

# MONTHLY ECONOMIC UPDATE

December 2010

## WEEKLY QUOTE

“The key to the ability to change is a changeless sense of who you are, what you are about and what you value.”

– Dr. Stephen Covey

## MONTHLY TIP

Have you donated money or goods to a charity this year? If you donate to a non-profit before the 31<sup>st</sup> of December, you can take the deduction and potentially lower your taxable income for the year.

## MONTHLY RIDDLE

The English language has a noun with three consecutive double letters in it. The word is 10 letters long, and it describes a job involving math. What is this word?

## Last month's riddle:

You see a large truck stopped just before the underpass of a low bridge. The driver informs you that his truck is 1" higher than the maximum clearance. This is the only road to his destination. What is the easiest way to help him get his truck through the underpass?

## Last month's answer:

Let enough air out of the tires to lower the truck.

## THE MONTH IN BRIEF

Overseas developments put pressure on U.S. stocks last month, and the S&P 500 lost 0.23% for November. The month got off to a bright start, with the DJIA and NASDAQ reaching highs unseen since 2008 ... but a new round of worries over debt in the European Union, an artillery attack on South Korea by North Korea and concerns about tightening in China changed the mood. Stateside, the midterm elections were a bonanza for Republicans. The Federal Reserve unveiled another round of monetary easing. Mortgage rates went up; home sales didn't. The dollar and gold both had a good month.

## DOMESTIC ECONOMIC HEALTH

A political development and a policy move livened the economic discussion even more last month. The Republicans won control of the House, and that comforted Wall Street. Perhaps less reform and regulation and a more business-friendly environment would follow. Capitol Hill was poised for a negotiation over EGTRRA, JGTRRA and estate taxes; the question was, could a lame-duck Congress make up its collective mind before the end of 2010? The Fed announced plans to purchase \$600 billion worth of Treasuries over an eight-month period, plus their intentions to buy as much as \$900 billion in debt by the end of September 2011.<sup>2</sup> Some thought it was a wise move to promote lending, inflation and the overall economy; others thought the announcement effectively invited a trade war and wondered if the Fed's actions would lead to bubbles.

The economy seemingly needed more encouragement. The Commerce Department put 3Q 2010 GDP at +2.5% -- not bad, but hardly what was needed to make a dent in the jobless situation. (Unemployment was at 9.6% in October, and in late November the Fed estimated it would stay well above 7% through 2012. It also forecast growth of 3.0-3.6% for the economy in 2011, down from prior projections.) However, the Commerce Department brought us word that personal spending was +0.4% for October. Additionally, personal wages were +0.5% for the month, and the personal savings rate even ticked up a tenth of a percent to 5.7%. In October, real disposable income was 2.5% above year-ago levels, the best 12-month gain registered since June 2008.<sup>3,4,5</sup>

Consumer prices (at least as gauged by the Consumer Price Index) had risen just 0.2% in October, and the core CPI didn't go up at all – it was flat for the third consecutive month. Retail sales were not flat – the Census Bureau said they were up 7.3% in October compared to 12 months before, and the monthly gain was 1.2%. With regard to Black Friday, many of the numbers were quite good: year-over-year sales improved at Macy's (+6.1%), Target (+5.1%) and Costco (+9.0%), all topping those companies' expectations.<sup>6,7,8</sup>

How was manufacturing doing in America? The sector expanded for the sixteenth straight month in November, according to the Institute for Supply Management's newest report. The pace of production did slow down a bit in November while stockpiles and supplier deliveries increased. The Commerce Department noted a 3.3% drop in hard goods orders for October.<sup>2,9</sup>

