

Weekly guidebook for the global investor



Macro viewpoint: Did payrolls decline 51,000 or 580,000?

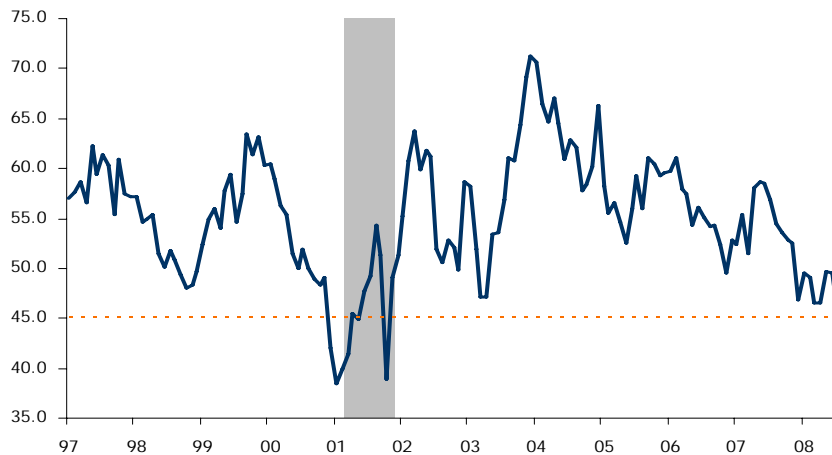
Nonfarm payrolls declined 51,000 in July, the seventh consecutive monthly decline with the damage thus far adding up to 463,000 net layoffs. To be sure, the headline decline was not as bad as consensus view of down 70,000, but for all practical purposes, payrolls might as well have fallen 580,000 in terms of what this overall employment report actually meant for the economy.

The week ahead: Growth & employment take center stage

The Federal Reserve FOMC convenes next week to ponder the future direction of monetary policy. We and the consensus expect no change in the funds rate, though there is still a chance of a dissent, or two, from hawkish committee members. After wading through a hefty economic data calendar, investors will have some respite in the week ahead, with just a handful of indicators on the docket.

New orders crater to a seven-year low

ISM Manufacturing: New orders index (50+ = increasing)



Shaded region represents period of US recession
Source: Institute for Supply Management, Merrill Lynch

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Macro viewpoint

Did payrolls decline 51,000 or 580,000?

The damage thus far has totaled 463,000 net layoffs

Nonfarm payrolls declined 51,000 in July, the seventh consecutive monthly decline with the damage thus far adding up to 463,000 net layoffs. To be sure, the headline decline was not as bad as consensus view of down 70,000, but for all practical purposes, payrolls might as well have fallen 580,000 in terms of what this overall employment report actually meant for the economy.

Aggregate hours worked down four months in a row

What are we talking about? The fact that together with the moderate net job downsizing, companies cut the hours for the rest of us who are still working to an average of 33.6 hours per week. This was the least amount of time people spent on the job in nearly four years. So the really critical number in this report was aggregate hours worked, which takes into account both inputs to the labor market, bodies and hours, contracted 0.4% (equivalent to a 580,000 payroll plunge had hours not fallen) and are now down four months in a row. That is a losing streak generally saved for recessions (last time was during the 2001-02 downturn), which we continue to believe began no later than January of this year (and not likely to end before mid-2009). As Chart 2 illustrates, never before have aggregate hours worked been as weak as they are today without the economy being in a full-blown recession, and not being “new era” enthusiasts, we aren’t prepared to say it’s going to be different this time.

Companies likely to cut bodies not hours going forward

The private workweek itself is now down to an average of 33.6 hours, which is rock bottom. It doesn’t get lower than that. In fact, not once in the 44-year history of the data series have hours worked been lower than they are today. This leads us to believe that going forward, any reduction in demand and order books is going to be met disproportionately by cuts in headcount rather than cuts in hours, which companies had been relying on, but that strategy has run its course.

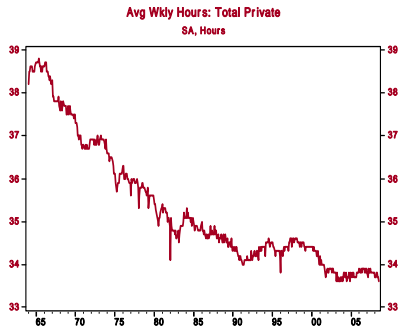
We could be entering a new range on payroll losses

Temp agencies trimmed their own head count by 29,000 in July on top of 88,000 in the prior three months in a clear-cut sign that they see the same rapid compression in labor demand ahead as we do. Indeed, the latest jump in jobless claims to a five-year high of 448,000 suggests that in the next few months, we could be seeing the nonfarm payroll losses moving into an entire new range of 150,000 to 200,000, during which time we would expect to see bond yields and equity valuations re-testing their cycle lows, and any residual Fed tightening expectations vanish completely from the Eurodollar strips.

