



# Weekly Economic Commentary

December 8, 2008



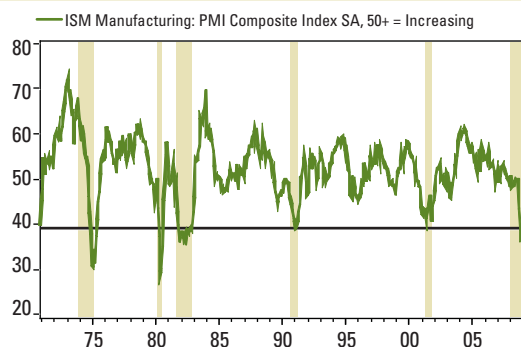
## John Canally, CFA

Investment Strategist  
LPL Financial

### ECONOMIC CALENDAR

Wednesday, Dec 10	Friday, Dec 12
Wholesale Inventories <i>October</i>	Core PPI <i>November</i>
Treasury Statement <i>November</i>	PPI <i>November</i>
Thursday, Dec 11	Retail Sales X-Autos <i>November</i>
Trade Balance <i>October</i>	Retail Sales <i>November</i>
Initial Claims <i>wk 12/6</i>	U of Mich Consumer Sentiment <i>December</i>
Import Price Index <i>November</i>	Business Inventories <i>October</i>

### 1 The ISM Report for November Was the Weakest Since the Severe 1981–1982 Recession



Source: Institute for Supply Management / Haver Analytics 12/08/08

## Executive Summary: It's Still Getting Worse

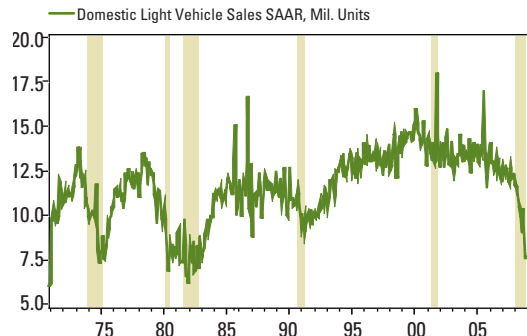
We were again disappointed by last week's batch of economic data, which revealed that the U.S. economy didn't stop getting worse in November. In fact, the economy probably got a lot worse in November than it was in October. For the second consecutive week, virtually every piece of economic data released referencing the month of November was either weaker than expected or worse than October, further solidifying the thesis that the U.S. economy contracted sharply in the current (fourth) quarter of 2008. We currently expect fourth quarter GDP to contract by at least 4.0%, which would be the weakest reading on GDP since the 1981-82 recession. The Q4 GDP data are due out in late January.

The good news is that despite all the bad news on the economy in November released last week—the worst of which came on December 5, with the release of the absolutely wretched November employment report—market participants seem to be warming up to the view that the U.S. economy is not headed for a 1930s-style Great Depression. The S&P 500 last week gave back only 2.25% of the 12.0% it gained the week ending November 28, all but shrugging off the horrible news on the economy. Is the equity market just “whistling past the graveyard”? We don't think so.

As we have mentioned often in these pages in recent weeks, ever since the mid-September collapse of Lehman Brothers turned what was shaping up to be a relatively mild U.S. recession into a vicious global recession, financial markets around the world have been trying to gauge the depth and breadth of the downturn. Through much of October and November, the wild volatility and multi-year lows seen in the U.S. equity markets suggested to us that market participants were pricing in a recession that would turn out to be far worse than even the severe recessions of 1973-75 and 1981-82. Indeed, on November 20, 2008, the S&P 500 was down 51.9% from its October 2007 high, trailing only the 86.2% drop in the market between 1929 and 1932 and the 60% drop experienced between 1937 and 1942. This 51.9% drop suggested that the market had priced in an economic climate similar to that seen in the Great Depression of the 1930s. The nearly 20% increase in the S&P 500 since hitting that 11-year low at the end of November suggests that the market is perhaps coming around to our view that the unprecedented amount of fiscal and monetary policy stimulus already in place (and in the pipeline) may indeed be enough to prevent the U.S. economy from sliding into another Great Depression similar to the 1930s.

