

<u>Date</u>	<u>Indicator</u>	<u>For</u>	<u>Estimate</u>	<u>Consensus*</u>	<u>Previous Period</u>
Jun. 23	Existing Home Sales	MAY	4.800M	4.810M	4.680M
Jun. 24	Durable Orders	MAY	-1.5%	-0.9%	1.7%
Jun. 24	Durable Orders ex-Trans.	MAY	-0.5%		0.4%
Jun. 24	New Home Sales	MAY	0.365M	0.360M	0.352M
Jun. 24	Fed Funds Target		UNCH		0.125%
Jun. 25	GDP Final	Q1	-5.5%	-5.7%	-5.7%
Jun. 25	GDP Chain Price Final	Q1	2.8%	2.8%	2.8%
Jun. 25	Initial Claims	06/20	595K		608K
Jun. 26	Personal Income	MAY	0.6%	0.4%	0.5%
Jun. 26	PCE	MAY	0.5%	0.4%	-0.1%
Jun. 26	PCE Chain Price, M/M	MAY	0.1%		0.1%
Jun. 26	Michigan Sentiment Final	JUN	69.0	69.5	69.0

\*Consensus from Action Economics

## **Is This a True and Sustainable Recovery?**

The current market discussion has been revolving around whether the U.S. and world economies can recover fast and strongly enough that we may have a V-shaped recovery (recall a previous FMS where I discussed economic cycles' "soup of letters"). However, the point seems to be, for all intents and purposes, moot. In every serious economic crisis in history, there is some type of V-shaped recovery. Normally, economies overshoot on the way down; that is, they drop more than what it would have been deemed "normal." Thus, there is a tendency for economic crisis triggered by financial collapses to be more pronounced because everybody runs for the exits. This is what happened to the U.S. economy and to the rest of the world after the collapse of Lehman Brothers on September 15, 2008. This means that when things start coming back to normal, then it shows as a strong bounce-back in economic activity, but the truth is that it is just that, a bounce-back from a very low level that shows in the numbers like a strong recovery, but it is not. However, what we have to do is to compare those numbers to the pre-crisis numbers, and when we do that it is clear that this "recovery" or "green shoots" is just that, a bounce-back from a very low level. But what is important is not the bounce-back but the sustainability of growth. This is what is going to determine how long it will take for the economy to get back to pre-crisis levels.

Today, this bounce-back is being helped by highly expansionary monetary and fiscal policy. Thus, what is important is to figure out what will happen when these two components of the bounce-back disappear. Will the economy have what it needs for growth to be sustainable? How many years will it take for the economy to recover the capital lost during this crisis? Some say that the amount of financial losses before the crisis is over will be close to \$2 trillion dollars, just in the U.S. Thus, how many years of U.S. profits will the economy need to replenish this loss so we can get back to the pre-crisis levels? These are some of the key questions that markets should be asking themselves. Have we solved the issues that put us in this crisis in the first place? Have we reformed the institutions that allowed us to get here? Have we stopped blaming all but ourselves for the current crisis?

## **What Rate of Growth is Enough for the Markets?**

The fact of the matter is that a large part of the growth the U.S. and world economy experienced during the last several decades was fueled by excessive fiscal expenditures and excessively low interest rates, which essentially translated to excessive lending and borrowing. The only difference with today's environment is that during those two decades, this excessive fiscal and monetary policy was done on top of "normal" economic growth, which pushed growth over the top. Today, this excessive fiscal and monetary policy is just barely filling in the holes produced by the collapse of the financial markets and the impressive losses that this collapse produced all across the world.

This means that if this type of monetary and fiscal expansion disappears, then economic growth will be much lower than what we have experienced during the last several decades. That is, we will have to rely more on either further increases in productivity or in resource availability or both, that is, on real economic factors rather than on temporary ones as is the case of fiscal and monetary policy.

My point here is that if we no longer have the Lehman Brothers, the Bear Stearns, and all of those financial institutions that had levels of leverage of 80 to 1, then something else will have to replace the growth coming from such levels of leverage if we want to go back to the rates of growth we experienced during those years. And with the new regulatory environment proposed by the Obama administration it seems that replicating those types of firms and those levels of leverage will be more difficult in the coming years. Thus, I will say that even, and when, we finally get to the point where we don't need the help of monetary and fiscal policy, the prospects of growth will be limited by our economy's ability to generate "real" economic resources through either an increase in the number of those resources, i.e., land (natural resources), labor, capital and entrepreneurship, or the productivity of them, or a combination of both.

I know that many say that the U.S. consumer is going to come roaring back to the market at any time now. However, all the data is pointing to a consumer that will remain weak for the foreseeable future. The consumer not only has to deal with the current economic and labor market environment but also with higher gasoline prices, which will take away any prospects of a strong consumer comeback any time soon. Furthermore, the data is also pointing to a consumer that continues to deleverage even as interest rates remain at historically low levels and to the dismay of monetary policymakers. Thus, I will not count on the consumer coming roaring back until they are able to replenish their wealth levels and pay down their debts, if not completely, at least partially.

