The Market Economist

Economic Analysis

Economics | United States
08 August 2008

Weekly guidebook for the global investor

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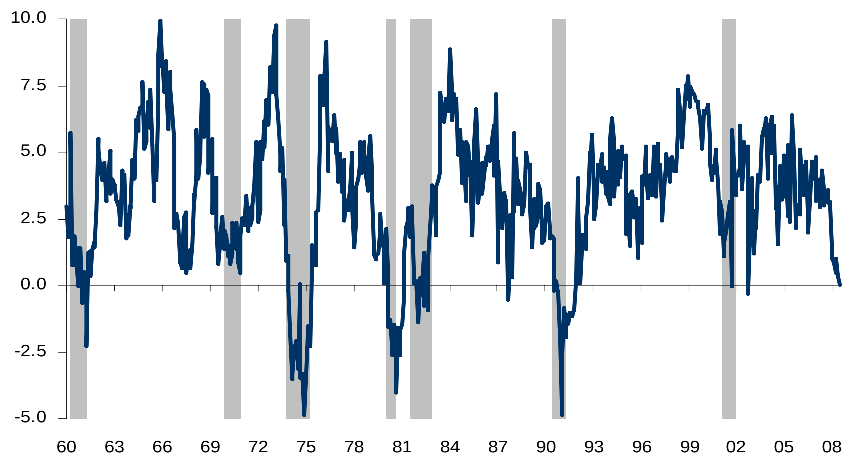
Macro viewpoint: Take it easy

As expected, the FOMC decided to leave rates unchanged at 2% its Tuesday meeting. Additionally, the FOMC also upgraded its growth risk assessment. In so doing, it moved the statement back from the tightening bias it had switched to in June to the neutral bias that had prevailed in April. With oil now officially in a "bear" market, easing concerns about inflation, the four-week average of claims at a 5-year high signaling a still-deteriorating labor market and credit conditions still tight, we think it likely we will see the return of an easing bias later this year as growth risks are realized and inflation risks fade.

The week ahead: Lots of data, most of it bad

Another busy week ahead, with the CPI, retail sales and trade reports in addition to releases on manufacturing and the Senior Loan Officer Survey for July. On the inflation front, food and energy price gains will again play a big role in the CPI figures for July, boosting the headline. However, we believe that the peak in inflation is near and that the slowdown in consumer spending will take hold, easing pressure. The two consumer indicators this week -- retail sales and initial unemployment claims -- are poised to disappoint.

Consumer spending on durables and semi-durables straddles the zero-line
(year-over-year % change)



Shaded region represents period of US recession
Source: Bureau of Economic Analysis, Merrill Lynch

Table of contents

Recent publications

Ozzie and Harriet, 7 August 2008

The Fed does a 180, 5 August 2008

The frugal future, 4 August 2008

Refer to important disclosures on page 14.

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Macro viewpoint

Take it easy

Shifting to neutral

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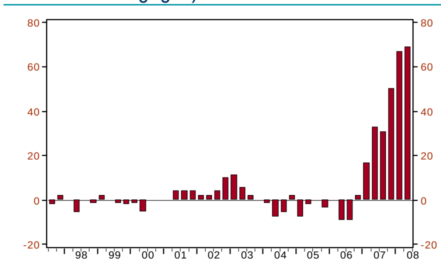
Misery loves company

The Federal Reserve was not alone in making a policy decision this week. Although both the Fed and the ECB seemed to increase their level of concern regarding growth risks, it is Merrill’s view that these two banks remain on divergent policy paths as they follow their distinct policy mandates. We expect the Federal Reserve will keep rates on hold at 2% through year end as the FOMC anticipates lower inflation in the medium-term and continues to attempt to revive a stalled financial system and, with it, an economy. In contrast, despite a weakening growth outlook, we continue to expect the ECB to raise rates. We look for the ECB to hike by 25 basis points later this year as the ECB maintains its focus on its sole policy mandate: inflation. Elsewhere in the G7, Merrill looks for both the Bank of England and the Bank of Canada to reduce rates by 25 basis points in the fourth quarter of this year. We anticipate these moves will be followed by further easing from the Fed in the first quarter of 2009.

Chart 1: Tightest lending standards on record
(Net share of banks tightening standards on residential mortgages)



Source: Federal Reserve Board, Haver Analytics, Merrill Lynch

Tight to tighter credit conditions?

