



Weekly Economic Commentary

Economy Review - Outlook

February 4, 2008

John Canally, CFA
Investment Strategist
LPL Financial

Economic Calendar for 1/04 - 2/08

Monday, Feb 04
Factory Orders
December

Tuesday, Feb 05
ISM Nonmfg Business
Activity Index
January

Wednesday, Feb 06
Productivity
Q4

Thursday, Feb 07
Initial Claims
wk 02/02

Consumer Credit
December

Chain Store Sales
January

Friday, Feb 08
Wholesale Inventories
December

Executive Summary:

For the most part, financial markets looked past last week's flood of economic data, focusing instead on the Fed and the health of the nation's bond insurers. Had financial markets paid attention, they would have found a mixed bag of data, that on balance shows the United States economy was slowing as 2007 ended and 2008 began.

The Federal Reserve's 50 bp rate cut last week helped to further align the Fed's view and the market's view on the state of the economy and interest rates.

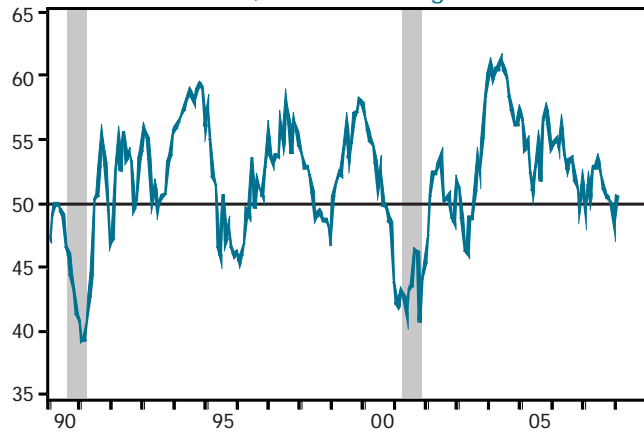
Quiet week ahead on the economic data front, with the key reports likely to be the weekly jobless claims data and the January retail sales reports from the nation's retailers.

Economic Landscape in Review:

Mixed Bag of Economic Data Confirms that Economy Continued to Slow as 2007 Ended and 2008 Began

Last week's barrage of economic data was largely ignored by the financial markets, as market participants focused instead on the Federal Reserve and the health of the nation's bond insurers. Had market participants bothered to pay attention to the economic data, they would have found further evidence that the economy was slowing as 2007 ended and 2008 began. The data wasn't universally weak, however. The manufacturing sector showed some signs of life, as both the December durable goods orders and the January Institute for Supply Management's report on manufacturing came in above economists' expectations. Note that a reading above 50 on the ISM indicates that the manufacturing sector is expanding, while a reading below 50 indicates a contracting manufacturing sector. The ISM has to dip into the 40s or below to indicate a recession in the broad economy.

ISM Manufacturing: PMI Composite Index SA, 50+ =Increasing



Source: Institute for Supply Management / Haver Analytics 02/01/08

On balance, the data released on manufacturing last week suggests that the inventory drawdown that hurt gross domestic product growth in the fourth quarter of 2008 may give way to some restocking in the first half of 2008.

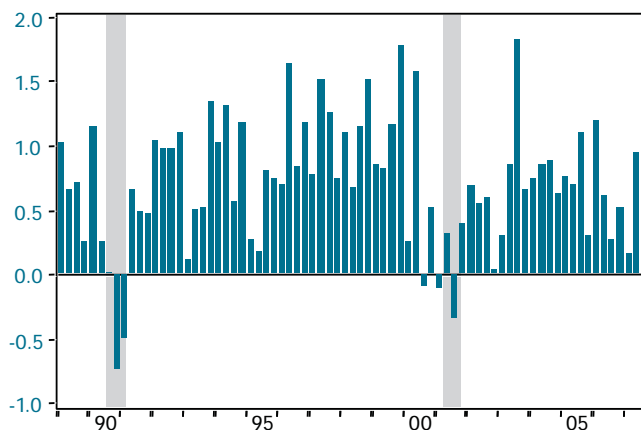
On balance, the data released on manufacturing last week suggests that the inventory drawdown that hurt gross domestic product growth in the fourth quarter of 2008 may give way to some restocking in the first half of 2008.

Unfortunately, the remainder of the data released last week was on the soft side, confirming that the economy slowed in the final quarter of 2007 and remained sluggish in early 2008. New home sales, personal spending, and construction spending for December all came in below expectations, while the data for January – vehicle sales consumer confidence, and most importantly the jobs report – were weaker than expected.

In addition, the GDP report for Q4 2007 came in well below expectations, posting a 0.6% gain in Q4 against expectations of a 1.2% gain. The 0.6% annualized gain in Q4 versus Q3 followed a robust 4.9% increase in GDP in the third quarter of 2007. Housing continued to deteriorate in Q4, but consumer spending, net exports and business investment spending decelerated between Q3 and Q4.