## GLOBAL ECONOMIC HEALTH

Ireland. Portugal. Spain. Greece. These were the economic hot spots in Europe in November, and the European Union was saddled with trying to put out either embers or full-fledged fires. Ireland was the latest nation to adopt austerity

measures and accept a bailout; the European Central Bank and the International Monetary Fund arranged to offer as much as 85 billion euros of help to recapitalize banks and aid its punctured bubble economy. Economists feared Spain was next. That nation was dealing with astonishingly high unemployment, a stock market swoon, and the collapse of its real estate market. The bad news was that Spain's debt was at about 64% of its GDP; the good news, so to speak, was that the majority of it was domestically financed. There hadn't been much growth in the Eurozone in the third quarter: Germany's economy expanded just 0.7%, and the Eurozone as a whole grew just 0.4%.<sup>10,11,12</sup>

The People's Bank of China twice set new capital ratio requirements for the nation's lenders in November, following its first interest rate hike since 2007. This decision came after China's consumer prices rose 4.4% in October. Speaking of an economy heating up, Japan's GDP improved to an annualized 3.9% in the third quarter.<sup>13,14</sup>

## **WORLD MARKETS**

It was generally a poor month for stocks worldwide. Yet Japan's Nikkei 225 rose 8.0% in November, buoyed by noteworthy economic growth. While the German DAX advanced 1.3%, losses were more common in Europe – France's CAC 40 slid 5.8% last month, the FTSE 100 lost 2.6%, Ireland's ISEQ descended 1.4% and Spain's IBEX fell a dramatic 14.3%. Away from Europe, India's Sensex lost 2.6% for November, Australia's All Ordinaries fell 1.2%, Brazil's Bovespa declined by 4.2% and the Shanghai Composite in Hong Kong lost 5.3%. However, the TSX Composite in Canada gained 2.2% for the month, and a couple of benchmarks in emerging markets did surprisingly well – Russia's RTSI gained 2.8% and Mexico's Bolsa gained 3.5%.<sup>15</sup>

Speaking of emerging markets, the MSCI Emerging Markets Index lost 2.70% in November in U.S. dollar terms. Its sibling, the World Index, fell 2.35%. Our own U.S. Dollar Index rose to 81.32 at the end of November, climbing 5.56% for the month.<sup>16,17</sup>

## **COMMODITIES MARKETS**

The key precious metals mostly advanced last month. Only platinum did not, declining 2.4%. Gold gained 2.1% on the COMEX, ending November at \$1,385.00 per ounce and making its gain 26.5% YTD. Silver rose 14.9% last month and palladium gained 9.0%. As for energy futures, oil advanced 3.3% to close the month at \$84.11 per barrel, ending November up 6.0% YTD. Natural gas futures rose 3.5% in November and gasoline futures gained 6.3%; heating oil futures gained 3.6%. In crops, sugar grabbed headlines with its first negative month since May, as those futures fell 5.4%.<sup>18,19,20,21</sup>

## **REAL ESTATE**

Hm. Perhaps the home buyer tax credit needs to be reinstated? In light of the home sales numbers from October, it might help. New home sales fell 8.1% for the month, and existing home sales slipped 2.2%. The existing home sales rate was 25.9% below October 2009 and the new home sales pace was 28.5% below that of a year ago (but that was when the initial deadline for first-time buyer tax breaks was approaching). Existing home prices were down 0.9% from a year prior, according to the National Association of Realtors; the Commerce Department said new home prices were down 8.2% from October 2009.<sup>22,23,24</sup>

Was there any upside worth noting? Yes. That came in the category of pending home sales. October's pending sales rose 10.4% - the largest one-month jump since the NAR began tracking that statistic in 2001.<sup>25</sup>

Mortgage rates went up. (At least for the short term.) Comparing Freddie Mac's October 28 and December 2 Primary Mortgage Market Surveys, we see that average rates on 30-year FRMs went from 4.23% to 4.46%. How about 15-year FRMs? The movement was similar: 3.66% to 3.81%. Over the same period, the average interest

rates on 5-year ARMs went from 3.41% to 3.49%; average interest rates on 1-year ARMs actually diminished a bit from 3.30% to 3.25%.<sup>26</sup>

## LOOKING BACK...LOOKING FORWARD

November was the first down month for the DJIA since August. Fortunately, the losses were relatively minor across all three major U.S. indices.