In its statement, the FOMC noted “tight credit conditions” as likely to “weigh on economic growth.” Next week should see the release of the Federal Reserve’s Senior Loan Officer Survey for July. It seems likely given trends in commercial bank balance sheets that this survey will show banks are still unwilling to lend to either consumers or businesses regardless of credit risk. Indeed, the reason this survey may not get that much worse is that, beyond a certain point, further tightening of lending standards becomes quite difficult for banks to accomplish. A further tightening of credit conditions, in conjunction with a weakening labor market and falling asset prices is likely to further hamstring an already stressed US consumer.

The consumer could write off the rest of 2008

Indeed, despite the tax rebate program, July’s personal income and consumption report showed that real consumption dropped during the month. This suggests that consumer spending in the third quarter is likely to weaken significantly and could fall into negative territory for the first time since 1991. We expect this rebate-driven hangover will continue into the fourth quarter and linger into the first quarter of 2009. If these forecasts are realized, this would mark the first time in the history of the Gross Domestic Product series (dating back to 1947) that the US experienced three consecutive quarters of negative personal consumption growth. Against a backdrop of falling inflation, this outcome would certainly open the door to additional Fed easing if, in easing, they felt they could nudge banks toward increasing lending through a steeper yield curve and, as a result, could stimulate consumer spending and/or the housing market.

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Key market movers

The week ahead: Lots of data, most of it bad

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Faltering consumer starting to become more apparent

In our view, the next leg down in the economy will come from the consumer. Our forecast calls for real spending to turn negative by 3Q, pulling the overall economy into a recession through the middle of next year. The upcoming data on the consumer is likely to show more obvious signs of this impending slowdown. Retail sales in July are expected to disappoint at 0.1% month-over-month despite a cumulative $106 billion of stimulus checks in hand by mid-month. The recent surge in consumer credit figures in June implies that more people are turning to credit cards to cover spending on basic goods. Such strains on consumer finances will likely be reflected in the University of Michigan survey of consumer sentiment, which we expect to fall in early August. The recently higher trend in unemployment claims will continue this week. We see initial claims in early August at 440K, suggesting steeper declines in payrolls in upcoming months.

Declines in manufacturing reports abound

This week we will get two new data points on manufacturing: Industrial production and the NY Empire survey. Both are expected to show a contraction of activity. July data on production is expected to post a decline of 0.5% over the month, taking the YoY reading into negative territory. Manufacturing production, also seen falling 0.5% M/M, is set to show its fourth YoY decline. We will also get our first glance at August data with Friday’s release of the Empire state manufacturing survey. We expect a modest improvement, but for it to continue to suggest a contraction in activity.

Tight credit conditions likely to be confirmed

The Federal Reserve's Senior Loan Officer Survey for July will be released early next week (likely Monday). This report has shown that banks dramatically tightened their lending standards for all borrowers across all kinds of products over the past year. It seems likely that July's report will show continued tight credit across the spectrum of clients and products even if, simply by the weight of previous tightening to date, the actual percentage of banks tightening standards this quarter relative to last declines. Nevertheless, both the data on the supply and demand for loans will prove of great interest as we have watched the growth in bank balance sheets come to a halt over the last few months. Additionally, the report should provide a good opportunity to contrast the credit crunch in the US relative to the Eurozone as the ECB released its bank lending survey for the quarter on Friday, 8 August.

Tuesday, 12 August

International Trade, June—8:30am

	Exp	Cons	Range	History
Trade Deficit	-$65.7bn	-$61.9bn	-$65.7 to -59bn	May = -$59.8bn vs. Apr = -$60.5bn

Source: Merrill Lynch, Bloomberg

We estimate that the trade balance will widen substantially in June to -$65.7B from -$59.8B in May. Consensus figures currently stand at -$61.5B. Imports are seen rising 3.1% over the month with higher prices, playing an important role in June. Several categories are expected to rebound from May, in particular energy goods. Energy imports are expected to rise 10% MoM on increases in both volumes and prices. Auto imports are also expected to rise following a decline in May. Several port officials made note of increased import volumes for smaller cars and hybrids, which are in relatively strong demand in the US. Also noted were higher import volumes in general during the month, as firms were wary of potential shutdowns related to the latest round of negotiations with the West Coast longshore workers contracts. On the export side, we expect a monthly decline in volumes which should be offset by price gains yielding a nominal MoM gain. Transports are seen producing a significant drag on auto and aircraft exports, evidenced by a 15% MoM decline in motor vehicle railcar loadings and softer foreign aircraft deliveries by Boeing. Though the trade data tend to be volatile from month-to-month, the underlying YoY trends in trade will continue be a story in June; real goods imports are expected to decline 2.4% while real goods exports are seen up 8.2%.

