. Traders are closely watching for any discussion surrounding QE2. Consumer credit for February will be announced on Thursday, with economists expecting a healthy move higher due to rising automotive sales.

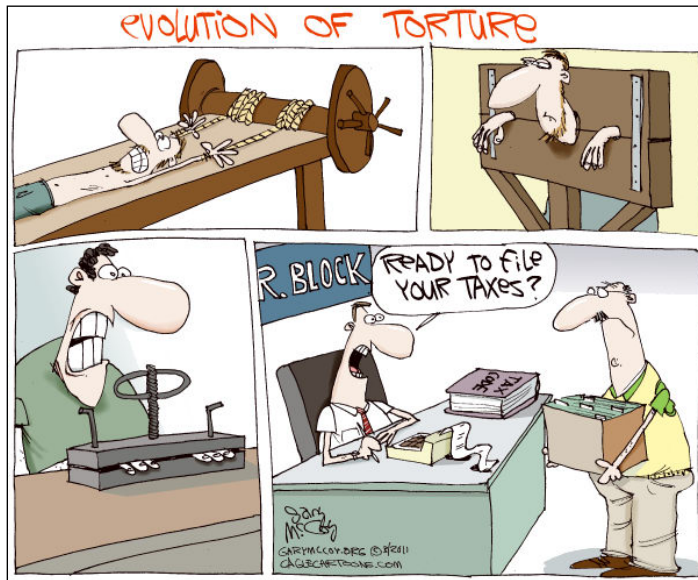
Earnings season unofficially begins with Alcoa’s earnings announcement on April 11th,

but in the meantime several companies worth watching will report. Included on the list are Monsanto, Bed Bath & Beyond, Constellation Brands, and Pier One.

Internationally, central banks from Australia, Japan, UK, and the ECB will meet at various points during the week. Based on comments from ECB President Trichet, traders are looking for the ECB to raise interest rates by 0.25%.

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LIGHTER SIDE



Source: Gary McCoy

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