The headline was the only real surprise

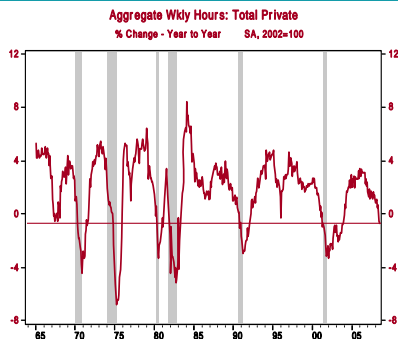
The only real surprise in the employment report was the headline – and it was due to a 25,000 gain in government jobs; not to mention our seasonal adjustments, which indicated that the Birth-Death model yet again added 30,000 to the nonfarm tally last month. Outside of the burst in the civil service, private sector employment declined 76,000 – right in line with consensus and yet again making a mockery of the ADP release.

Chart 1: Hours worked down to record low levels



Source: Bureau of Labor Statistics, Haver Analytics, Merrill Lynch

Chart 2: Aggregate hours worked in recession terrain



Source: Bureau of Labor Statistics, Haver Analytics, Merrill Lynch

Plurality of industries shedding labor

In stock market parlance, the internals in this report were awful. The diffusion index fell to 41.2 from 42.2 in June and 46.4 in May, the lowest since May 2003 when the funds rate was last on its way to 1%. This metric tells you that the plurality of industries is now shedding labor.

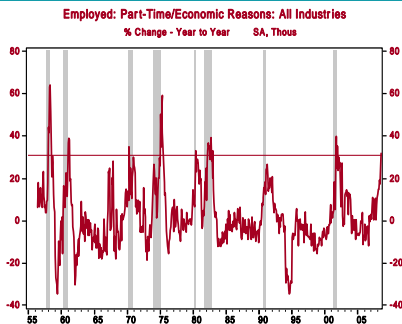
Absolutely no sign of wage acceleration

Even with the boost to the minimum wage, there is absolutely no sign of any wage acceleration. In fact, the combination of the lower workweek and stagnant wage growth meant that the income proxy in the payroll report – average weekly earnings – was flat in nominal terms and very likely negative 0.5% in real terms. Combining the hours worked figure, wage number and inflation (including our July estimate), this proxy of total real income has fallen at nearly a 7% annual rate over the past three months, the worst performance since 1990, where only two months posted larger declines.

Slack is sharply building in the labor market

This is what is critical – income fundamentals in the consumer sector are steadily deteriorating; the difference now is that there are no more tax rebates to keep spending afloat. With the unemployment rate heading up to 5.7% from 5.5%, the highest level in 4 1/2 years, and we believe on a track to 7% next year, be assured that organic income growth is going to become even more *challenged* in coming quarters. In fact, the headline unemployment rate actually understates the degree of slack that is building up in the labor market – the U-6 measure of unemployment, which includes all measures of unutilized resources, has soared from 9.2% in April to 10.3% in July in the sharpest increase over a three-month span since November 2001.

Chart 3: Working part-time for economic reasons – up 32% year-over-year



Source: Bureau of Labor Statistics, Haver Analytics, Merrill Lynch

More people working part-time for economic reasons

One measure of *slack* or *excess capacity* that is mounting in the jobs market, which is not captured in the headline unemployment number but is certainly an important metric for any labor economist, is the number of people working part-time for *economic reasons*. This metric surged 5.7% (a 94% annual rate!) in July. Those who are working part-time because they can't find a full-time job due to the weak economy has surged 32% in the past year – another tried, tested and true recession barometer. And, their share of the employment pie has climbed to 3.8%, which is the highest since December 1993 when the headline unemployment rate was sitting at 6.5%. That's where we are headed.

Nothing has bottomed just yet

We are on the precipice of the first consumer recession since 1990-91 and in our view, potentially the most severe since the six-quarter turndown from 1973-75. If that is the case, the S&P 500 is still only 40% priced for such an outcome; the consumer discretionary group is priced barely 50%; and financials 75% of the way. From our vantage point, nothing has bottomed just yet.

David Rosenberg, North American Economist, Merrill Lynch, +1 212 449 4937

Key market movers

The week ahead

Highlight of the week: Tuesday FOMC meeting

The FOMC meeting is widely expected to produce an unchanged Fed funds rate, but the tone of the statement may garner some attention

The Federal Reserve FOMC convenes next week to ponder the future direction of monetary policy. We and the consensus expect no change in the funds rate, though there is still a chance of a dissent, or two, from hawkish committee members. After wading through a hefty economic data calendar, investors will have some respite in the week ahead, with just a handful of indicators on the docket.

A scattering of economic reports

Key economic reports released in the week ahead include second quarter productivity and costs, consumer income, spending and inflation for June and the ISM Non-manufacturing data for July. Given the recent elevated weekly prints, the unemployment claims report is also likely to cause some stir in the markets.

Solid productivity but at the expense of employees

Productivity growth is seen rising 2.2% Q/Q at an annualized rate in 2Q. Though this will be slightly weaker than an upwardly revised 2.7% gain in 1Q, the 2Q yearly pace of 3.2% will be an impressive pace in light of the material slowing in economic activity. Thus, not surprisingly, we expect unit labor costs to post a rather benign 1.2% quarterly annualized gain that will merely edge the year on year rate up to 0.5%.

Expect another claims shocker

We remain out of consensus on our expectations for the weekly jobless claims figures and it largely centers on our read of the recent statistical quirks in the data. We expect claims to be about unchanged at 450K, reflecting a material deterioration in labor market conditions. The BLS has speculated that the recent jump has more to do with the government's new extended UI program, but we have reason to believe the numbers are clean and that the new trend has been established at the 425k to 450k level. That translates into deeper declines in monthly payrolls in the months ahead.

