

**Weekly Market Monitor**

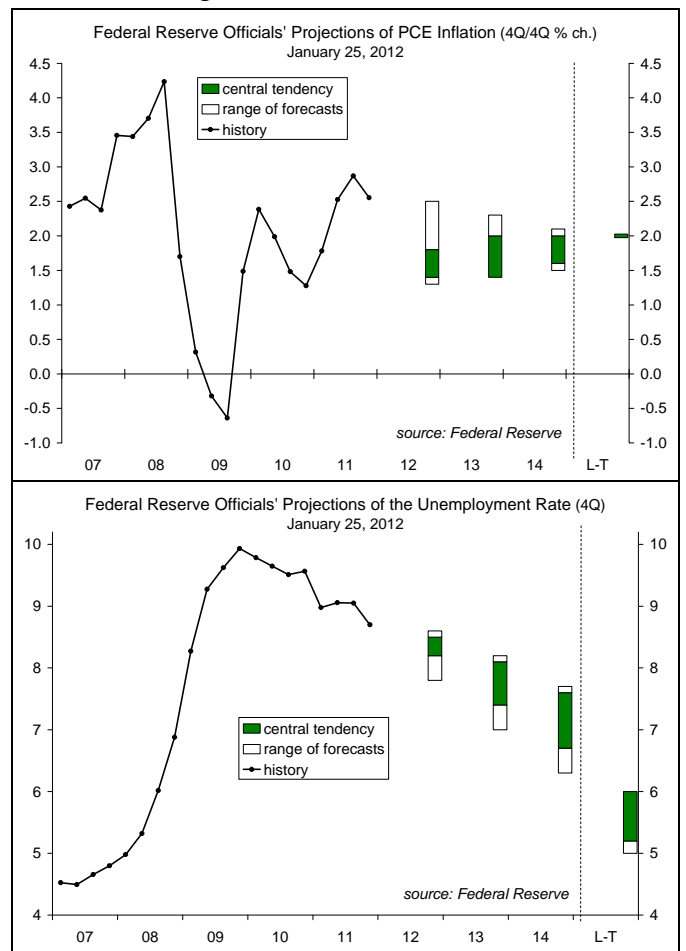
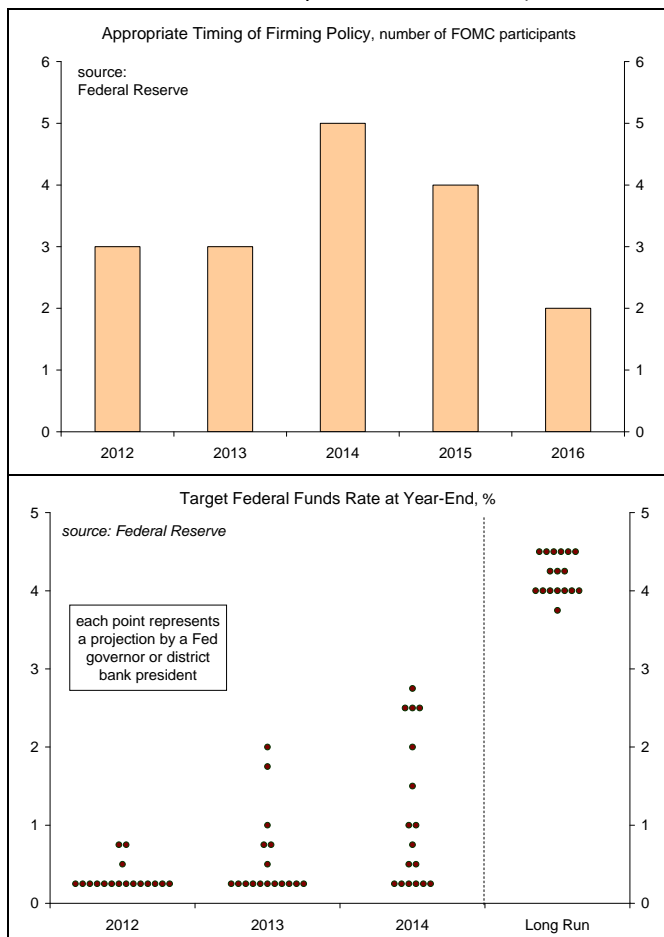
**The Fed: Dual Targets Or Dueling Targets?**

The Federal Reserve has adopted an inflation target, as many other central banks have done long ago. However, the Fed retained its dual mandate, with a soft employment target. How will the two goals be achieved and what happens when they conflict? The Fed says it will use a balanced approach.

