

ECONOMIC & MARKET UPDATE: MAY 31, 2011
"RECOVERY SHOWS SIGNS OF CRACKING"
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Economic Data - Previous Week					
Date	Series	Actual	Survey	Prior	
5/24	New Home Sales	323K	300K	301K	Surprise uptick after March rebound
5/25	Durable Goods	-3.6%	-2.5%	4.4%	Broad weakness in new orders, -1.5% ex transportation
5/26	GDP - Q1 2nd Est.	1.8%	2.2%	1.8%	Weaker consumer data keeps Q1 GDP unchanged
5/27	Personal Spending	0.4%	0.5%	0.5%	Spending higher, largely due to inflation pressures
5/27	UMich Confidence	74.3	72.4	72.4	Optimism on future conditions supports sentiment

Economic Data - Upcoming Week					
Date	Series	Actual	Consensus	Previous	
5/31	S&P/CS 20 City Idx	--	-0.20%	-0.18%	Continued slow bleed in home prices expected
5/31	Consumer Confidence	--	66.6	65.4	Improvement in gas prices may lift confidence
6/1	Construction Spending	--	0.3%	1.4%	Weak starts report points to modest constr spending
6/1	ISM Mfg Idx	--	57.5	60.4	Moderation expected due to weaker regional surveys
6/3	Nonfarm Payrolls	--	180K	244K	Forecast lower on pickup in initial claims data
6/3	Unemployment Rate	--	8.9%	9.0%	Analysts look for slight improvement in jobless rate
6/3	ISM Non-Mfg Idx	--	54.0	52.8	Slight rebound anticipated after sharp April drop

Source: Bloomberg

CONSUMERS STRUGGLE TO CARRY THE TORCH

Equity markets stumbled again last week with the S&P 500 Index closing down 0.2% and the Dow Jones Industrial Average losing 0.6%.

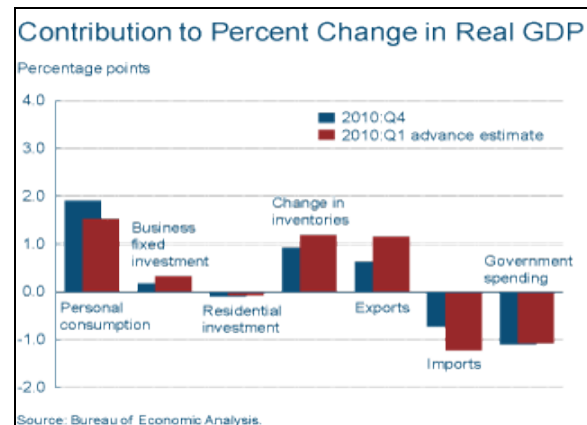
There was a limited amount of economic data released last week, and most of it turned out to be disappointing.

From a broad perspective, the second revision to GDP showed the economy growing at an annual rate of 1.8% in the first quarter, unchanged from the initial estimate.

Though the headline figure was unchanged, several important changes occurred in the underlying data. Specifically, the Bureau of Economic Analysis (BEA) stated that consumer demand actually rose at a 2.2% annual pace in the quarter, down from the 2.7% annual rate initially reported.

In addition, the BEA revealed that an inventory buildup played a larger role in first quarter growth than originally thought.

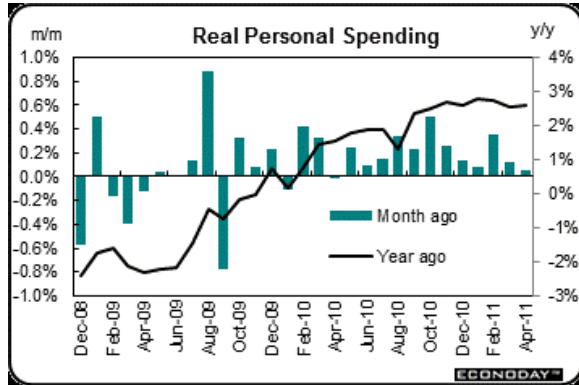
Overall, GDP was weaker than feared in the first quarter as higher inventories and not consumer spending drove expansion. Without a happy and healthy consumer to drive growth, inventories will continue to accumulate at the expense of growth.



Source: Federal Reserve Bank of Cleveland

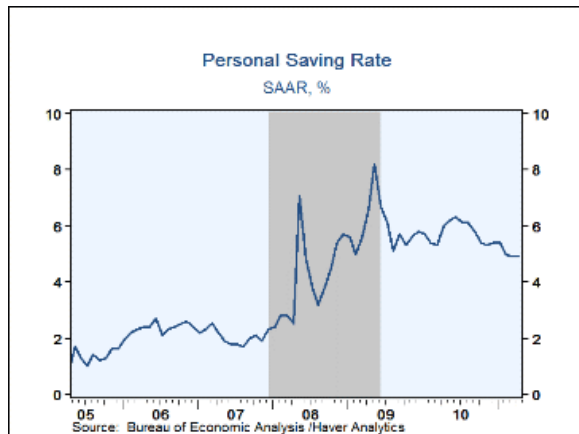
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There are indications that consumer spending is struggling at the start of the second quarter. Personal spending increased a healthy 0.4% in April, but after adjusting for inflation, spending was up a modest 0.1%, following a similar 0.1% gain in March.