Core PCE to tick higher in June

We expect the core PCE price index to rise 0.2% MoM in June, which will bump the yearly rate up to 2.3% from 2.2%. The forces of weakening demand will in our view soon start to overwhelm any pass through cost pressure. We expect core and headline inflation to be converging back towards the 2% threshold by early next year.

Fed on hold, hawks have less ammo

The FOMC meeting is widely expected to produce an unchanged Fed funds rate, but the tone of the statement may garner some attention. This will be the first unified communiqué from the Fed since they and the Treasury department made the implied G-stamp on Fannie and Freddie a bit more indelible. We expect the economic outlook to remain largely unchanged though we may detect slightly less concern on the inflation front. Oil prices have slid nearly \$15 from the lofty levels at the time of the June 30 confab and the CRB commodity price index is down more than 10%. While the hawkish presidents on the committee will no doubt attempt a more forward looking case, with signs emerging that the commodity complex is succumbing to the downturn in global economic activity, their opinions will likely have much less sway on any middle-of-the-road voters.

Monday, 4 August

Personal Income & Outlays, June—8:30am

	Exp	Cons	Range	History
Personal Income	0.3%	-0.2%	-0.8 to 1.2%	May = 1.9% vs. Apr = 0.3%
Personal Spending	0.6%	0.4%	-0.5 to 0.9%	May = 0.8% vs. Apr = 0.4%
Core PCE (YoY)	2.3%	2.2%	2.2 – 2.3%	May = 2.1% vs. Apr = 2.1%

Source: Merrill Lynch, Bloomberg

We expect the core PCE price index to rise 0.2% MoM in June, which will bump the yearly rate up to 2.3% from 2.2%. The core PCE price index increased by 2.1% QoQ annualized rate in 2Q, above our tracking estimate for 1.8%. We expect this difference to be reflected in higher April and May readings (previously reported +0.1%MoM), or possibly in June. Our outlook for slower economic growth into 2009, suggests that core inflation will peak in 3Q 2008 and decelerate thereafter. Note, that if the entire revision is incorporated into June, an unlikely event, we would see an outsized 0.4% MoM gain and a corresponding YoY rate of 2.4% (versus the recent trend of 2.1% YoY).

Consumer spending (in nominal terms) is expected to rise 0.3% MoM in June following a 0.8% gain in May. This slower pace is in-step with the weak monthly reading in retail sales over the month, which also reflected that most spending went into basic necessities. A hefty portion of the rebate checks were delivered up to June totaling almost \$80 billion. However, our estimates suggest that consumers probably spent very little of these checks, opting instead to save or pay down debt. Real disposable income is forecast to post a 2.1% MoM decline in June after rising by 5.0% MoM in May, as less rebate checks were sent out to households in June than in May. We expect the savings rate to drop from 5% in May to 2.5% in June, which is still a significant rise from close to zero at the start of the year.

Factory Orders, June—10:00am

	Exp	Cons	Range	History
Factory Orders	0.8%	0.7%	-0.2 to 2.0%	May = 0.6% vs. Apr = 1.3%

Source: Merrill Lynch, Bloomberg

Factory orders are expected to rise 0.8% MoM in June following a 1.2% gain May. The advance report for durable goods in June showed a 0.8% monthly gain in orders heavily boosted by defense equipment. Gains were limited to metals, machinery, electrical equipment/appliances and autos over the month, while technology and aircraft industries declined. Still, private non-defense ex-air orders rose 1.5% MoM in June and are a figure we will be watching for revisions to in this report. Orders for non-durable goods -- the key missing component thus far -- is forecast to rise 0.8% over the month. Price gains will likely play an important role one more in this sub-category as indicated by the 3.0% increase in the PPI for nondurable goods.

Tuesday, 5 August

ISM Nonmanufacturing Index, July—10:00am

	Exp	Cons	Range	History
ISM Nonmanufacturing	48.0	48.8	47 – 52.5	Jun = 48.2 vs. May = 51.7

Source: Merrill Lynch, Bloomberg

The ISM non-manufacturing index likely eased from 48.0 in July from 48.2 in June, extending a trend that has seen this index remain right around the 50-mark since the beginning of the year. Weakness in the services and construction sectors was generally widespread, according to the Beige Book, as well as the latest homebuilder sentiment (NAHB index now at an all-time low of 16). In addition, the Richmond Fed's services revenue index (which has a moderate 57% correlation to the ISM non-manufacturing index) also eased one point to -15 in July, a five-year low. Employment prospects have also been soft, as was attested to in the near-five year high on the unemployment rate, as well as the latest week's jump in jobless claims. Price pressures shot up to 84.5 in June, the highest in the 11-year history of the series, but will probably ease somewhat in July.