The Fed lengthened the period for which it expects to keep short-term interest rates at exceptionally low levels (now, "at least through late 2014"). However, the five Fed governors and 12 district bank presidents have differing opinions on when the Fed should start raising short-term interest rates and what the appropriate level of the federal funds rate target will be at the end of 2014. There was closer agreement on where the federal funds rate target is expected to be over the long run (a 2% inflation rate + a 2.0-to-2.5% premium = 4.0-4.5%)

targeting central banks have a similar goal. For the Fed, a 2.0% inflation rate is "price stability."

The Fed also is required to achieve maximum sustainable employment, which "stands on an equal footing with price stability as an objective of monetary policy," according to Fed Chairman Bernanke. The unemployment rate statistic is an imperfect measure. It excludes discouraged workers and underemployment. Improvement over the last year has been exaggerated. Moreover, the unemployment rate consistent with maximum sustainable employment may change over time or may not be directly measurable. The Fed's second goal is a judgment call, and opinions vary. Officials believe the appropriate unemployment rate target is currently between 5.2% and 6.0% – higher than it was before the financial crisis.



The Fed will now shoot for a 2.0% annual rate in the PCE Price Index, which is similar to the CPI, but adjusts for changing patterns of consumption. The 2.0% goal would allow for more effective monetary policy during recessions. Other inflation-

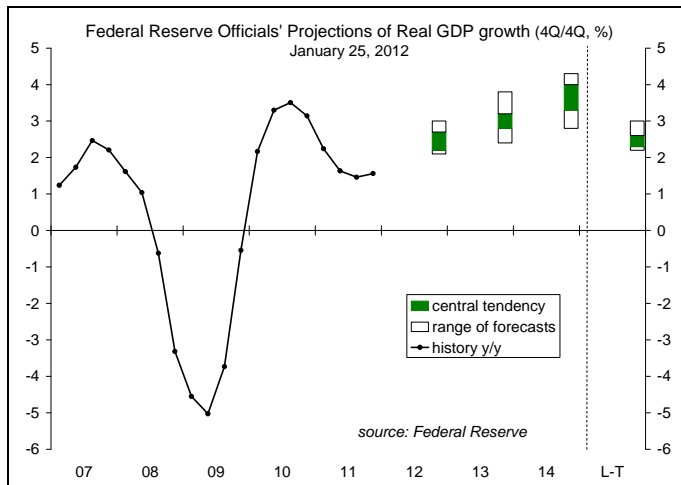
What happens when the Fed's two goals conflict or when one goal is near its target and the other is far from it goal? Would a balanced response imply that a higher inflation rate is acceptable in the short run to help push the unemployment rate down? That's possible, but it's not what the Fed is currently forecasting.

© 2012 Raymond James & Associates, Inc., member New York Stock Exchange/SIPC. All rights reserved. All expressions of opinion reflect the judgment of the Research Department of Raymond James & Associates, Inc. (RIA) as of the date stated above and are subject to change. Information has been obtained from third-party sources we consider reliable, but we do not guarantee that the facts cited in the foregoing report are accurate or complete. Other departments of RJA may have information that is not available to the Research Department about companies mentioned in this report. RJA or its affiliates may execute transactions in the securities mentioned in this report that may not be consistent with the report's conclusions.

	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	\$/Euro	\$/BP	JY/\$	CD/\$	NASD	SPX	DJIA
12/30/11	0.02	0.06	0.10	0.24	0.36	0.83	1.88	2.90	1.297	1.554	76.98	1.017	2605.15	1257.60	12217.56
1/20/12	0.05	0.07	0.10	0.24	0.37	0.89	2.03	3.10	1.295	1.554	76.97	1.014	2786.70	1315.38	12720.48
1/27/12	0.05	0.08	0.10	0.22	0.31	0.75	1.90	3.06	1.323	1.574	76.63	1.001	2816.55	1316.32	12660.46

## Recent Economic Data and Outlook

Fed policymakers were more dovish than expected, but investors wondered why that should be the case.



