

THE ECONOMIC OUTLOOK GROUP



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ECONOMIC TALKING POINTS

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The U.S. Recovery Continues, While Dubai Fades Into the Background

We are now some six months into the recovery and there are no signs it is losing any momentum. Indeed recent economic indicators show improvements in both output AND employment in recent weeks.

Yesterday, for example, the important Chicago division of Institute for Supply Management (ISM) surprised analysts with the strength of business activity in the Midwest. November's manufacturing index surged to its highest level since August 2008. The all-important new orders gauge, a leading indicator of future production, was the strongest seen in more than 2 years. We also got better than expected news on the employment front when that index leaped to a 14-month high.

ISM

Today we got the much-anticipated nationwide ISM report for November and it brought news that manufacturing activity expanded for the fourth month in a row. The index slipped a bit to 53.6 last month from 55.7, but remember, readings above 50 indicate more firms said they were growing than said they were contracting. In any case, November's slowdown will be short-lived because the new orders index shot up to 60.3, compared with the 58.5 in October, suggesting that companies will further ramp up production in coming weeks.

Of the 17 industries surveyed, 13 reported growth in new orders (Petroleum & Coal

Products; Electrical Equipment, Appliances & Components; Apparel, Leather & Allied Products; Miscellaneous Manufacturing; Printing & Related Support Activities; Computer & Electronic Products; Paper Products; Plastics & Rubber Products; Primary Metals; Food, Beverage & Tobacco Products; Chemical Products; Machinery; and Fabricated Metal Products.)

Four noted fewer orders last month (Wood Products; Nonmetallic Mineral Products; Furniture & Related Products; and Transportation Equipment.)

One closely watched subset in the ISM release was that of employment in manufacturing, and there was good news here as well. The employment index for showed growth in jobs occurred in hiring for the second month in a row. The measure stood at 50.8% compared with 53.1% in October. Again, we expect the pace of hiring to pick up in response to the acceleration in new orders.

One especially vital source of strength in today's economy is exports and, once again, manufacturers reported strong sales in foreign markets. New export orders jumped to 56.0 in November, the most activity manufacturers have seen since August 2008! Nine industries saw growth in export orders, while only two reported declines.

Pending Home Sales

The housing sector, whose collapse helped precipitate worst financial crises since the Great Depression, is now on comeback. Pending home sales surged 3.7 in October, according to the National Association of Realtors, the ninth consecutive monthly increase and the longest streak of gains seen since the NAR began this series! The pending home sales index itself rose to 114.1, the most seen in 3 ½ years. The number of contracts signed now stands 31.8% above its year ago level, which is also a record high. This series already follows a string of other bullish reports on residential real estate, including rising new and existing homes sales, higher home prices, and shrinking inventories of unsold new homes.

Construction Spending

Further reinforcing the improvement in housing was the government's own construction spending report. Although the change in overall building activity was flat in October from the month before, spending on residential construction actually increased 4.2% last month to a seven-month high --- all of it by private developers. What drove the headline number down was the decline in spending on commercial real estate, which dropped 1.5% in October, bringing such outlays to a 3-year low.

Consumer Are Shopping

The holiday season also got off to a decent start. Americans appear ready to unleash some the pent-up demand they have accumulated during the recession. *The national data*

shows Black Friday sales were up 0.5% from last year. OK, that number won't ignite any celebratory fireworks. But when you've got double-digit levels of unemployment and Armageddon type headlines on the Dubai debt crisis, I'd say these shopping numbers were actually quite respectable.

Moreover, the International Council of Shopping Centers reported that chain store sales for the week ending November 28th increased 3.1% from year ago sales.

The improved outlook for consumer spending caused investors to turn bullish for retail stocks as well. The ETF index that replicates the performance of retailers (XRT) has been on a tear today for three reasons. First, the latest set of economic indicators corroborates other signs that an economic recovery is well underway. Second, we have now seen several employment measures in the last week uniformly showing an improvement in the labor market. Third, the Dubai debt problem is now fading fast into the background (stocks this morning are up by triple digits, risk appetite has returned, the dollar is down, gold is up...)

Not a bad way to start the month of December. We expect to finish the week with similar good news on the jobs front.

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