Monthly Budget Statement, July—2:00pm

	Exp	Cons	Range	History
Treasury Statement	-$100bn	-$87.0bn	-$105 to -$47bn	July 2007 = $36.4bn

Source: Merrill Lynch, Bloomberg

The budget deficit for July is likely to be $100 billion versus a deficit of just $36 billion recorded for the same month in 2007. Fiscal year to date July's deficit suggests a $367 billion deficit, $210 billion worse than the same period in FY2007. However, a significant portion of the deterioration this month relative to last year was driven by the payment of tax rebates and a calendar effect which pushed entitlement payments into July from August in FY2007. Interestingly, some of the deterioration was also caused by disbursements from the FDIC. These are estimated at $15 billion. This suggests our FY2008 deficit is likely to reach $440 billion versus our previous estimate of $425 billion.

Wednesday, 13 August

Import Prices, July—8:30am

	Exp	Cons	Range	History
Import Prices	1.1%	1.0%	0.4 – 2.0%	Jun = 2.6% vs. May = 2.6%

Source: Merrill Lynch, Bloomberg

Import prices are expected to rise 1.1% over the month in July, led by a strong 5.9% gain in petroleum prices. Industrial materials (which include energy) are seen rising by around 2%, as a decline in metal prices offsets some of the energy gains. Our model for food prices suggests a gain of just 1% in July following four months of consecutive gains in excess of 2.5%. Other import prices, namely for consumer and capital goods, will likely remain modest, rising 0.4% and 0.2%, respectively. On a year-over-year basis total import prices are expected to remain elevated, up 20% in July, reflecting the weaker US$ and the resulting higher costs of imported goods.

Retail Sales, July—8:30am

	Exp	Cons	Range	History
Retail Sales	0.1%	-0.1%	-0.6 to 0.7%	Jun = 0.1% vs. May = 0.8%
Retail Sales ex Autos	0.8%	0.5%	-0.2 to 1.0%	Jun = 0.8% vs. May = 1.2%

Source: Merrill Lynch, Bloomberg

Retail sales will probably rise 0.1% MoM in July following an equally soft 0.1% gain in June. Despite the cumulative delivery of $106bln in stimulus check rebates through mid-July, consumers are have begun to show clearer signs of financial stress, supportive of our below consensus forecast for July. Consumer credit figures in June -- a month which included the delivery of $32bln in net rebate checks -- showed a marked gain in both revolving and non-revolving debt. This corresponded with a light monthly retail sales gain and suggests that July sales will follow suit. Recently reported chain store sales for the month revealed that most spending gains over the month were concentrated among discounters, as consumers also struggled with expensive gasoline (on average $4.12/gallon). As a result, gas station sales are poised to rise 1.8% MoM in the months' report. We also expect to see gains for food and health care, reflecting spending channeled mostly to basic goods. Another area expected to rise are sales at electronics/appliance stores, as stronger sales were cited within several of the weekly chain store sales reports over the month. Auto sales, which fell to new lows in July last seen in early 1993, are expected to be a significant drag, falling 3.1% MoM. Ex auto sales are seen rising 0.8%MoM, while sales ex autos, gas and building materials are set to rise by 0.7% MoM.

Business Inventories, June—10:00am

	Exp	Cons	Range	History
Business Inventories	0.7%	0.5%	0.3 – 0.8%	May = 0.4% vs. April = 0.5%

Source: Merrill Lynch, Bloomberg

Business inventories probably rose by 0.7% MoM in June following a gain of 0.4% in May. Already released data on manufacturing and wholesales inventories showed gains of 1.0% and 1.1% over the month, respectively. Higher prices played an import role in both the manufacturing and wholesale gains, as energy, food and metal inventories all rose in-step with coincident gains in the underlying commodities. The one missing component ahead of this report is retail inventories, which are seen rising by a much more modest 0.1% in June. Auto inventories are expected to drop 1.0% MoM, as production related shutdowns (related to the auto parts strike through the end of May) overwhelmed a sharp decline in auto sales. Outside of autos, retail stocks are forecast to rise 0.6%.