The **Federal Open Market Committee** said it expects to keep short-term interest rates at exceptionally low levels “at least through late 2014” (vs. the previous “through mid-2013”). The Fed adopted a hard PCE Price Index inflation target (2.0%) and a soft employment target (an unemployment rate at 5.2% to 6.0%, but that’s subject to change over time). In his press briefing, Chairman Bernanke said that officials were still debating whether to increase the Fed’s asset purchases.

**Real GDP** rose at a 2.8% annual rate in the advance estimate for 4Q11 (vs. a median forecast of +3.0%), up 1.6% y/y. Consumer spending rose at a 2.0% pace (vs. +1.7% in 3Q11). Business fixed investment rose at a 1.7% pace (vs. +15.7%). A faster pace of inventory accumulation added 1.94 percentage points to GDP growth. Net exports subtracted 0.11 ppt. Domestic Final Sales (GDP less net exports and the change in inventories) rose at a 0.9% annual rate, up 1.3% y/y. Government subtracted 0.93 ppt (defense -0.73, state & local gov’t -0.32). The PCE Price Index rose at a 0.7% annual rate (+2.6% y/y), a +1.1% pace ex-food & energy (+1.7% y/y, below the Fed’s target rate).

**New Home Sales** fell 2.2% in December, to a 307,000 seasonally adjusted annual rate (-2.2% y/y). Results were mixed across regions. The supply of unsold homes slipped 0.6%, down 29.1% from a year ago (a 6.1-month supply).

The **Pending Home Sales Index** fell 3.5% in December, following a 7.3% gain in November and a 10.4% increase in October (+5.6% y/y). Results were mixed across regions.

**Durable Goods Orders** rose 3.0% in December, following a 4.3% increase in November. Once again, strength was led by transportation (civilian aircraft +18.9%, defense aircraft -6.8%, motor vehicles +0.6%). Ex-transportation, orders were mixed across industries (primary metals +5.1%, fabricated metals

-1.4%, machinery +6.0%, computers and electronics +1.2%, electrical equipment and appliances -1.1%). Nondefense capital goods ex-aircraft (a proxy for business fixed investment) showed weakness in orders and shipments in October and November, but rebounded sharply in December – shipments for this category were flat in 4Q11 (vs. +17.3% in 3Q11 and +11.2% in 2Q11). Inventories rose more slowly in 4Q11.

**Mass Layoffs**, claims for unemployment insurance benefits for those laid off in groups of 50 or more, rose to 145,648 in December, vs. 131,627 in November – still a low trend.

The Index of **Leading Economic Indicators** rose 0.4% in December, following a 0.2%. In addition to annual benchmark revisions, the LEI underwent a significant revision to the methodology. Four components were replaced or modified. These revisions significantly lowered the last several monthly changes, but continued to point toward further expansion.

The **Chicago Fed’s National Activity Index** rose to +0.17 in December, vs. -0.46 in November. The three-month average rose to -0.08 (vs. -0.19), suggesting that overall economic growth is only slightly below its historical trend.

The **IMF** lowered its expectation for global growth to +3.3% (vs. a forecast of +4.0% in September), with the euro area at -0.5% (vs. September’s forecast of +1.1%). The IMF’s outlook for U.S. growth in 2012 was unrevised at +1.8%.

**Economic Outlook (1Q12):** +1.5% to +2.5% GDP growth.

**Employment:** Job destruction remains low. New hiring has picked up. Growth in nonfarm payrolls has improved. State and local government job losses appear to be waning.

**Consumers:** The holiday shopping season was a good one and pent-up demand should help in some areas, such as autos. However, spending has outpaced income growth in recent months. The payroll tax reduction was extended two months.

**Manufacturing:** Activity remains mixed across industries. New orders and production are likely to remain choppy and uneven in the early part of 2012. Despite continued strength in corporate profits, orders and shipments of capital goods appeared to soften in October and November.

**Housing/Construction:** Mild weather may have helped in November and December. Mortgage rates are at a record low, but home prices remain weak and refinancing remains difficult.