Thursday, 7 August

Initial Jobless Claims, week ending 08/02/08—8:30am

	Exp	Cons	Range	History
Initial Claims	450K	420K	390 – 463K	July 26 th = 448K

Source: Merrill Lynch, Bloomberg

Initial claims for unemployment benefits for the week ending August 2nd are expected to remain essentially unchanged at 450K versus the prior week. The Department of Labor noted that the 44K gain in the previous week was influenced to the upside by the UI extension bill (pass by Bush at the end of June to extend benefits for those unemployed beginning July 1st). The BLS speculated that claimants came forward (after receiving notice that they may potentially qualify for the extension benefit program from their state office) who did not actually qualify for extended UI program, but who did file a new initial claim. The numbers which did more clearly reflect the impact of the UI bill were the continuing claims, which rose 185K WoW in the 2nd of week of July to 3.28mln. Looking forward, we expect that both initial and continuing claims will trend at these recently higher levels reflecting both deterioration in labor markets as well as higher ongoing benefits for those unemployed. We expect these trends to show up in a higher unemployment rate and deepening declines in monthly payrolls.

Consumer Credit, June—3:00pm

	Exp	Cons	Range	History
Consumer Credit	\$3.5bn	\$6.4bn	\$3 – 8.0bn	May = \$7.8bn vs. Apr = \$7.8bn

Source: Merrill Lynch, Bloomberg

We expect consumer credit outstanding to rise by a below-consensus \$3.5bn MoM in June, a substantial slowdown from the average \$9.4bn year-to-date. Rebate checks are expected to allow households to pay down some of their high interest credit card debt. Through the two prior periods of stimulus in 2001 and 2003, we saw notably weaker consumer credit growth, with credit card debt, on net, being paid down. Nonetheless, the slowing in credit growth is expected to be temporary, as consumers are likely to resume tapping different sources of financing purchases, including revolving credit, as well as home equity borrowing. The latter accelerated in June, rising \$6.1bn, following a gain of \$5.4bn in May. Non-revolving credit, including loans for big ticket items such as cars, probably posted small declines, as spending in these areas remains weak.

Friday, 8 August

Productivity & Costs, 2Q (P)—8:30am

	Exp	Cons	Range	History
Nonfarm Productivity	2.2%	2.5%	0.7 – 3.5%	1Q = 2.6% vs. 4Q = 1.8%
Unit Labor Costs	1.2%	1.4%	-1.2 to 3.0%	1Q = 2.2% vs. 4Q = 4.7%

Source: Merrill Lynch, Bloomberg

The data released in this report will include revisions from 1Q05 through 1Q08, as the BLS incorporates the new figures released in last week's GDP report. All of our forecasts for 2Q are based off these changes levels.

Nonfarm business sector productivity is expected to rise 2.2% Q/Q at an annual rate in 2Q following what we expect to be a 2.7% gain in 1Q. Output is seen posting a strong gain of 1.7% over the quarter given a boost in consumer spending from stimulus checks and solid growth in exports and business investment. We expect to see a 0.5% annualized drop in employee hours worked in 2Q, marking the fourth consecutive quarterly decline -- a trend typically seen only in recessions and partially the reason that productivity has remain strong thus far. The ongoing surge in input costs (raw material prices in particular) has pressured firms to cut employee hours worked as opposed to raising end-product prices (difficult to pass-through in the generally weak domestic environment). On a year-over-year basis, productivity growth will likely come in at 3.2% marking a slowing from what we expect will be an impressive 3.8% in 1Q. Hours are set to decline by -0.5% in 1Q after falling 1.8% in 2Q (we do not anticipate any material revision to hours worked).

Nonfarm compensation is estimated to rise by 3.4% at an annual rate in 2Q, while unit labor costs register a 1.2% annualized gain. We expect the yearly rate to rise to a scant 0.5% from what we expect will be a downwardly revised -0.6% in 1Q.

Wholesales Inventories, June—10:00am

	Exp	Cons	Range	History
Wholesale Inventories	1.3%	0.6%	-1.4 to 1.3%	May = 0.8% vs. Apr = 1.4%

Source: Merrill Lynch, Bloomberg

Wholesale inventories are forecast to rise 1.3% MoM in June versus consensus estimates of 0.6%. Prices are likely to play a significant role in this months' report, as has been the case YTD. Gains are expected in the energy, metals and chemicals industries where higher commodity prices will boost the value.

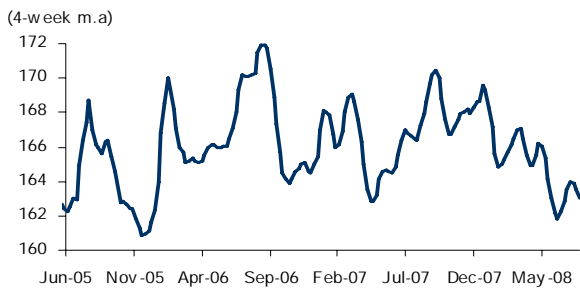
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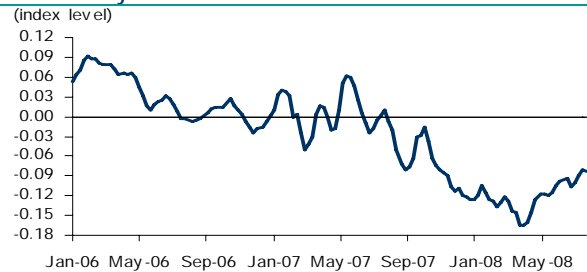
Merrill Lynch proprietary indicators

The Merrill Lynch production index



Our production index fell for the third consecutive week and is off about 0.3% from June, indicating weak industrial production in July. While the details in our index were mixed, we saw intense weakness across a number of components. Truck and auto production continued to drop sharply, down 6.2% and 1.6%, respectively. Electrical production sank 0.6%, the fourth consecutive weekly decline. Some components managed to increase in the latest week. Among them was raw steel production, which rose 0.3% – matching the increase seen the week before. Coal production was up as well, rising 0.8% on top of a 2.8% increase. Railcar loadings were up 0.3%, the fourth consecutive increase. Finally, crude oil production rose for the third week in a row, up 0.3%.