# Major Economic Indicators

June 19, 2009

Economic Data	History					Forecast								Q4 to Q4 % Chg or Annual Average			
	2008.1	2008.2	2008.3	2008.4	2009.1	2009.2	2009.3	2009.4	2010.1	2010.2	2010.3	2010.4	2007	2008	2009	2010	
Real GDP*	0.9	2.8	-0.5	-6.3	-5.7	-1.8	0.4	1.8	2.0	3.1	3.2	3.6	2.3	-0.8	-1.4	3.0	
Personal Consumption Expenditures*	0.9	1.2	-3.7	-4.3	1.5	-0.5	-0.5	1.4	1.6	2.4	2.0	2.2	2.2	-1.5	0.5	2.1	
Private Housing Starts (000s units)	1,053	1,025	876	661	523	485	500	550	625	650	735	775	1,341	904	515	696	
Vehicle Sales (mill. Units, annualized)	15.2	14.1	12.9	10.3	9.5	10.2	10.6	10.9	11.2	11.7	12.1	12.5	16.1	13.1	10.3	11.9	
Nonfarm Payroll Employment (mil.)	137.9	137.7	137.3	135.6	133.5	132.2	131.2	130.7	130.9	131.4	132.2	133.2	137.6	137.2	131.9	131.9	
Unemployment rate	4.9	5.3	6.0	6.9	8.1	9.3	9.5	9.8	9.9	9.9	9.7	9.5	4.6	5.8	9.2	9.8	
CPI* (percent)	4.5	4.5	6.2	-8.3	-2.4	0.6	2.2	1.1	0.8	0.5	0.6	0.7	4.0	1.7	0.4	0.7	
PPI* (percent)	8.1	9.9	9.7	-19.0	-6.3	-0.6	3.6	-1.4	0.3	-0.6	-0.3	-0.3	6.8	1.9	-1.2	-0.2	
Compensation Per Hour*	3.7	1.7	5.7	5.1	4.2	3.2	2.0	1.9	2.0	2.0	1.7	1.3	3.6	4.1	2.8	1.8	
Productivity*	2.6	4.7	2.2	-0.6	0.8	2.3	2.2	2.2	2.5	2.8	2.6	2.5	2.7	2.2	1.9	2.6	

\*Quarterly Data Percent Change At Annual rate; Annual Data Q4 to Q4 % Chg.

Financial Data	History					Month-to-Date		Current	Forecast (monthly)							
	2008.12	2009.01	2009.02	2009.03	2009.04	2009.05	2009.06	6/19/2009	2009.07	2009.08	2009.09	2009.10	2009.11	2009.12	2010.01	2010.02
S & P 500	877	867	806	757	849	902	933	924								
Dow Jones Industrial Average	8,590	8,408	7,698	7,235	7,996	8,393	8,683	8,589								
NASDAQ	1,526	1,539	1,488	1,432	1,642	1,724	1,835	1,832								
Federal Funds Rate	0.13	0.17	0.23	0.22	0.15	0.18	0.21	0.25	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20
Treasury-3 Month Bills (yield)	0.03	0.13	0.30	0.22	0.16	0.18	0.17	0.18	0.18	0.19	0.19	0.19	0.19	0.20	0.20	0.20
Treasury-10 Year Notes (yield)	2.41	2.50	2.87	2.82	2.93	3.30	3.78	3.79	3.74	3.78	3.83	3.88	3.93	3.98	4.03	4.03
Prime Rate	3.61	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25
Libor 3-Mo. U.S. Dollar	1.80	1.22	1.24	1.27	1.11	0.82	0.67	0.61	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60
Mortgage-15 Year (yield)	5.17	4.73	4.79	4.65	4.51	4.51	4.84	4.89	4.84	4.88	4.93	4.98	5.03	5.08	5.13	5.13
Mortgage-Adjustable (yield)	5.02	4.90	4.88	4.85	4.83	4.76	4.88	4.95	4.90	4.94	4.99	5.04	5.09	5.14	5.19	5.19
Mortgage-30 Year (yield)	5.42	5.05	5.13	5.02	4.82	4.84	5.33	5.38	5.33	5.37	5.42	5.47	5.52	5.57	5.62	5.62
GNMA (yield)	5.78	5.30	5.21	5.15	4.85	4.48	4.18	4.31	4.25	4.29	4.34	4.39	4.44	4.49	4.54	4.54
BAA Corporate (yield)	8.42	8.13	8.09	8.42	8.40	8.07	7.64	7.47	7.42	7.46	7.51	7.56	7.61	7.66	7.71	7.71

Source: Wells Fargo Economics, Macroeconomic Advisers, Bloomberg, Federal Reserve