**Prices:** Food and energy prices have begun to unwind and pipeline inflation pressures have eased. Core consumer price inflation rose in 2011, but from very low levels in 2010. Inflation expectations remain contained and wage pressures are mild.

**Interest Rates:** The Fed will keep the overnight lending rate near zero through the middle of 2013 (conditional on “*low rates of resource utilization and a subdued outlook for inflation over the medium run*”). The Fed’s maturity extension program should keep long-term interest rates low. The Fed may increase purchases of mortgage-backed securities later this month.

This Week:					<i>forecast</i>	last	last -1	comments
Monday	1/30	8:30	Personal Income Personal Spending <b>PCE Price Index ex-f&amp;e</b>	Dec	<b>+0.4%</b> <b>+0.0%</b> <b>+0.1%</b>	+0.1% +0.1% +0.1%	+0.4% +0.1% +0.1%	should rebound from a soft November soft +1.1% (a.r.) 4Q-over-3Q
Tuesday	1/31	8:30 9:00 9:45 10:00	Employment Cost Index S&P/C-S Home Price Index year-over-year Chicago PM Index <b>Consumer Confidence</b>	4Q11 Nov  Jan Jan	<b>+0.4%</b> <b>NF</b> <b>NF</b> <b>61.5</b> <b>67.8</b>	+0.3% -0.6% -3.4% 62.5 64.5	+0.7% -0.7% -3.5% 62.4 55.2	a relatively low trend trending lower in the fall likely to stabilize in 2012 should remain relatively strong likely to improve further
Wednesday	2/01	8:15 10:00 10:00 tba	ADP Payroll Estimate, th. Construction Spending <b>ISM Manf. Index</b> Motor Vehicle Sales, mln domestically built	Jan Dec Jan Jan	<b>NF</b> <b>NF</b> <b>53.6</b> <b>13.7</b> <b>10.6</b>	+325 +1.2% 53.9 13.5 10.5	+204 -0.2% 52.7 13.6 10.7	seen more moderate, but still strong mild weather may have helped likely to remain moderate trend likely to remain gradually higher but some month to month noise
Thursday	2/02	7:30 8:30 8:30 10:00	Challenger Layoffs, th. Jobless Claims, th. Productivity (preliminary) Unit labor Costs Bernanke Testimony	Jan 1/28 4Q11  Jan	<b>NF</b> <b>380</b> <b>+0.8%</b> <b>+0.8%</b>	41.8 377 +2.3% -2.5%	42.5 356 -0.1% -0.1%	may be a bit higher, still a low trend  should be softer in 4Q11 no threat to the inflation outlook to House Budget Committee
Friday	2/03	8:30 10:00 10:00	<b>Nonfarm Payrolls, th.</b> private-sector <b>Unemployment Rate</b> employment/population Avg. Weekly Hours Avg. Hourly Earnings Factory Orders <b>ISM Non-Manf. Index</b>	Jan  Dec Jan	<b>+135</b> <b>+145</b> <b>8.5%</b> <b>58.6</b> <b>34.4</b> <b>+0.2%</b> <b>+1.5%</b> <b>53.1</b>	200 212 8.5% 58.5 34.4 +0.2% +2.3% 52.6	100 120 8.7% 58.5 34.3 0.0% -0.2% 52.0	should be relatively strong annual benchmark revisions due likely to hold steady should trend gradually higher seen steady limited wage pressures mixed, but moderate
Next Week:								
Monday	2/06		no significant data					Super Bowl hangover
Tuesday	2/07	1:00	Treasury Note Auction					3-year notes
Wednesday	2/08	1:00	Treasury Note Auction					10-year notes
Thursday	2/09	7:00 7:45 8:30 1:00	BOE Policy Decision ECB Policy Decision Jobless Claims, th. Treasury Bond Auction		<b>0.50%</b> <b>1.00%</b> <b>375</b> <b>380</b>	0.50% 1.00% <b>380</b>	0.50% 1.00% 377	a better-than-even chance of more QE some change of another rate cut still a bit noisy 30-year bonds
Friday	2/10	8:30 9:55 2:00	<b>Trade Balance, \$bln</b> goods only Consumer Sentiment Treasury Budget, \$bln	Dec m-Feb Jan	<b>-47.8</b> <b>-63.2</b> <b>NF</b> <b>NF</b>	-47.8 -63.2 75.0 -49.8	-43.3 -58.6 71.2 -42.6	little change is expected assumed flat in advance GDP est. improving a slightly smaller deficit than a year ago