Real Gross Domestic Product

% Change - Period to Period SAAR, Bil. Chn. 2000\$

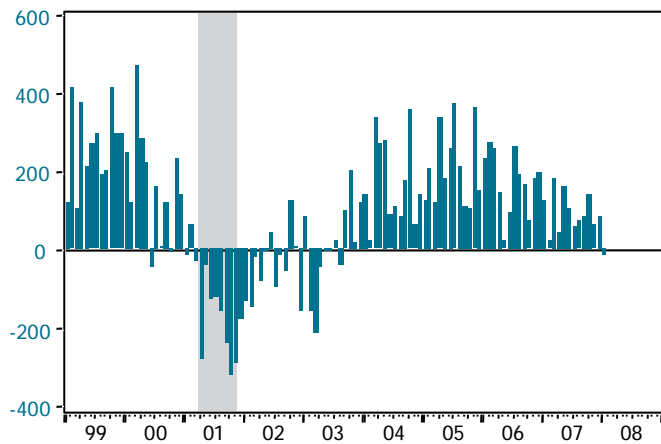


Source: Bureau of Economic Analysis / Haver Analytics 02/04/08

The unemployment rate fell 0.1% to 4.9%, which is encouraging, but the outright decline in jobs in January – the first monthly job loss since mid 2003 – was the attention grabber in the report.

The January jobs report was quite weak, as the economy shed 17,000 jobs in the month, against expectations of a 75,000 gain. The January data are particularly difficult to interpret because the employment data have been revised back to the beginning of 2006. The unemployment rate fell 0.1% to 4.9%, which is encouraging, but the outright decline in jobs in January – the first monthly job loss since mid 2003 – was the attention grabber in the report. The job losses in January were widespread, with declines in manufacturing, construction, financial, business services and government. The bright spots were in the health care and leisure and hospitality industries, consistent with the trends we are seeing from corporate America as they report their Q4 2007 earnings and provide guidance for 2008.

All Employees: Total Nonfarm
Difference - Period to Period SA, Thous

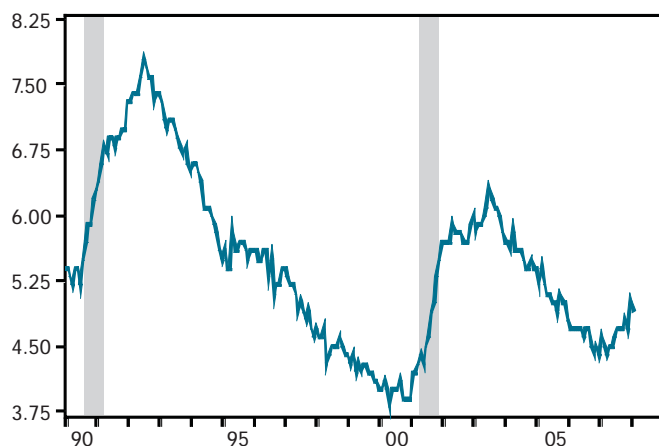


Source: Bureau of Economic Analysis / Haver Analytics 02/01/08

...the overall report is on the weak side and still suggests that the United States economy is slowing, but not yet in a recession.

On balance, however, net of the revisions, the overall report is on the weak side and still suggests that the United States economy is slowing, but not yet in a recession. We would need to see jobs decline for several months in a row before making the call that the United States is in recession.

Civilian Unemployment Rate: 16 yr +
SA, %



Source: Bureau of Labor Statistics / Haver Analytics 02/01/08

The weak jobs data keeps the Fed in the picture, and argues for more Fed rate cuts in the coming month.

The weak jobs data keeps the Fed in the picture, and argues for more Fed rate cuts in the coming months. The market is pricing in another 100 bps of cuts over the next year, with the end point on Fed funds at 2.0% from the 3.0% reading today. Our view is that the Fed is

likely to do at least another 50 bps in cuts, bringing the Fed Funds rate down to 2.50%, and we think the Fed will most likely front-load those cuts into the first half of the year

Fed Cuts 50, Market and Fed Now on the Same Page:

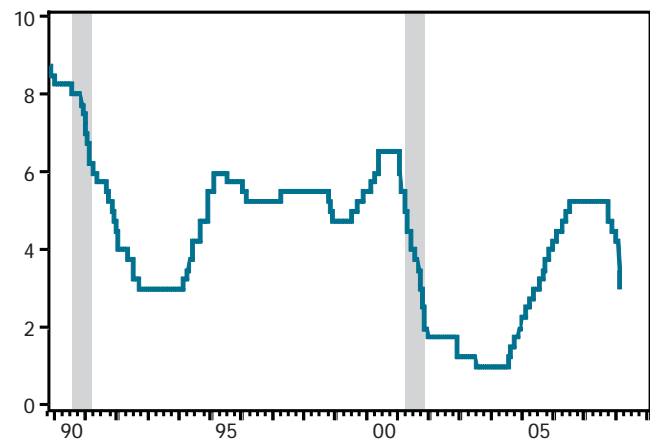
The Federal Reserve Open Market Committee (FOMC) announced a 50 basis point cut in its Fed funds rate target at the conclusion of its regularly scheduled two day meeting on January 30. The target Fed funds rate is now 3.00%. The Fed also cut its discount rate by 50 bps to 3.50%. The move was fully priced in, although as recently as the middle of January, the market was pricing in a 75 bp cut at this meeting. The 50 bp cut came a little more than a week after the Fed's surprise 75 bp cut on January 22, which was the first "intermeeting" cut – i.e., not at a regularly scheduled FOMC meeting – since September 17, 2001 when the Fed cut rates by 50 bps in reaction to the terrorist attacks on the U.S. on September 11, 2001.