The Merrill Lynch consumer index



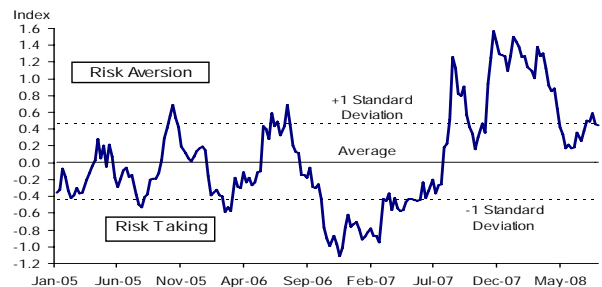
Our consumer index fell for the first time in four weeks. This week marks a full-year that the index has camped in negative territory. The latest data indicate that the consumer has weakened sharply. The labor market deteriorated markedly in the latest week. Initial jobless claims spiked to 448,000, the highest level since April 2003. Continuing claims rose in the latest week too suggesting it's getting increasingly difficult to find work once out of a job. That will put upward pressure on the unemployment rate going forward. This makes it no surprise that consumer confidence broke to a nine-week low. Crude oil prices, despite the latest sell-off, remain elevated. Finally, in addition to their homes, consumer equity assets remain deflated. In fact, the S&P 500 is running below its two-year average.

The Merrill Lynch housing index



Our housing index rose fractionally in the latest week but has now spent a full year in negative territory and that is where the index is likely to remain as the housing market continues to search for a bottom. The four-week moving average on initial jobless claims rose for the second week in a row while the four-week average on continuing claims spiked to their highest level since January 2004. The MBA's purchase index is running below its one-year average, reflecting a meaningful pullback in the demand for housing. And, in a sign of tight credit conditions, commercial bank real estate loans continue to run below their one-year average. Finally, the rates on 30-year conventional mortgages are about where they were this time last year, which means that the private sector is not feeling the effects of the Fed's rate relief.

The Merrill Lynch financial stress index



Our financial stress index was flat in the latest week and remains at the edge of risk aversion territory suggesting that financial market conditions have not returned to normal. Baa spreads, for example, ticked up in the latest week. Two-year swap spreads, were flat in the latest week but remain above their one-year average. Meanwhile, investors continue to rotate away from equities. In fact, Treasuries outperformed the S&P 500 in the latest week. There are however, signs of risk taking. For example, the VIX index, a measure of equity market volatility dipped in the latest week and is now below its one-year average. The price of gold has come off sharply as well and is at its lowest level in five weeks.

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Debt issuance

Treasury financing (billions of \$)

<u>Announcement date</u>	<u>Auction date</u>	<u>Settlement date</u>	<u>Issue</u>	<u>Size</u>	<u>New cash</u>
31-Jul	4-Aug	7-Aug	3-month	25.0	
31-Jul	4-Aug	7-Aug	6-month	24.0	
4-Aug	5-Aug	7-Aug	4-week	24.0*	
7-Aug	11-Aug	14-Aug	3-month	22.0*	
7-Aug	11-Aug	14-Aug	6-month	21.0*	
30-Jul	6-Aug	15-Aug	10-year	17.0	
30-Jul	7-Aug	15-Aug	30-year (R)	10.0	

* Estimate. () = Paydown. (R) = Reopening. CMB = Cash Management Bill. ** New cash for combined 2 and 5-year note auction
 Source: Bloomberg, U.S. Treasury, Merrill Lynch

Agency financing (billions of \$)

<u>Announcement date</u>	<u>Auction date</u>	<u>Settlement date</u>	<u>Issue</u>	<u>Size</u>
1-Aug	4-Aug	5-Aug	FRE 3-month	
1-Aug	4-Aug	5-Aug	FRE 6-month	
4-Aug	6-Aug	7-Aug	FNM 3-month	
4-Aug	6-Aug	7-Aug	FNM 6-month	
8-Aug	11-Aug	12-Aug	FRE 3-month	
8-Aug	11-Aug	12-Aug	FRE 6-month	

FRE = Freddie Mac, FNM = Fannie Mae, (R) = Reopening
 Source: Bloomberg, Freddie Mac, Fannie Mae.