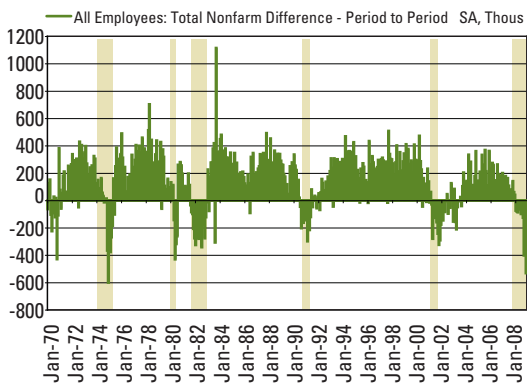


## 2 The Pace of Domestic Vehicle Sales in Nov. was the Slowest Since the Severe 1981-82 Recession



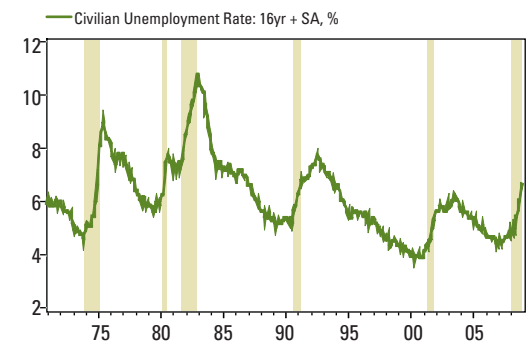
Source: Bureau of Economic Analysis / Haver Analytics 12/08/08

## 3 Nonfarm Payrolls Declined by 533,000 in Nov., the Largest Drop since December 1974



Source: Bureau of Labor Statistics / Haver Analytics 12/08/08

## 4 Unemployment Rate Has Risen by Two Full Points Over the Past 12 Months and is at its Highest Since 1993



Source: Bureau of Labor Statistics / Haver Analytics 12/08/08

Looking quickly at last week's economic data, the following reports fit solidly into the "didn't stop getting worse in November" category:

- November Institute for Supply Management's index on manufacturing fell 2.7 points to 36.2, the lowest reading since May 1982.
- November Institute for Supply Management's index on non manufacturing activity fell 7.1 points to 37.3, a new record low reading on the index, which begins in 1997.
- November vehicle sales fell to a 7.6 million annualized pace, the lowest monthly sales pace since October 1982.
- November nonfarm payroll job count fell 533,000, the most severe one-month decline in jobs since December 1974 when the count fell by 602,000.
- In November, the unemployment rate ticked up by 0.2 percentage points to 6.7%, up two full points over the past 12 months and to its highest level since late 1993.

The data released last week referencing October, all of which was worse than lowered expectations, included:

- The moribund October construction spending report, which revealed a 1.2% drop in construction spending in the month, the ninth gain in the past 12 months.
- The steep 5.1% drop in factory orders in October, which suggests that business capital spending will be a detractor from real GDP growth in Q4 2008.

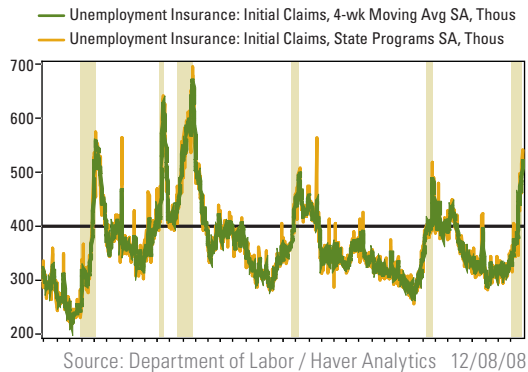
The one bright spot in last week's data was the outright decline in initial claims for unemployment insurance in the week ending November 29 to 509,000, down 21,000 from the 530,000 reading in the week ending November 22. The market was looking for a rise in claims to 535,000. While we would certainly welcome a halt to the recent rise in jobless claims as a sign that the labor market was beginning to heal, it is probably too soon to tell, especially given that claims in late November are often distorted by the difficulty in properly seasonally adjusting the data around the Thanksgiving holiday. The four-week average on claims, which smoothes out the volatile week-to-week changes, is at 524,500 jobless claims, its highest reading since December 1982, just after the end of the severe 1981-82 recession.

While we continue to remain hopeful that the economy will "stop getting worse" in November, the reports released last week for November (employment, ISM, vehicle sales) do not bode well for the remainder of the data to be released for November. As is often the case the week after the release of the monthly employment report, this week is a relatively quiet one on the data front. The key reports due this week include:

- The weekly jobless claims for the week ending December 6
- The University of Michigan's consumer sentiment data for the first half of December
- The November retail sales report
- The November produce price index report



## 5 Despite a Small Drop in the Latest Week, Jobless Claims Remain at their Highest Level Since the 1981-82 Recession



- The October pending home sales data vehicle sales reports
- The October trade balance report

Of these, the market will pay closest attention to the data for December (claims and sentiment), to begin to gauge whether or not the economy stopped getting worse in December.

### 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., Mutual Service Corporation, Waterstone Financial Group, Inc., and Associated Securities Corp., each of which is a member of FINRA/SIPC.

Not FDIC or NCUA/NCUSIF Insured | No Bank or Credit Union Guarantee | May Lose Value | Not Guaranteed by any Government Agency | Not a Bank/Credit Union Deposit