Thursday, 14 August

Initial Jobless Claims, week ending 08/09/08—8:30am

	Exp	Cons	Range	History
Initial Claims	440k	432k	400 – 465k	Aug 2nd = 455k

Source: Merrill Lynch, Bloomberg

Initial claims for unemployment benefits in the week ending August 9th are expected fall by 15K over the week to 440K. This implies a trailing 3-week average of 448K and an accelerated deterioration in the labor markets relative to May and June. The trailing 4-week average, at 437K, remains slightly depressed from the artificially low claims we saw in July. The July claims were the result of overly aggressive seasonal adjustments by the Department of Labor, related to auto retooling shutdowns. The DOL continues to assert that the recent initial claims data have been influenced higher by the UI extension bill passed by Bush at the end of June, which extended benefits for those unemployed beginning July 1st. We do not believe this to be a significant factor. However, those filing for benefits are showing up in the continuing claims data -- as they should -- which have risen by 108K from the end of June to 3.3 million, the highest level since end-2003. We expect that claims, both and initial and continuing, will remain near these higher levels in upcoming reports.

Consumer Prices, July—8:30am

	Exp	Cons	Range	History
CPI	0.5%	0.4%	0.1 – 0.6%	Jun = 1.1% vs. May = 0.6%
Core CPI	0.2%	0.2%	0.1 – 0.3%	Jun = 0.3% vs. May = 0.2%

Source: Merrill Lynch, Bloomberg

Consumer prices are expected to rise 0.5% MoM in July following a 1.1% increase in June. On a year-over-year basis, this implies a 5.2% pace in July from 4.9% in June. Both food and energy prices are poised to play another big role in July, with monthly gains of 0.6% and 2.6%, respectively. On the energy side, gasoline and natural gas prices are set to contribute the strongest monthly gains in July. Excluding food and energy, core CPI is seen rising 0.25% MoM, holding the year-over-year rate at 2.4% in July versus June. Owners equivalent rent, which accounts for 31% of core CPI, is expected to post a more moderate gain of 0.2% MoM after the 0.3% figure we saw in June. In aggregate, core goods prices (whose largest weights include autos and apparel) are seen posting a flat reading in July, while core services is expected to rise 0.4% with gains from medical care and airfares. Over the next couple of months, we expect to see continued pressure from food and energy prices, driving the headline rate towards a peak of near 6% in year-over-year terms. Some additional pass-through into core prices are also expected, suggesting a peak YoY rate of 2.6% by year-end. Thereafter, and perhaps by this fall in the case of headline CPI, we believe that inflation will retreat as the headwinds faced by the consumer take hold, leading to declines in consumer spending. Furthermore, if we do see a sustained decline in energy prices, the yearly comparisons will also work in favor of the headline rate.

Friday, 15 August

Empire Manufacturing Index, August—8:30am

	Exp	Cons	Range	History
Empire Manufacturing	-1.0	-4.5	-10 to 5.6	Jul = -4.9 vs. Jun = -8.7

Source: Merrill Lynch, Bloomberg

The New York Empire manufacturing index likely rose to -1.0 in August from -4.9 in July. Activity was thought to have improved in July, with new orders and shipments both firmly in positive territory. This district's manufacturing sector is strongly influenced by the technology space, which showed little shift in the month – the S&P 500 information technology index up about 1% month-to-date, while orders for computers and electronic products are nearly flat on a three-month annualized basis. Previously, the region benefited to some degree from a weaker USD and resilient global economic backdrop, though most recent data suggest this also may also be waning. We continue to see this index remaining in negative territory, given the New York Fed's Beige Book said manufacturers were seeing weaker sales since the prior month, with employment in particular bearing the brunt of the softening economic environment. Indeed, employment and inventory indexes in July suggested that businesses are reducing costs elsewhere to cope with higher input prices. Prices paid and received both hit all-time highs in the eight-year history of the series, but should see some easing in line with softer commodity prices.

Net Foreign Purchases of US Longer-term Securities, June—9:00am

	Exp	Cons	Range	History
TIC Data	$60.0bn	$50.0bn	$30bn to $70bn	May = $67.0bn vs. Apr = $111.0bn

Source: Merrill Lynch, Bloomberg

Net foreign purchases of US long-term securities likely rose $60bn in June, following two strong prints. Federal Reserve custody data showed a somewhat larger $41.4bn increase (relative to May) in government and agency securities held for foreign accounts, and the USD rose slightly on a trade-weighted basis. However, net equity flows could see some decline, in line with the very weak monthly performance that saw all three major exchanges post declines ranging from 8.6% to 10.2% in the month. On a longer term basis, TIC data could moderate somewhat, in line with the improving trade deficit. Going forward, purchases of Agency debt by foreign official sources, particularly Asian central banks, will bear watching, given the loss in confidence over solvency of GSEs in early July, and the Treasury's efforts later in the month to provide liquidity and allay investor concerns.