Policy speakers

Key speaking engagements and news events*

<u>Monday, August 4</u>	<i>None scheduled at this points</i>
<u>Tuesday, August 5</u>	<i>2:15 pm FOMC Rate Decision Expected</i>
<u>Wednesday, August 6</u>	<i>None scheduled at this points</i>
<u>Thursday, August 7</u>	<i>None scheduled at this points</i>
<u>Friday, August 8</u>	<i>None scheduled at this points</i>

*Time and date subject to change
 Source: Bloomberg, Market News, Merrill Lynch

Economic forecast summary

Real Economic Activity, % SAAR	4Q2007	1Q2008	2Q2008	3Q2008	4Q2008	1Q2009	2Q2009	3Q2009	4Q2009	2007	2008F	2009F
Real GDP	-0.2	0.9	1.9	1.2	-2.5	-2.3	-0.5	2.0	2.5	2.0	1.4	-0.5
% Change, Year Ago	2.3	2.5	1.8	0.9	0.4	-0.4	-1.0	-0.8	0.4			
Final Sales	0.8	0.9	2.4	0.0	-2.4	-2.3	-0.1	1.4	2.5	2.4	1.4	-0.6
Domestic Demand	-0.1	0.1	1.3	-0.2	-2.4	-3.3	-0.8	1.1	2.3	1.8	0.5	-1.1
Consumer Spending	1.0	0.9	1.5	0.2	-3.0	-2.4	0.0	1.8	2.5	2.8	0.9	-0.7
Durables	0.4	-4.3	-3.0	-0.7	-18.5	-10.0	0.5	2.5	3.5	4.8	-2.3	-6.0
Nondurables	0.3	-0.4	4.0	-3.5	-6.0	-3.5	-3.0	1.5	2.0	2.5	0.1	-2.5
Services	1.4	2.4	1.1	2.3	1.3	-0.5	1.3	1.8	2.5	2.6	1.8	1.1
Residential Investment	-27.0	-25.0	-15.6	-13.9	-20.2	-21.0	-7.9	4.4	5.1	-17.9	-20.8	-12.9
Nonresidential Investment	3.4	2.4	2.4	-2.0	-1.2	-12.3	-8.7	-5.5	1.6	4.9	3.0	-5.7
Structures	8.6	8.7	13.9	-5.1	-9.0	-10.8	-8.0	-5.0	1.0	12.7	8.5	-6.4
Equipment and Software	1.0	-0.5	-3.4	-0.4	3.0	-13.0	-9.0	-5.8	2.0	1.7	0.4	-5.4
Government	0.8	1.9	3.6	1.5	1.9	1.7	1.8	1.8	1.6	2.1	2.3	1.9
Exports	4.4	5.1	9.2	5.2	4.8	3.0	2.8	3.2	2.4	8.4	8.0	3.9
Imports	-2.3	-0.8	-6.6	2.6	2.5	-4.0	-2.4	1.0	1.5	2.2	-1.3	-0.9
Net Exports (Bil 00\$)	-484.5	-462.0	-395.1	-388.0	-381.7	-349.9	-327.2	-319.4	-317.0	-546.5	-406.7	-328.4
Inventory Accumulation (Bil \$)	-8.1	-10.2	-62.2	-26.1	-29.3	-29.3	-40.1	-25.3	-26.5	-2.5	-32.0	-30.3
Nominal GDP (Bil \$)	14031	14151	14257	14428	14471	14467	14469	14564	14692	13808	14327	14548
% SAAR	2.3	3.5	3.0	4.9	1.2	-0.1	0.1	2.7	3.6	4.8	3.8	1.5
% Change, Year Ago	4.9	4.7	3.8	3.4	3.1	2.2	1.5	0.9	1.5			
Key Indicators												
Industrial Production (% SAAR)	0.2	0.6	-3.2	-1.4	-6.4	-7.2	-2.8	1.0	1.5	1.7	-0.4	-3.7
Capacity Utilization (%)	81.0	80.6	79.8	79.2	77.5	75.8	74.9	74.8	74.8	81.0	79.3	75.1
Civilian Unemployment Rate (%)	4.8	4.9	5.3	6.2	6.5	6.7	7.0	7.0	6.8	4.6	5.7	6.9
Productivity (% SAAR)	2.2	2.7	2.2	2.9	-0.7	0.4	2.5	3.1	2.5	1.8	0.7	2.4
% Change, Year Ago	3.1	3.8	3.2	2.5	1.8	1.2	1.3	1.3	2.1			
Real Disp. Personal Inc. (% SAAR)	0.6	-0.1	11.3	-4.7	-4.4	1.0	2.2	2.9	3.0	2.8	1.6	0.4
% Change, Year Ago	1.8	0.7	3.6	1.6	0.3	0.6	-1.5	0.4	2.3			
Personal Savings Rate (%)	0.4	0.3	2.6	1.3	0.9	1.3	1.9	2.3	2.7	0.6	1.3	2.1
Light Vehicle Sales (Millions SAAR)	16.2	15.3	14.1	13.6	12.8	12.8	13.5	13.8	14.0	16.4	14.0	13.5
Housing Starts (Thous. SAAR)	1151	1053	1016	880	730	675	750	795	820	1341	920	760
Current Account (Bil \$)	-167.2	-176.4	-184.3	-205.8	-201.5	-192.2	-178.5	-177.6	-182.4	-731.2	-768.0	-730.7
U.S. Budget Balance (Bil \$)										-163	-425	-500
Corporate Profits and Earnings												
Operating Corp. Profits After Tax (Bil \$)	1177.6	1190.6	1133.6	987.7	854.9	896.5	910.8	940.8	993.2	1192.1	1041.7	935.3
% Change, Year Ago	-0.6	1.8	-5.9	-18.9	-27.4	-24.7	-19.7	-4.8	16.2	8.4	-12.6	-10.2
S&P 500 Reported EPS (\$)	7.8	15.5	17.0	12.5	10.7	12.2	12.6	12.3	14.0	66.2	55.8	51.0
% Change, Year Ago	-61.4	-27.1	-22.3	-17.5	37.1	-21.7	-25.8	-1.7	30.3	-18.8	-15.7	-8.5
S&P 500 Operating EPS (\$)	15.2	16.6	18.8	16.7	15.8	15.0	15.5	15.7	16.8	82.5	68.0	63.0
% Change, Year Ago	-30.8	-25.8	-21.7	-20.0	3.8	-9.7	-17.8	-6.0	6.6	-5.9	-17.7	-7.2
Inflation												
GDP Price Index (% SAAR)	2.8	2.6	1.1	3.7	3.7	2.2	0.5	0.7	1.1	2.7	2.4	2.0
% Change, Year Ago	2.6	2.3	2.0	2.6	2.8	2.7	2.5	1.8	1.1			
CPI, Consumer Prices (% SAAR)	5.0	4.3	5.0	7.3	3.9	1.4	-2.1	0.5	1.1	2.9	4.8	2.0
% Change, Year Ago	4.0	4.2	4.3	5.4	5.1	4.4	2.6	0.9	0.2			
CPI ex Food & Energy (% SAAR)	2.5	2.5	1.9	3.2	2.7	2.0	1.5	1.4	1.7	2.3	2.4	2.1
% Change, Year Ago	2.3	2.4	2.3	2.5	2.6	2.4	2.3	1.9	1.7			