## This Week...

The January economic data will begin to pour in. The focus should be on Friday's payroll figures. Note that annual benchmark revisions to the payroll data will be included in this report. Seasonal adjustment is likely to remain an important factor in the January jobs data and we may see some roll back of special factors that boosted the December total. Fed Chairman Bernanke will testify on the economic outlook on Thursday.

## Monday

**Personal Income and Spending (December)** – Quarterly figures, included in the advance GDP report, point to a moderate increase in income in the final month of 2011 and flattish spending (but watch for revisions). The inflation figures should be relatively benign (core trending below the Fed's target rate).

## Tuesday

**Employment Cost Index (4Q11)** – The ECI (which includes the cost of benefits) should have risen mildly in the fourth quarter.

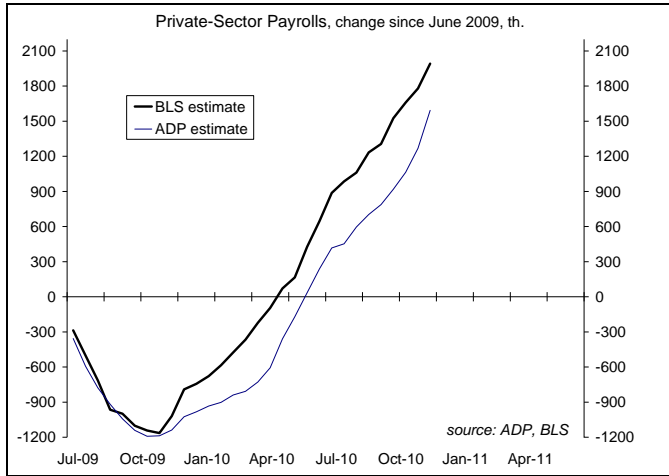
**S&P/Case-Shiller Home Price Index (November)** – Home prices fell 3.7% (seasonally adjusted) from May to October. That's not good. We need to see prices stabilize and start to improve, but many expect to see another decline in November.

**Chicago Purchasing Managers Index (January)** – The Chicago PM Index has been relatively strong in recent months, but we should see some slowing in January. Seasonal adjustment could exaggerate the figure.

**Consumer Confidence (January)** – The Conference Board's measure of consumer attitudes is likely to see some pickup, reflecting a better outlook for business. Job market perceptions should be less depressed (still a long way to go).

## Wednesday

**ADP Payrolls Estimate (January)** – The markets are unlikely to put much weight on the ADP figure, but could use a surprise to justify a move higher or lower. Benchmark revisions are expected a month from now (following BLS revisions this week).



**ISM Manufacturing Index (January)** – While manufacturing activity has continued to improve generally, orders and production have been mixed across industries. The ISM gauge is likely to remain at a moderate level in January.

**Motor Vehicle Sales (January)** – Consumers spending on motor vehicles add 0.81 percentage points to overall growth in the advance estimate of 4Q11 GDP. Further improvement is expected for 1Q12, but we should see a more gradual pace.

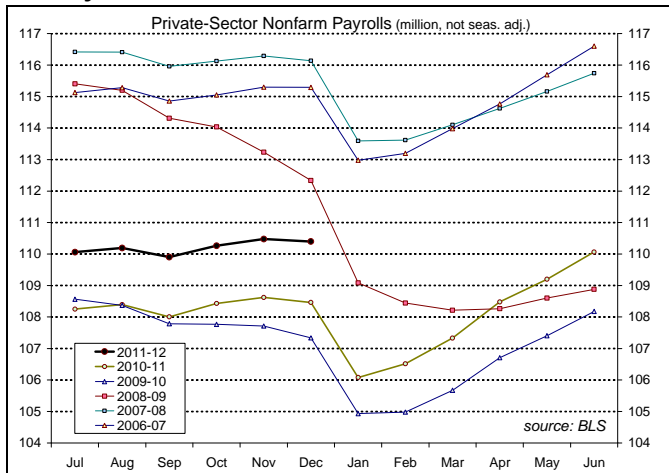
**Thursday**

**Challenger Layoff Report (January)** – Job destruction has continued to trend at a relatively low level in recent months.