Industrial Production & Capacity Utilization, July—9:15am

	Exp	Cons	Range	History
Industrial Production	-0.5%	0.0%	-0.2 to 0.3%	Jun = 0.4% vs. May = -0.2%
Capacity Utilization	79.3%	79.8%	79.4 – 80.4%	Jun = 79.9% vs. May = 79.6%

Source: Merrill Lynch, Bloomberg

Industrial production is forecast to fall 0.5% MoM in July following a 0.5% gain in June. Utilities output, which tends to be volatile from month-to-month, is expected to drop 1.8% in July following a 2.1% monthly gain in June. Manufacturing production is seen falling 0.5% over the month despite a gain in autos. Our forecast for July would otherwise call for a decline in auto production, however, seasonal factors are seen boosting the monthly gain. In June, auto output rebounded 5.4% MoM following the resolution of the American Axle strike. Production of tech-related goods is expected to remain an area of strength with YoY gains averaging 26% YTD. Excluding tech, manufacturing output will probably drop 1.0% over the month reflecting the underlying weakness in production. We will have our eye on the manufacturing ex tech and autos figure for July, which we believe will be a truer indication of trends over the month. This measure has posted consecutive monthly declines over the past three months and shows accelerating momentum to the downside. On a year-over-year basis, output is expected to move into negative territory in July, while manufacturing output will post its fourth consecutive decline. Capacity utilization for overall industries is estimated to fall from 79.9% in June to 79.3% in July. The corresponding measure for manufacturing industries is seen ticking down slightly from 77.6% in June to 77.0% in July.

University of Michigan Index of Consumer Sentiment, August (P)—10:00am

	Exp	Cons	Range	History
Consumer Sentiment	60.0	62.0	57 to 67	Jul = 61.2 vs. Jun = 56.4

Source: Merrill Lynch, Bloomberg

The University of Michigan index of consumer sentiment looks set to weaken slightly to 60.0 in August after a jump to 61.2 in July. That rise was related largely to the oil price declines and stock market rally, both of which have continued in the two weeks since the July survey was completed. Retail gasoline prices have slipped to below $4 a gallon, the lowest since May. Equity markets have also been generally flat, after falling through the previous three months. Moreover, labor markets have been deteriorating, but much of the weakness has come through hours worked instead of huge layoffs. However, we maintain our below-consensus call, given the end to any stimulus check “euphoria”, coupled with fragile state of household sentiment, as reflected in the weekly ABC News confidence figures. The most recent week’s readings dropped back down to -49, from an average of -43 in July, and now stand at the lowest level since late May. We will also be closely watching the inflation expectations figures. The five- to ten-year forward expectations fell to 3.2% from 3.4%, coincident with the decline in oil prices, and we expect that the continued slide in energy prices will alleviate concerns to the upside.

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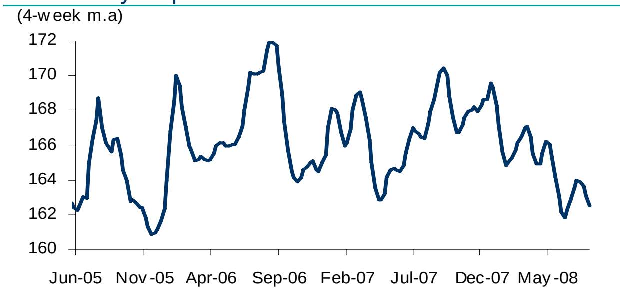
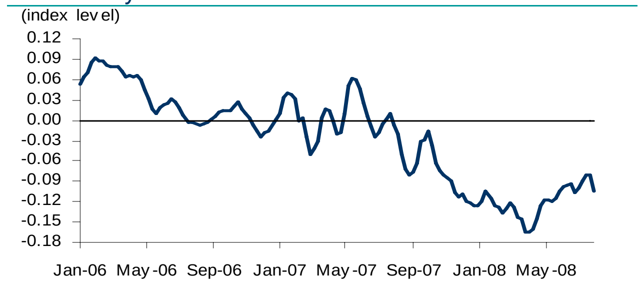
Merrill Lynch proprietary indicators

The Merrill Lynch production index



Our production index fell for the fourth consecutive week and indicates that industrial production remains soft. We continue to see declines in truck production, which is not surprising given that appetites in autos are changing rapidly. Truck production dropped a staggering 9.4% this week on top of a 6.2% slide the week before. Auto production was down as well, falling 0.4% – the fourth consecutive weekly decline. Railcar loadings were off as well, down 0.6% after rising for four weeks. Meanwhile, electrical production, which has the highest weight in our index, was flat for the week. We did see some components put upward pressure on our index. Coal production, rose 0.8%, matching last week's jump. Raw steel production was up 0.7% on top of a 0.3% increase last week. And, crude oil production rose 1% – the fourth jump in a row.

