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The pessimistic global economic outlook continues to dominate market activity, though the negative news-flow of economic data abated somewhat in recent weeks from the pace through June and early July. This is a reversal of upside pressure on economic outlooks through April and May, and we continue to project a slow but positive growth path for the economy from the trough in June of last year. With the mid-year revisions, GDP now looks poised for 3.0% growth in 2010 on both a year-average and Q4/Q4 basis. We still expect growth to edge up to 4% in late 2011 and 2012, as real final sales growth continues to accelerate.

Recent FOMC policy statements have exhibited only a modest drift away from the ultra-accommodative language of the recession. As a result of the recent moderation of growth, the Fed will be reinvesting principal payments from its agency and mortgage-backed securities holdings into longer-term Treasuries.

The July non-farm payroll report showed that overall employment fell by 131,000 jobs during the month, with the unemployment rate holding steady at 9.5%. June's overall employment report was revised to a loss of 221,000 jobs from a loss of 125,000. Private payrolls, which exclude government jobs, rose by 71,000 jobs. June's addition to private payrolls was revised downward to 31,000 new jobs from 83,000. The underemployment rate, which is comprised of part-time workers seeking full-time employment, and people who have sought work but have given up looking, held at 16.5%. The slow economic recovery continues to have a negative impact on job creation.

The overall CPI decreased 0.1% in June. The core CPI, which excludes food and energy, rose 0.2%. The core CPI reading was the strongest since October 2009 and may ease concerns that a slowdown in economic growth will spur deflation.

The unwind of the various housing and factory figures from an April peak (attributable to the homebuyers' tax credit and cash-for-appliances) is now largely dissipating. We expect the flight to quality that has lifted U.S. Treasury prices will unwind through the third quarter, leaving some return to normalcy for bonds, stocks and the dollar. The second-quarter scare to global central banks has clearly spooked the Fed, and we continue to assume that policy will remain accommodative through early next year. Bond yields should rise in advance of the Fed, and we expect a steady climb in yields through 2011 and 2012.

U.S. Forecast Summary

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KEY ECONOMIC INDICATORS	Actual →				Forecast →					Forecast →			
	3Q09	4Q09	1Q10	2Q10	3Q10	4Q10	1Q11	2Q11	3Q11	2009	2010	2011	2012
Gross Domestic Product	1.6%	5.0%	3.7%	2.4%	2.4%	3.5%	3.7%	3.9%	4.1%	-2.6%	3.0%	3.5%	4.1%
Change in Inventory (2000\$, bln)	\$33.6	\$91.5	\$80.8	\$31.6	\$1.2	-\$23.6	-\$8.5	\$41.4	\$0.6	-\$75.5	\$175.7	\$5.8	-\$28.2
Civilian Unemployment Rate	9.7%	10.0%	9.7%	9.7%	9.6%	9.7%	9.6%	9.4%	9.1%	9.3%	9.7%	9.2%	8.1%
Capacity Utilization	69.9%	71.1%	72.5%	73.8%	74.8%	75.6%	76.5%	77.2%	77.9%	70.0%	74.2%	77.5%	79.5%
ISM Index	51.4	54.6	58.2	58.8	55.2	55.7	55.7	55.3	55.0	46.2	57.0	55.3	55.0
ISM Non-Manufacturing Index	48.3	49.4	53.0	54.9	54.3	55.5	56.8	56.6	56.5	46.2	54.4	56.6	56.5
Retail Sales	7.3%	7.5%	8.2%	4.1%	0.5%	5.5%	5.8%	5.4%	5.9%	-6.3%	5.5%	4.9%	5.8%
Michigan Consumer Sentiment	68.4	70.2	73.9	73.9	69.3	73.7	76.9	79.2	80.7	66.3	72.7	79.8	84.1
Total Vehicle Sales (mln units)	11.7	11.1	11.2	11.5	11.9	12.2	12.5	12.9	13.3	10.5	11.7	13.1	15.0
Housing Permits (millions)	0.601	0.626	0.655	0.589	0.595	0.615	0.646	0.705	0.778	0.583	0.614	0.744	1.000
New Home Sales (millions)	0.401	0.373	0.360	0.340	0.340	0.355	0.371	0.391	0.412	0.374	0.349	0.403	0.520
Existing Home Sales (millions)	5.280	5.970	5.140	5.607	4.850	5.025	5.125	5.200	5.275	5.160	5.155	5.238	5.538
S&P Case-Shiller C-20 (Y/Y)	-8.5%	-2.3%	2.0%	0.0%	-2.5%	-1.3%	2.4%	1.3%	0.5%	-11.4%	-0.5%	1.2%	2.6%
WTI Oil Price	\$68.20	\$76.07	\$78.63	\$77.89	\$79.07	\$79.53	\$83.75	\$92.45	\$95.53	\$61.69	\$78.78	\$91.55	\$109.25
CPI	3.7%	2.6%	1.5%	-0.7%	0.8%	1.6%	1.8%	1.8%	2.0%	-0.3%	1.5%	1.5%	2.3%
CPI (Y/Y)	-1.6%	1.4%	2.4%	1.8%	1.0%	0.7%	0.8%	1.4%	1.7%	2.7%	0.7%	1.9%	2.4%
CPI Core (Y/Y)	1.4%	1.7%	1.3%	0.9%	1.0%	0.9%	1.2%	1.3%	1.3%	1.8%	0.9%	1.5%	1.9%
PPI	3.2%	6.2%	8.6%	-0.3%	-0.6%	3.0%	2.7%	2.7%	2.9%	-2.5%	3.9%	2.2%	3.2%
PPI (Y/Y)	-5.4%	1.4%	4.9%	4.5%	3.5%	2.7%	1.2%	2.0%	2.8%	4.3%	2.0%	2.9%	3.3%
Fed Funds Rate	0.07%	0.05%	0.09%	0.09%	0.18%	0.18%	0.18%	0.50%	1.00%	0.16%	0.16%	0.65%	2.94%
2-Year Note Yield	0.95%	1.14%	1.02%	0.61%	0.80%	1.00%	1.25%	1.65%	2.20%	0.95%	0.82%	1.80%	3.29%
10-Year Note Yield	3.31%	3.85%	3.84%	2.97%	3.15%	3.45%	3.60%	3.75%	3.90%	3.29%	3.35%	3.76%	4.19%

Source: Action Economics

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