**Jobless Claims (week ending January 28)** – Still subject to some seasonal noise, but the underlying trend is moderate.

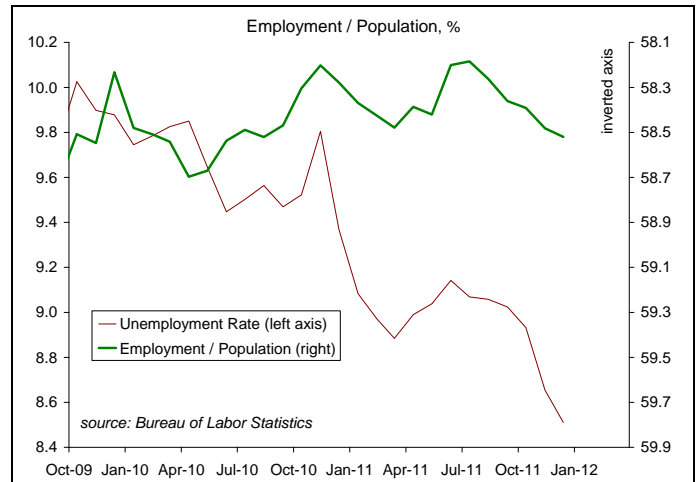
**Productivity (4Q11, preliminary)** – Nonfarm business GDP rose at a 3.6% annual rate in 4Q11, but private-sector hours rose at a 3.0% pace. Hence, productivity growth should be lackluster.

**Friday**

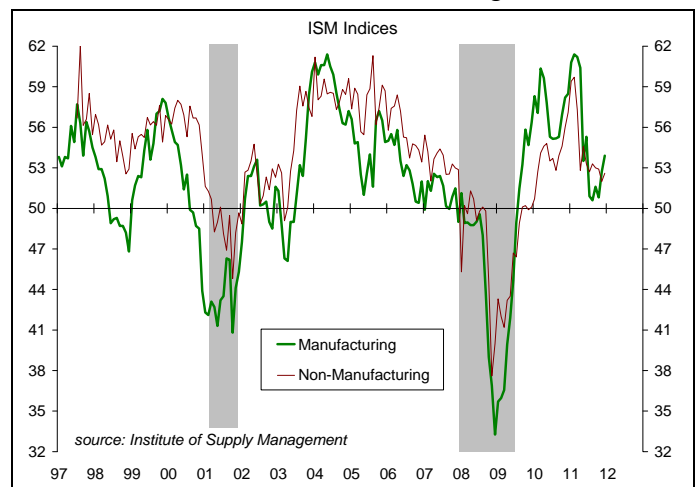


**Employment Report (January)** – Annual benchmark revisions are expected to add 192,000 (or +0.1%) to the March 2011 level of payrolls. Seasonal adjustment is huge in January. We normally shed more than 2.5 million jobs before seasonal adjustment. Seems silly to worry about the nearest 20,000 or so. Delivery personnel jumped 42,200 in December, reflecting seasonal

adjustment issues, which are likely to unwind in January. The unemployment rate is likely to hold steady.



**ISM Non-Manufacturing Index (January)** – The ISM’s other survey will be overshadowed by the Employment Report, but should remain consistent with moderate economic growth overall.



**Next Week ...**

The economic calendar thins out considerably. The bond market will face some supply (the quarterly Treasury refunding).

**Coming Events and Data Releases**

- February 5 Super Bowl (Indianapolis)
- February 14 Retail Sales (January)
- February 17 Consumer Price Index (January)
- February 20 Presidents Day (markets closed)
- March 9 Employment Report (February)
- March 13 FOMC Policy Meeting (no press briefing)
- April 24-25 FOMC Policy Meeting  
Bernanke Press Briefing
- June 19-20 FOMC Policy Meeting  
Bernanke Press Briefing