The Merrill Lynch consumer index

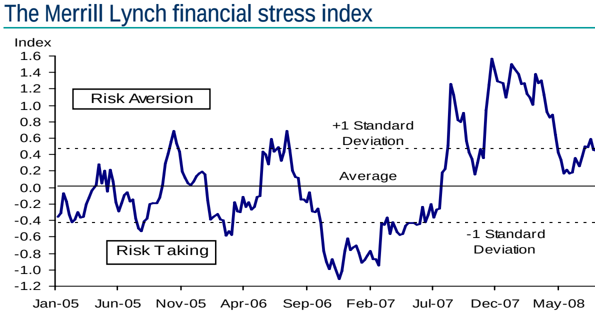


Our consumer index fell for the second consecutive week in a sign that the US consumer continues to weaken. The latest decline in the index was driven by the continued softening in labor markets. Initial jobless claims rose to the highest level since March 2002. Meanwhile, continuing claims rose for the second week in a row to their highest level since December 2003. With the labor market deteriorating, it is no surprise that consumer confidence continues to falter. Confidence dropped for the second consecutive week to its lowest level since May. Another variable weighing on confidence and our index, is crude oil prices, which despite the recent drop-off, remain elevated. Finally, consumers continue to see the value of their equity assets erode. The S&P 500 dropped in the latest week and remains below its two-year average.

The Merrill Lynch housing index

Our housing index dropped for the second time in three weeks. The index has spent over a year in negative territory, which is where it is likely to remain as the housing market continues to carve out a bottom. For starters, the labor market continues to weaken. Initial jobless claims rose for the fourth week in a row. Continuing claims continue to rise as well, indicating upward pressure on the unemployment rate in coming quarters. The MBAs' purchase index continues to run below its one-year average, indicating a pullback in the demand for housing. Commercial bank real estate loans are running below the levels of a year-ago as well. And, contract rates on conventional 30 year mortgage continue to rise, illustrating that the Fed's monetary stimulus has not gained traction.

The Merrill Lynch financial stress index



Our financial stress index rose in the latest week, entering risk aversion territory for the first time in three weeks. This continues to suggest that financial markets have not normalized. Two-year swap spreads rose in the latest week. Baa spreads rose for the second week in a row and are at their widest level since April. TED spreads were up as well. We did see signs of risk taking, however. The price of gold, for example, fell for the third consecutive week. The VIX index, a measure of equity market volatility, dropped for the fourth week in a row and is running below its one-year average. And, speaking of equity markets, we saw the S&P 500 outperform Treasuries in the latest week. Within the equity sectors, tech outperformed less risky consumer staples stocks.

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Debt issuance

Treasury financing (billions of $)

Announcement date	Auction date	Settlement date	Issue	Size	New cash
7-Aug	11-Aug	14-Aug	3-month	26	
7-Aug	11-Aug	14-Aug	6-month	25	
11-Aug	12-Aug	14-Aug	4-week	28*	(5)*
7-Aug	12-Aug	13-Aug	CMB (155 day)	26*	26*
14-Aug	18-Aug	21-Aug	3-month	24*	
14-Aug	18-Aug	21-Aug	6-month	23*	
18-Aug	19-Aug	21-Aug	4-week	20*	(8)*
21-Aug	25-Aug	28-Aug	3-month	20*	
21-Aug	25-Aug	28-Aug	6-month	19*	
25-Aug	26-Aug	28-Aug	4-week	26*	
21-Aug	26-Aug	28-Aug	1-year	16*	3
28-Aug	1-Sep	4-Sep	3-month	20*	
28-Aug	1-Sep	4-Sep	6-month	19*	
1-Sep	2-Sep	4-Sep	4-week	16*	(19)*
25-Aug	27-Aug	2-Sep	2-year	31*	
25-Aug	28-Aug	2-Sep	5-year	21*	30*

* 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 $)

Announcement date	Auction date	Settlement date	Issue	Size
11-Jul	14-Jul	15-Jul	FRE 3-month	
11-Jul	14-Jul	15-Jul	FRE 6-month	
14-Jul	16-Jul	17-Jul	FNM 3-month	
14-Jul	16-Jul	17-Jul	FNM 6-month	

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

Policy speakers

Key speaking engagements and news events*

Monday, August 11		*None scheduled at this point*
Tuesday, August 12		*None scheduled at this point*
Wednesday, Aug13		*None scheduled at this point*
Thursday, August 14	2:30 pm	Minneapolis Fed President Stern (voter) speaks on "Repercussions from the Financial Shock"
Friday, August 15	12:30 pm	Chicago Fed President Evans (non-voter) speaks on the US economic outlook