Only one member of the FOMC, Richard Fisher, the President of the Dallas Fed – and a well known inflation hawk— voted against the move. This nearly unanimous vote is notable, because there have been a wide range of opinions from voting members of the FOMC in the press in recent weeks and it's another sign that Fed Chairman Ben Bernanke may be gaining the respect of his colleagues on the FOMC

After last week's 50 bp move, the Fed's view of what it needs to do and the market's view of what the Fed needs to do seem to be in sync for the first time in a while.

The change in the wording of the statement accompanying the most recent rate cut announcement compared to the statement accompanying the January 22 rate cut suggests that the FOMC thinks it has done enough for now. However, the Fed has left the door open for more cuts by saying "downside risks to growth remain." The market has already priced those cuts in, and now expects a 2.5% Fed funds rate by yearend 2008. After last week's 50 bp move, the Fed's view of what it needs to do and the market's view of what the Fed needs to do seem to be in sync for the first time in a while. Recall that just two weeks ago, the market was pricing in a 1.75% or 2.00% end point for the Fed funds rate. A 2.25% or 2.50% end point now seems more reasonable.

Federal Open Market Committee: Fed Funds Target Rate



Source: Federal Reserve Board / Haver Analytics

01/30/08

The Week Ahead:

Focus on Jobless Claims and January Retail Sales

After an incredibly busy week last week, this week is shaping up to be a rather quiet one on the economic data calendar.

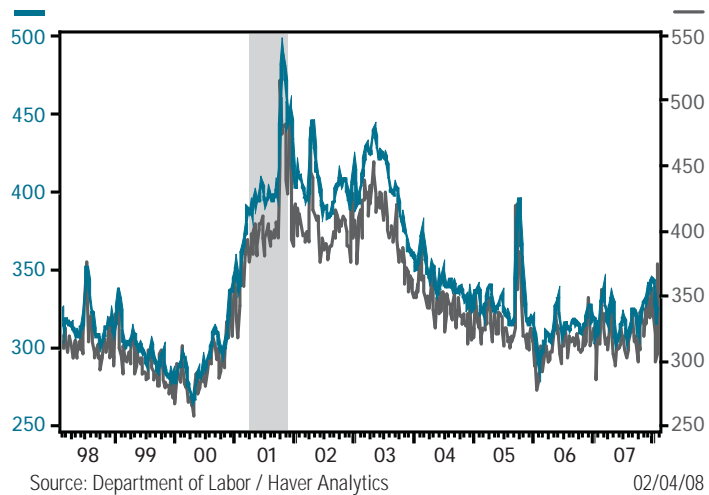
The main reports will be the latest reading on initial jobless claims and the reports from the nation's retailers on their January same store sales.

The weekly jobless claims data will be closely watched this week, especially after the spike in claims up to 375,000 in the week ending January 26.

The weekly jobless claims data will be closely watched this week, especially after the spike in claims up to 375,000 in the week ending January 26. The Labor Department has had difficulty seasonally adjusting the claims data in the early part of 2008, and last week's report was no exception. In fact, the Labor Department took the relatively unusual step of saying that the report was subject to quirky seasonal factors surrounding the Martin Luther King Jr. holiday on January 21. Still, the reading at 375,000 was disturbing to market participants. As in the past, a reading on claims consistently at or above the 375,000 level has indicated that the broad economy was in a recession. Thus, the market will be looking for a sharp decline in claims in the latest week, and a four week average on claims staying in the 300,000 to 325,000 range it has been in for more than two years now.

Unemployment Insurance: Initial Claims, 4-Week Moving Average SA, Thous

Unemployment Insurance: Initial Claims, State Programs SA, Thous



Important Disclosures

This report has been prepared by LPL Financial from sources believed to be reliable but no guarantee can be made as to its accuracy or completeness. The opinions expressed herein are for general information only, are subject to change without notice, and are not intended to provide specific advice or recommendations for any individuals. Please contact your advisor with any questions regarding this report.

Investing in international and emerging markets may entail additional risks such as currency fluctuation and political instability. Investing in small-cap stocks includes specific risks such as greater volatility and potentially less liquidity.

Stock investing involves risk including loss of principal.

Past performance is not a guarantee of future results. Indices are unmanaged and cannot be invested into directly.

This research material has been prepared by LPL Financial.

The LPL Financial family of affiliated companies includes LPL Financial, UVEST Financial Services Group, Inc., IFMG Securities, Inc., Mutual Service Corporation, Waterstone Financial Group, Inc., and Associated Securities Corp., each of which is a member of FINRA/SIPC.

Not FDIC/NCUA Insured	Not Bank/Credit Union Guaranteed	May Lose Value
Not Guaranteed by any Government Agency		Not a Bank/Credit Union Deposit