Source: Merrill Lynch

01 August 2008

Interest rate forecast summary

(% EOP)	4Q 07	1Q 08	2Q 08	3Q 08	4Q 08	1Q 09	2Q 09	3Q 09	4Q 09	2007	2008	2009
Fed Funds	4.25	2.25	2.00	2.00	2.00	1.50	1.50	1.50	2.00	4.25	2.00	2.00
3-Month T-Bill	3.36	1.38	1.74	1.65	1.60	1.40	1.25	1.45	1.90	3.36	1.60	1.90
3-Month LIBOR	4.85	2.95	2.78	2.80	2.75	2.15	2.05	1.95	2.35	4.85	2.75	2.35
2-Year T-Note	3.04	1.62	2.62	2.60	2.25	1.95	1.65	2.05	2.30	3.04	2.25	2.30
5-Year T-Note	3.45	2.46	3.33	3.45	3.20	2.75	2.40	2.60	2.85	3.45	3.20	2.85
10-Year T-Note	4.05	3.45	3.97	4.15	3.90	3.65	3.25	3.50	3.65	4.05	3.90	3.65
30-Year T-Bond	4.45	4.30	4.53	4.75	4.50	4.25	3.75	3.90	4.00	4.45	4.50	4.00

Shaded regions represent Merrill Lynch forecast.

Source: Merrill Lynch

Monthly CPI forecast update

	Total CPI					Core CPI			
	(nsa)		(sa)			(nsa)		(sa)	
2008: Apr	214.823	0.61	3.9	0.21	3.9	0.09	2.3	0.10	2.3
2008: May	216.632	0.84	4.2	0.65	4.1	0.06	2.3	0.20	2.3
2008: Jun	218.815	1.01	5.0	1.06	4.9	0.17	2.4	0.32	2.4
2008: Jul	219.168	0.16	5.2	0.53	5.2	0.16	2.4	0.25	2.4
2008: Aug	219.394	0.10	5.5	0.31	5.5	0.27	2.5	0.26	2.5
2008: Sep	219.955	0.26	5.5	0.35	5.5	0.27	2.6	0.25	2.6
2008: Oct	220.565	0.28	5.6	0.33	5.6	0.37	2.6	0.22	2.6
2008: Nov	220.534	-0.01	4.9	0.29	4.9	0.00	2.6	0.18	2.6
2008: Dec	220.287	-0.11	4.9	0.31	4.9	-0.08	2.5	0.18	2.5
2009: Jan	220.763	0.22	4.6	0.11	4.6	0.23	2.4	0.18	2.4
2009: Feb	221.470	0.32	4.6	0.06	4.6	0.43	2.5	0.13	2.5
2009: Mar	221.995	0.24	4.0	-0.28	4.0	0.45	2.4	0.14	2.4