*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	2.1	0.6	-2.5	-2.3	-0.5	2.0	2.5	2.0	1.4	-0.5
% Change, Year Ago	2.3	2.5	1.9	0.8	0.3	-0.5	-1.2	-0.8	0.4			
Final Sales	0.8	0.9	3.8	-0.6	-2.4	-2.3	-0.1	1.4	2.5	2.4	1.6	-0.6
Domestic Demand	-0.1	0.1	1.3	-0.8	-2.4	-3.3	-0.8	1.1	2.3	1.8	0.4	-1.2
Consumer Spending	1.0	0.9	1.5	-0.5	-3.0	-2.4	0.0	1.8	2.5	2.8	0.8	-0.8
Durables	0.4	-4.3	-3.0	-6.7	-18.5	-10.0	0.5	2.5	3.5	4.8	-3.1	-6.7
Nondurables	0.3	-0.4	4.0	-2.0	-6.0	-3.5	-3.0	1.5	2.0	2.5	0.3	-2.3
Services	1.4	2.4	1.1	1.3	1.3	-0.5	1.3	1.8	2.5	2.6	1.7	1.0
Residential Investment	-27.0	-25.0	-15.6	-14.2	-20.2	-21.0	-7.9	4.4	5.1	-17.9	-20.8	-13.0
Nonresidential Investment	3.4	2.4	2.4	-2.7	-1.2	-12.3	-8.7	-5.5	1.6	4.9	2.9	-5.8
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	-3.3	-1.5	3.0	-13.0	-9.0	-5.8	2.0	1.7	0.3	-5.6
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	-56.0	-20.9	-24.1	-24.0	-34.8	-20.1	-21.2	-2.5	-27.8	-25.0
Nominal GDP (Bil $)	14031	14151	14257	14406	14449	14445	14447	14542	14669	13808	14315	14526
% SAAR	2.3	3.5	3.0	4.3	1.2	-0.1	0.1	2.7	3.6	4.8	3.7	1.5
% Change, Year Ago	4.9	4.7	3.8	3.3	3.0	2.1	1.3	0.9	1.5			
Key Indicators												
Industrial Production (% SAAR)	0.2	0.6	-3.2	-2.6	-7.2	-7.1	-2.7	0.9	1.5	1.7	-0.6	-4.0
Capacity Utilization (%)	81.0	80.6	79.8	78.9	77.1	75.4	74.6	74.4	74.4	81.0	79.1	74.7
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)	2.7	2.6	2.2	2.9	-0.7	0.4	2.5	3.1	2.5	1.4	0.5	2.4
% Change, Year Ago	3.3	4.2	3.3	2.6	1.7	1.2	1.3	1.3	2.1			
Real Disp. Personal Inc. (% SAAR)	0.6	-0.1	11.3	-4.1	-4.5	1.0	2.2	2.9	3.0	2.8	1.6	0.5
% Change, Year Ago	1.8	0.7	3.6	1.7	0.4	0.7	-1.4	0.3	2.3			
Personal Savings Rate (%)	0.4	0.3	2.6	1.3	1.0	1.3	1.9	2.3	2.7	0.6	1.3	2.1
Light Vehicle Sales (Millions SAAR)	16.0	15.3	14.2	12.8	12.8	12.8	13.5	13.8	14.0	16.4	13.7	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	-440	-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	8.0	4.0	1.5	-2.1	0.4	1.1	2.9	4.9	2.1
% Change, Year Ago	4.0	4.2	4.3	5.6	5.3	4.6	2.8	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

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	219.165	0.16	5.2	0.52	5.2	0.16	2.4	0.25	2.4
2008: Aug	219.212	0.02	5.4	0.22	5.4	0.27	2.5	0.26	2.5
2008: Sep	221.220	0.92	6.1	1.01	6.1	0.27	2.6	0.25	2.6
2008: Oct	221.008	-0.10	5.8	-0.05	5.8	0.37	2.6	0.23	2.6
2008: Nov	220.969	-0.02	5.1	0.28	5.1	0.00	2.6	0.19	2.6
2008: Dec	220.707	-0.12	5.1	0.30	5.1	-0.08	2.5	0.18	2.5
2009: Jan	221.179	0.21	4.8	0.11	4.8	0.23	2.4	0.18	2.4
2009: Feb	221.933	0.34	4.8	0.08	4.8	0.43	2.5	0.13	2.5
2009: Mar	222.456	0.24	4.2	-0.28	4.2	0.45	2.5	0.14	2.5