% CHANGE	Y-T-D	1-MO CHG	1-YR CHG	10-YR AVG
DJIA	+5.54	-1.01	+6.39	+0.57
NASDAQ	+10.10	-0.37	+16.49	-0.38
S&P 500	+5.87	-0.23	+7.75	-1.02
REAL YIELD	11/30 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.74%	1.41%	2.12%	4.03%

Sources: online.wsj.com, bigcharts.com, ustreas.gov, bls.gov - 11/30/10<sup>1,27,28,29</sup>  
Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly.  
These returns do not include dividends.

December tends to be a very bullish month on Wall Street. Citing data from *The Stock Trader's Almanac*, CNBC.com notes that since 1990, the S&P 500 has gained an average of 1.79% in the last month of a year, and posted monthly gains in 16 of the past 20 Decembers.<sup>30</sup> Of course that is simply past performance, and no guarantee of future results. December has certainly gotten off to a great start as global markets have reacted to assurances from the ECB about controlling EU member debt, the big rebound in pending home sales, and retail sales numbers from Black Friday weekend. If Congress extends the Bush-era tax cuts and sets a reasonable estate tax for 2011 and beyond, the rally at the top of December could potentially gain fresh legs.

**UPCOMING ECONOMIC RELEASES:** Here is some notable data coming out across the balance of the month: October wholesale inventories (12/9), the initial December University of Michigan consumer sentiment survey (12/10), an FOMC rate decision, the November PPI, November retail sales and October business inventories (12/14), the November CPI and November industrial output (12/15), November housing starts and building permits (12/16), the Conference Board's November leading indicator index (12/17), November existing home sales and the final estimate of 3Q GDP (12/22), and then plenty of data just before Christmas: November consumer spending, durable goods orders and new home sales plus the final December University of Michigan consumer sentiment survey (12/23). The last market week of 2010 brings us the Conference Board's December poll of consumer confidence and October's Case-Shiller home price index (12/28).

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Renita M. Owens, CPA, PFS

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companies listed on the London Stock Exchange. The ISEQ 20 is a benchmark stock market index composed of companies that trade on the Irish Stock Exchange. The IBEX 35 is the benchmark stock market index of the Bolsa de Madrid, Spain's principal stock exchange. The BSE Sensex or Bombay Stock Exchange Sensitive Index is a value-weighted index composed of 30 stocks that started January 1, 1986. The S&P/ASX All Ordinaries Index represents the 500 largest companies in the Australian equities market. The Bovespa, the benchmark stock index of Brazil, is the second largest in the Americas, and the leading exchange in Latin America. The Shanghai Stock Exchange Composite Index is a capitalization-weighted index that tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange. The RTS Index (RTSI) is an index of 50 Russian stocks that trade on the RTS Stock Exchange in Moscow. The IPC Index is the main benchmark stock index of the Mexican Stock Exchange (BMV: BOLSA), which is Mexico's only stock exchange. The S&P/TSX Composite Index is an index of the stock (equity) prices of the largest companies on the Toronto Stock Exchange (TSX) as measured by market capitalization. The MSCI World Index is a free-float weighted equity index that includes developed world markets, and does not include emerging markets. The MSCI Emerging Markets Index is a float-adjusted market capitalization index consisting of indices in more than 25 emerging economies. The US Dollar Index measures the performance of the U.S. dollar against a basket of six currencies. Additional risks are associated with international investing, such as currency fluctuations, political and economic instability and differences in accounting standards. All information is believed to be from reliable sources; however we make no representation as to its completeness or accuracy. All economic and performance data is historical and not indicative of future results. Market indices discussed are unmanaged. Investors cannot invest in unmanaged indices. The publisher is not engaged in rendering legal, accounting or other professional services. If assistance is needed, the reader is advised to engage the services of a competent professional.

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