Source: Econoday

In order to offset rising costs for food and energy, consumers dipped into savings accounts. The personal savings rate for April held steady at 4.9% but prior months were revised lower, suggesting that consumers relied on savings to combat higher costs.



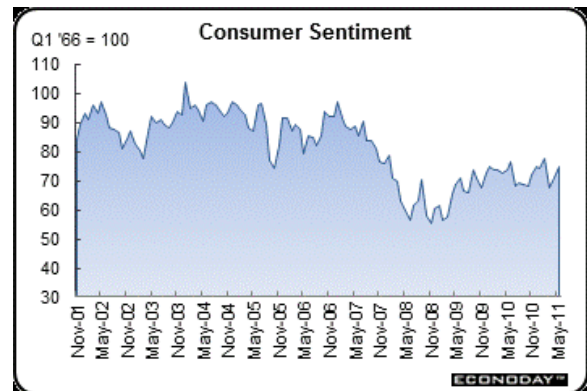
Source: Haver Analytics

The good news, at least temporarily, is that gas costs are easing. AAA reports the current average price for a gallon of gas is \$3.79, down from \$3.93 only one month ago.

Whether those prices will hold is uncertain, but comments from Saudi Arabia over the weekend offer insight into the future. Saudi Prince Al-Waleed bin Talal said the price for a barrel of oil should ideally reside between \$70 and \$80. His primary concern is that the US will eventually move away from its dependence on Saudi oil. The trouble for Saudi Arabia, and eventually the US, is that production costs are trending higher.

Currently, MarketWatch estimates the breakeven price for a barrel of Saudi oil at \$85. By 2015, they project it will climb to \$110.

Consumers are staying resilient despite current economic difficulties. According to the latest University of Michigan Consumer Sentiment Survey, sentiment increased from 72.4 to 74.3 in May. Consumers' view of current conditions fell slightly, but their view of the outlook rose.



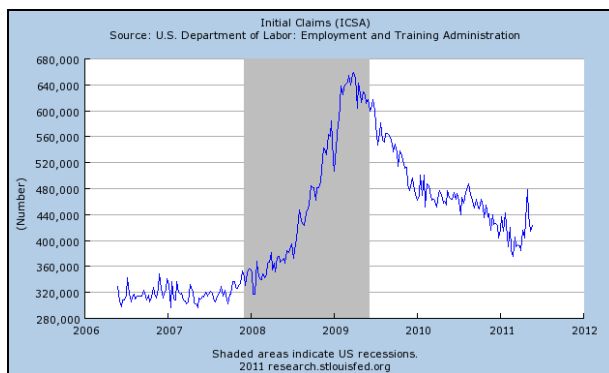
Source: Econoday

Labor remains a touchy area for most consumers. After showing signs of improvement throughout last year and the start of 2011, initial claims for unemployment benefits have started rising over the past two months. There were a number of special factors behind the initial increase, but that was

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not the case this past week, according to the Department of Labor.

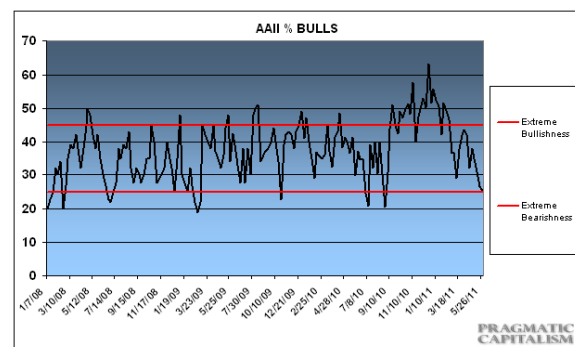
Economists are frustrated that at this point in the recovery the economy is struggling to find sustainable job growth. The upcoming nonfarm payroll report for May is scheduled for release on Friday. It will offer additional insight into the health of the labor market. Based on initial claims data, robust job growth appears to be some ways off.



Source: Federal Reserve Bank of St. Louis

Overriding macroeconomic concerns are fueling investor bearishness on stocks. The latest AAI Sentiment Survey showed that 41.4% of retail investors were bearish on the six-month outlook for stock prices.

That degree of bearishness was last seen in the early fall, just prior to a multi-month rally in stocks. On average, bearish sentiment is 30% and bullish sentiment is 39%. Current sentiment is entering “stretched” territory and indicates that stocks may be ready to rally.



Source: Pragmatic Capitalism

THE WEEK AHEAD

Following a long holiday weekend, there will be a series of important economic releases in the US.

On Friday, nonfarm payrolls for May are announced. Economists are expecting healthy growth around 200,000, but volatility in initial claims for unemployment benefits suggest the report could disappoint. In addition, the ISM manufacturing index comes out on Wednesday, followed by the ISM non-manufacturing index on Friday.

Manufacturing activity has been steadily declining since hitting a near-term peak in February.

On the earnings front, reports are expected from companies such as Bank of Nova Scotia, Dollar General, Diamond Foods and SAIC.

Central banks from several countries will meet this week, including Russia, Colombia, Canada and Thailand.



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