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$/Euro	1.50	1.51	1.48	1.42	1.40	1.38	1.33
Japanese Yen	¥/US$	110	103	102	100	98	98	98
	¥/Euro	166	156	151	142	137	135	130
British Pound	US$/£	1.92	1.91	1.87	1.82	1.82	1.82	1.75
	£/Euro	0.78	0.79	0.79	0.78	0.77	0.76	0.76
Swiss Franc	SF/US$	1.08	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$/US$	1.07	1.04	1.06	1.08	1.11	1.12	1.12
Australian $	US$/A$	0.89	0.91	0.84	0.80	0.74	0.72	0.70
Chinese Renminbi	RMB/US$	6.86	6.75	6.70	6.60	6.60	6.50	6.50
Hong Kong $	HK$/US$	7.81	7.75	7.75	7.75	7.75	7.75	7.75
Korean Won	KRW/US$	1028	1000	975	950	975	1000	1000
Singapore $	SGD/US$	1.41	1.33	1.32	1.32	1.32	1.32	1.33
Taiwan $	TWD/US$	31.27	30.25	30.00	30.25	30.50	30.75	31.00
Brazilian Real	BRL/US$	1.61	1.65	1.70	1.75	1.75	1.80	1.80
Mexican Peso	MXN/US$	10.13	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
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 .... 0.1%* 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 0.7%*	14 August 8:30 am: Initial Jobless Claims —(week ending 8/9/08) – 440k* 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 Apr .... $111.9bn May .... $67.0bn Jun .... $60.0bn* 9:15 am: Industrial Production May .... -0.2% Jun .... 0.5% Jul .... -0.5%* 9:15 am: Capacity Utilization May .... 79.6 Jun .... 79.9 Jul .... 79.3%* 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 Jun .... 18 Jul .... 16 Aug 17*	19 August ABC/Washington Post Consumer Comfort Survey —(week ending 8/16/08) LJR Redbook —(week ending 8/15/08) 8:30 am: PPI May .... 1.4% Jun .... 1.8% Jul .... 1.6%* 8:30 am: Core PPI May .... 0.2% Jun .... 0.2% Jul .... 0.2%* 8:30 am: Housing Starts May .... 0.977mn Jun .... 1.066mn Jul .... 0.920mn* 8:30 am: Building Permits May .... 0.978mn Jun .... 1.138mn Jul 0.930mn*	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 Jun .... -17.1 Jul .... -16.3 Aug .... -15.0* 10:00 am: Leading Indicators May .... -0.2% Jun .... -0.1% Jul .... -0.4%*	22 August
25 August 10:00 am: Existing Home Sales – Jul May .... 4.99mn Jun 4.86mn	26 August ABC/Washington Post Consumer Comfort Survey —(week ending 8/23/08) LJR Redbook —(week ending 8/22/08) 9:00 am: Case-Shiller Home Price Index (Composite 20) – Jun Apr .... 1.3% May .... -0.9% 10:00 am: Consumer Confidence – Aug Jun .... 51.0 Jul .... 51.9 10:00 am: OFHEO Home Price Index – 2Q 4Q .... 0.3% 1Q .... -0.2% 10:00 am: New Home Sales – Jul May .... 533k Jun .... 530k 2:00 pm: *Minutes from the August 5 FOMC Meeting Released*	20 August MBA Mortgage Applications —(week ending 8/22/08) 8:30 am: Durable Goods Orders – Jul May .... 0.1% Jun .... 0.8% 8:30 am: Durable Goods ex Transportation – Jul May .... -0.5% Jun 2.0%	21 August 8:30 am: Initial Jobless Claims —(week ending 8/23/08) 8:30 am: Real GDP – 2Q (P) 1Q .... 0.9% 2Q (A) .... 1.9% 8:30 am: GDP Price Index – 2Q (P) 1Q .... 2.6% 2Q (A) 1.1%	22 August 8:30 am: Personal Income – Jul May .... 1.8% Jun .... 0.1% 8:30 am: Personal Spending – Jul May .... 0.8% Jun .... 0.6% 8:30 am: Core PCE (YoY) – Jul May .... 2.2% Jun .... 2.3% 10:00 am: Chicago PMI – Aug Jun .... 49.6 Jul .... 50.8 10:00 am: University of Michigan Consumer Sentiment – Aug (F) Jun .... 56.4 Jul 61.2

*Projections—subject to revision as additional data become available during the month. (R) denotes reopening.

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