nsa: not seasonally adjusted, sa: seasonally adjusted

Source: Merrill Lynch

FX rate forecast summary

(end of period)		Spot	Sep 08	Dec 08	Mar 09	Jun 09	Sep 09	Dec 09
Euroland Euro	US\$/Euro	1.56	1.51	1.48	1.42	1.40	1.38	1.33
Japanese Yen	¥/US\$	108	103	102	100	98	98	98
	¥/Euro	167	156	151	142	137	135	130
British Pound	US\$/£	1.97	1.91	1.87	1.82	1.82	1.82	1.75
	£/Euro	0.79	0.79	0.79	0.78	0.77	0.76	0.76
Swiss Franc	SF/US\$	1.05	1.05	1.07	1.10	1.10	1.12	1.16
	SF/Euro	1.63	1.59	1.58	1.56	1.54	1.54	1.54
Canadian \$	C\$/US\$	1.02	1.04	1.06	1.08	1.11	1.12	1.12
Australian \$	US\$/A\$	0.93	0.91	0.84	0.80	0.74	0.72	0.70
Chinese Renminbi	RMB/US\$	6.84	6.75	6.70	6.60	6.60	6.50	6.50
Hong Kong \$	HK\$/US\$	7.80	7.75	7.75	7.75	7.75	7.75	7.75
Korean Won	KRW/US\$	1015	1000	975	950	975	1000	1000
Singapore \$	SGD/US\$	1.37	1.33	1.32	1.32	1.32	1.32	1.33
Taiwan \$	TWD/US\$	30.77	30.25	30.00	30.25	30.50	30.75	31.00
Brazilian Real	BRL/US\$	1.56	1.65	1.70	1.75	1.75	1.80	1.80
Mexican Peso	MXN/US\$	9.96	10.90	10.80	10.90	11.00	11.20	11.00

Spot prices are as of Friday morning

Source: Merrill Lynch FX Strategy Team., Bloomberg

Rolling Calendar of Business Indicators

Monday	Tuesday	Wednesday	Thursday	Friday
4 August 8:30 am: Personal Income Apr 0.3% May 1.9% Jun 0.3%* 8:30 am: Personal Spending Apr 0.4% May 0.8% Jun 0.6%* 8:30 am: Core PCE (YoY) Apr 2.1% May 2.1% Jun 2.3% 10:00 am: Factory Orders Apr 1.3% May 0.6% Jun 0.8%	5 August ABC/Washington Post Consumer Comfort Survey —(week ending 8/2/08) LJR Redbook —(week ending 8/1/08) 10:00 am: ISM Nonmanufacturing May 51.7 Jun 48.2 Jul 48.0* 2:15 pm: FOMC Rate Decision <i>expected</i>	6 August MBA Mortgage Applications —(week ending 8/1/08)	7 August 8:30 am: Initial Jobless Claims —(week ending 8/2/08) – 450k* 10:00 am: Pending Home Sales – Jun Apr 7.1% May 4.7% 3:00 pm: Consumer Credit Apr \$7.8bn May \$7.8bn Jun \$3.5bn	8 August 8:30 am: Nonfarm Productivity 4Q 1.8% 1Q 2.6% 2Q (P) 2.2%* 8:30 am: Unit Labor Costs 4Q 4.7% 1Q 2.2% 2Q (P) 1.2%* 10:00 am: Wholesale Inventories Apr 1.4% May 0.8% Jun 1.3%
11 August	12 August ABC/Washington Post Consumer Comfort Survey —(week ending 8/9/08) LJR Redbook —(week ending 8/8/08) 8:30 am: Trade Balance Apr -\$60.5bn May -\$59.8bn Jun -\$65.7bn* 2:00 pm: Treasury Statement Jul 2007 \$170.4bn Jul 2008 -\$56.0bn*	13 August MBA Mortgage Applications —(week ending 8/8/08) 8:30 am: Import Prices May 2.6% Jun 2.6% Jul 1.0%* 8:30 am: Retail Sales May 0.8% Jun 0.1% Jul 0.7%* 8:30 am: Retail Sales ex Autos May 1.2% Jun 0.8% Jul 0.8%* 10:00 am: Business Inventories Apr 0.5% May 0.3% Jun 0.8%*	14 August 8:30 am: Initial Jobless Claims —(week ending 8/9/08) 8:30 am: CPI May 0.6% Jun 1.1% Jul 0.5%* 8:30 am: Core CPI May 0.2% Jun 0.3% Jul 0.2%*	15 August 8:30 am: Empire Manufacturing Jun -8.7 Jul -4.9 Aug -1.0* 9:00 am: TIC Data – Jun Apr \$111.9bn May \$67.0bn 9:15 am: Industrial Production May -0.2% Jun 0.5% Jul -0.3%* 9:15 am: Capacity Utilization May 79.6 Jun 79.9 Jul 79.5%* 10:00 am: University of Michigan Consumer Sentiment Jun 56.4 Jul 61.2 Aug (P) 60.0*
18 August 1:00 pm: NAHB Housing Market Index – Aug Jun 18 Jul 16	19 August ABC/Washington Post Consumer Comfort Survey —(week ending 8/16/08) LJR Redbook —(week ending 8/15/08) 8:30 am: PPI – Jul May 1.4% Jun 1.8% 8:30 am: Core PPI – Jul May 0.2% Jun 0.2% 8:30 am: Housing Starts – Jul May 0.977mn Jun 1.066mn 8:30 am: Building Permits – Jul May 0.978mn Jun 1.138mn	20 August MBA Mortgage Applications —(week ending 8/15/08)	21 August 8:30 am: Initial Jobless Claims —(week ending 8/16/08) 10:00 am: Philly Fed – Aug Jun -17.1 Jul -16.3 10:00 am: Leading Indicators – Jul May -0.2% Jun -0.1%	22 August
*Projections—subject to revision as additional data become available during the month. (R) denotes reopening.				

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